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Evaluation of Southeast Europe Enterprise Development

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Preface and acknowledgements

This report was prepared for Southeast Europe Enterprise Development (SEED) and the Operations Evaluation Group (OEG) of the International Finance Corporation (IFC) by Nexus Associates, Inc. – an economics and management consulting firm based in Belmont, Massachusetts, USA – in fulfillment of Contract # 7123799.

Nexus Associates and the other consultants involved in this evaluation worked under direct contract with IFC's Operations Evaluation Group (OEG), an independent unit that reports directly to IFC's Board of Directors through the Director General, Operations Evaluation, of the World Bank Group.

Linda Morra (Head of Studies, OEG) and Walter Cohn (Walter I. Cohn & Associates, LLC), who have been charged by OEG with responsibility for an overall evaluation of the IFC-managed project development facilities, developed the terms of reference, selected the consultants, provided supervision and guidance to them, and commented on all report drafts. SEED and the joint World Bank-IFC Small and Medium Enterprises Department, which has management responsibility for SEED, provided OEG with the bulk of the funding for the evaluation, commented on the terms of reference, the selection of consultants, and the draft reports, but were not in a position to circumscribe the consultants' independence or control the scope or execution of the assignment.

Members of the evaluation team included the following:

- Eric Oldsman, Ph.D. (Nexus Associates, Inc.). *Study Director*. Responsible for developing the study design, conducting field interviews in Bosnia and Herzegovina and Serbia, overseeing data collection and analyses, interacting with OEG, SEED and the SME Department, and drafting the final report.
- Adam Korobow, Ph.D. (Nexus Associates, Inc.) Responsible for supervising data collection efforts, compiling of SEED records, administering the client survey, conducting statistical analyses, interacting with SEED staff, and drafting elements of the report.
- Chris Green (SQW Ltd.). Responsible for conducting field interviews in Kosovo, Albania and FYR Macedonia.
- Michael Wenborn (ERM). Responsible for assessment of environmental and social issues.

In addition, Prism Research (Sarajevo) was retained to administer the survey designed by Nexus Associates.

After a two-month process involving a series of meetings with representatives of SEED, the SME Department, and OEG, the study design was finalized in January 2003. Field interviews were conducted in March and April 2003 with the broader survey effort ending in May 2003.

We would like to thank the staff of SEED and the SME Department for their assistance throughout the course of the study.

Abbreviations and Acronyms

AL	Albania
BAC	Business Environment Adjustment Credit
BDS	Business Development Services
BEE	Business Enabling Environment
BIDCO	Balkan Investment and Development Company
BiH	Bosnia and Herzegovina
BPK	Bank and Payments Authority of Kosovo
CAS	country assistance strategies
CB	Capacity Building (CB-SME or CB-BDS)
CFO	Chief Financial Officer
CIDA	Canadian International Development Agency
CIPE	Center for International Private Enterprise
CME	Canadian Manufacturers & Exporters
CN	Consultancy Network
DFID	Department for International Development (UK)
E&S	Environmental and Social
EAR	European Agency for Reconstruction
EBRD	European Bank for Reconstruction and Development
FBiH	Federation of Bosnia and Herzegovina
FIAS	Foreign Investment Advisory Service
FIPA	Foreign Investment Promotion Agency
FM	Financial Management
FMO	Netherlands Development Finance Company
FSVC	Financial Services Volunteer Corps
FTE	Full Time Equivalent
FY	Fiscal Year for SEED, beginning July 01 and ending on June 30.
FYRM	Former Yugoslavia Republic of Macedonia
GMDP	General Management Development Program
IBRD	International Bank for Reconstruction and Development
ICU	Interim Credit Unit
IEP	Internal Enhancement Plan
IFC	International Finance Corporation
IFI	International Finance Institutions
ILO	International Labor Organization
IP	Investment Plan
IS	Investment Services
KM	Konvertible Marka
MIER	Ministry of International Economic Relations
MIS	Management Information Systems
MOF	Ministry of Finance
NGO	Non-governmental Organizations
OEG	Operations Evaluation Group (IFC)
OHR	The Office of the High Representative
P & L	Profit and loss
PCN	Project Concept Note
PDF	Project Development Facility
PEP	Private Enterprise Partnership
PSD	Private Sector Development
PTMRS	Project Tracking and Management Reporting System
QIF	Quick Impact Facility
RJB	Raiffeisenbank Jugoslavija
RS	Republic of Srpska
SBU	Small Business Unit
SCG	Serbia and Montenegro
SEED	Southeast Europe Enterprise Development
SIDA	Swedish International Development Bank
SME	Small and Medium sized Enterprises
SPPF	South Pacific Project Development Facility
TA	Technical Assistance
US\$	United States dollars
WBS	Work Breakdown Structure

Executive Summary

Southeast Europe Enterprise Development (SEED) was established in January 2000 by the International Finance Corporation (IFC) and international donors “to help support the development of the private sector” in the Balkan Region. The facility is managed by the IFC and is sponsored by bilateral institutions from nine countries. In addition to the IFC, the other nine SEED sponsors are: Austria, Canada, Greece, the Netherlands, Norway, Slovenia, Sweden, Switzerland, and the United Kingdom.

The funding agreements between IFC and each of the donors required that a mid-term evaluation be carried out by an independent party. The required mid-term evaluation coincides with a broader study of IFC-managed Project Development Facilities being conducted by IFC’s Operations Evaluation Group (OEG). Thus, the evaluation of SEED serves three principal purposes:

- Satisfy donor requirements for an independent mid-term evaluation of SEED;
- Serve as an input into the OEG evaluation of IFC-managed Project Development Facilities; and
- Facilitate learning within each of the respective organizations and broader development community.

This report presents the principal findings and conclusions of an independent evaluation of SEED focusing on the period from its inception in the summer of 2000 through December 2002, and offers recommendations on needed actions.

Principal findings and conclusions

The original rationale for the establishment of SEED remains sound...

The private sector in each of the four countries (Bosnia and Herzegovina, Albania, Serbia and Montenegro, and Former Yugoslav Republic of Macedonia) faces significant hurdles resulting from years of war and economic sanctions, undeveloped markets, unfavorable laws and regulations, limited access to capital, and inadequate management skills of small and medium enterprise (SME) owners and managers. SEED was intended to help spur the development of the private sector by providing needed services directly to SMEs, building a sustainable local capacity to continue to meet the needs of SMEs in the future, and pushing for desired government reform. In so doing, SEED was intended to complement the activities of other bilateral and multilateral organizations that were active in the region.

The findings of this evaluation generally support the original rationale for the program and suggest that it remains valid. Survey results and interviews point to the limited availability of high-quality services at prices SMEs consider they can afford. They also highlight the reluctance of companies to pay for services given uncertainties with respect to potential benefits and high transactions costs. In light of these and other market imperfections, there is justification for SEED’s provision of subsidized services. Although SEED competes to some extent with private consultants, the evaluation did not find evidence to suggest SEED had crowded-out commercial suppliers of comparable services. Furthermore, the evaluation did not find evidence that SEED has duplicated efforts of other international organizations.

... however, the extent to which the organization can overcome constraints in financial markets may be limited.

The original rationale for the establishment of SEED highlighted the importance of financing to the growth of companies stating, “the major constraint faced by the SMEs is the lack of access to capital.” The availability of capital under acceptable terms is clearly an issue. Credit – particularly in the form of long-term loans – remains scarce and is accompanied by high collateral requirements. Thus, SEED’s ability to help SMEs secure needed capital is constrained by existing bank policy: firms that lack collateral cannot access debt finance even with a solid business plan. As a result, SEED has placed less emphasis on helping companies to secure financing and greater emphasis on improving

emphasis on helping companies to secure financing and greater emphasis on improving management capabilities of firms and upgrading business operations. The results of the evaluation support the decisions that SEED has made in this regard, however, the question of how best to address capital constraints remains open.

SEED has done a great deal in a relatively short period of time.

Since its inception in mid-2000, the organization has established offices in four countries, developed a highly professional staff, launched numerous initiatives, and established a good reputation among entrepreneurs, government officials and international donors. As envisioned, SEED has provided a wide range of services to assist individual SMEs; enhance the capabilities of local consulting firms, business associations, and local economic development organizations; and improve the business enabling environment.

Most SMEs are satisfied with the services provided by SEED and perceive value greater than or equal to fees paid.

An important determinant of success for any program is the degree of satisfaction among clients. In this regard, of the survey respondents who received investment services (IS), roughly 71 percent (17 of 25) of Internal Enhancement Plan (IEP) clients and 67 percent (10 of 15) of Investment Plan (IP) clients were satisfied with the services provided by SEED. Of companies that participated in training, 80 percent (70 of 87) report being satisfied with the services provided by SEED. Similarly, 75 percent of IS clients and 79 percent of training clients believe that the value that they derived from SEED services was equal to, or greater than, the fees charged by SEED.

Clients made changes in their businesses and reported improved performance ...

Approximately 82 percent IS clients and 88 percent of training clients reported making some change in their strategy or operations as a result of SEED services. As a result of these changes, 59 percent of IS clients and 46 percent of training clients reported at least one dimension of improved performance in areas such as product quality, capacity utilization, and on-time delivery.

... however, in most cases, these gains have yet to be reflected in higher sales, profit or employment.

However, only one-third of IS clients and 22 percent of training clients reported higher sales as a result of SEED services. In terms of net profits, the proportion of clients reporting gains was approximately 36 percent and 18 percent of IS clients and training clients, respectively. A few companies account for the bulk of aggregate gains in sales and employment. These results, of course, may improve as companies have more time to realize benefits from the steps taken based on SEED's efforts.

SEED has helped arrange approximately €2.5 million in debt and equity for ten companies...

SEED has completed Investment Plan projects with 20 companies. Ten of these firms were able to secure some or all of the financing needed for planned investments. Eight of the companies have already completed or plan to complete investment projects within the next year, representing a total investment of €9.5 million.

Some of the companies that were not able to secure financing pointed to high collateral requirements as the principal constraint.

... but half believe that SEED did not play an essential role.

Four of the companies that received financing believe that they could have done so on their own. Five of the firms that received financing believe they would have gone ahead with their respective projects without SEED's assistance.

SEED has enhanced the capacity of local consultants, business

One objective of SEED has been to encourage local consulting firms to develop and deliver new services aimed at SMEs. Consultants indicate that they have changed certain aspects of their business as a result of interactions with SEED. Roughly, 63 percent (26 of 41) of consultants responding to the survey report using what they learned from SEED with clients. While the market for services may expand in the future, thus far,

associations, and local economic development organizations, however, the impact on SMEs appears limited so far.

consultants have typically used the content and techniques obtained from SEED with three or fewer of their clients. The unwillingness or inability of SMEs to pay prevailing rates for services may have limited consultants' ability to apply what they learned from SEED more widely. SEED, however, may be lessening this constraint: 43 percent of the responding SMEs indicated that they were more likely to use private consulting services, training services, or both as a result of their interactions with SEED.

SEED has worked with a number of business associations in the region since late 2000. After initial efforts met with little result, SEED launched a new initiative in the fall of 2002 that has already met with some success. SEED has helped six associations develop strategic plans, define member services, and increase their membership. With one noted exception, associations have not yet assumed a strong advocacy role. The political process is fluid and some associations do not want to assume this role until they establish a stronger membership base. Moreover, the sustainability of some associations is questionable given weak financial situations.

In the two municipalities where SEED has been working since March 2002 to develop strategies to promote SMEs and foster economic growth, community members indicated they had learned a great deal about analytical methods and participatory planning processes. Both communities have drafted preliminary strategies and begun to refine plans for specific projects. The sources of funding, however, were not clear, and the municipalities were looking to SEED for help with international donors. SEED recently reported the first concrete results—the opening of a one-stop-shop development agency in October 2003.

SEED has contributed to specific reforms aimed at enhancing the business environment, but it is too early to see any impact on SMEs.

SEED's efforts at legal and regulatory reform have contributed to changes in specific laws and regulations, particularly with respect to leasing. But the impact on SMEs will not be felt until leasing companies are established, particularly firms that focus on equipment, rather than consumer goods. SEED has participated in policy discussions, taken steps to foster greater dialogue on the needs of SMEs, and contributed to the formulation of the World Bank's Business Environment Adjustment Credit in Bosnia. It is too early, however, to assess the impact of these efforts.

While it is too early to judge the overall efficiency of SEED, some activities are more cost-effective than others.

In many respects, it is too early to judge whether the monies invested in SEED have been well spent – there is an inherent mismatch in the timing of costs and benefits; while a significant share of costs are front-loaded, many of the outcomes that SEED is attempting to achieve are best considered over a longer horizon.

Through 31 December 2002, SEED had expenditures of US\$12.6 million. According to SEED records, SEED had allocated a total of US\$5.8 million to Investment Services (27 percent), Capacity Building – SME (22 percent), Capacity Building – BDS (37 percent), and Business Enabling Environment (14 percent). The remaining funds have been allocated to start-up and ongoing general management and administrative expenses.

As far as enterprise-level services are concerned, the evaluation suggests that the management consulting services provided by SEED to SMEs are relatively more cost-effective than efforts to help companies secure financing or improve firm performance through training.

Within CB-BDS, SEED has spent upwards of \$2.6 million on efforts to promote local consultants when direct project expenses, indirect program expenses, and allocated SEED overhead are taken into account. The cost-effectiveness of these activities can be called into question. Based on responses to the survey, interviews with consultants and discussions with SEED staff, it is hard to conclude that results – in terms of developing

local consultants that can provide high quality services to a significant number of SMEs – have been commensurate with this level of investment. At the time of the evaluation, SEED was taking steps to adopt a new approach to working with service providers to establish ongoing training programs for SMEs.

As noted above, given the time required for reforms to have an impact on SMEs, it is too early to gauge the cost-effectiveness of activities in the business enabling environment.

Given its current cost structure, the services offered by SEED are not commercially viable.

While the organization has charged for some of its services, it was never intended that SEED recover the full costs of its operations from client-paid fees. As originally designed, SEED was expected to generate roughly seven percent of its total operating budget through fees over its five year life. It was anticipated that these fees would be derived primarily through enterprise-level services. As of the end of December 2002, SEED client-paid fees have amounted to 1.5 percent of its operating budget.

Services offered under CB-BDS and BEE are not expected to be commercially viable. However, the potential for offering services to companies on a commercial basis is being actively considered.

Commercial viability means that an organization obtains revenue from the sale of services sufficient to cover *total* costs. While cost recovery has increased, SEED is still far from generating sufficient fees to cover the *direct project expenses* associated with IS and CB-SME services. When indirect program expenses and allocated overhead are included, the gap increases significantly. In the first two quarters of FY03, client-paid fees represented 13.6 percent and 4.3 percent of total IS and CB-SME expenditures respectively. For the current services to be commercially viable, SEED would need to reduce costs and/or increase prices dramatically without a significant decrease in the volume of business. However, given that the majority of clients state that the value of SEED services is equivalent to fees charged, the prospects of being able to raise prices without experiencing a drop in demand is unlikely. From a cost perspective, SEED would need to reduce *direct project expenses* while still providing the same quality of services. It would *also* need to take steps to reduce the fixed cost of operations beyond the 14 percent attributed to being part of the IFC structure.

This is not to say that it is impossible for SEED staff to leave the organization and establish commercially viable consulting firms based on know-how and materials developed under the auspices of SEED. These spin-off firms would need to redefine services based on their own expertise, establish lower cost operations, and adopt an appropriate pricing strategy. It is unlikely that a commercial venture based on brokering the services of third-party experts can be viable without support from international donors.

Recommendations

Donors should explicitly state whether they intend to continue funding SEED beyond FY05.

Donors' commitments are based on the originally planned five-year life of SEED, which ends in FY05. The organization has funding in place for the next two years; however, it is not clear what donors expect to happen beyond this point. Uncertainty with respect to future funding places the organization in a difficult position. For example, without a clear commitment of ongoing support, staff are likely to begin to seek alternative employment. Furthermore, companies and organizations may be unwilling to invest in building partnerships with SEED not knowing whether SEED will be in existence two years from now. As a result, the ability of SEED to achieve its objectives over the next two years may be compromised.

As noted above, the original rationale for SEED still applies – there are still numerous constraints to the development of a thriving private sector in all four countries. As such, donors should address the prospects for continued support and any conditions under

which such support would be provided. They should also address issues related to potential commercial spin-offs.

SEED should define its objectives with respect to spinning-off commercial ventures and formulate an explicit strategy.

One of the goals of SEED has been to “leave a legacy of sustainable consultant and training capacity” in the region. SEED management (and the SME Department) have interpreted “capacity” to include members of SEED staff as well as local firms. SEED has expected that staff would gain sufficient skills and experience to enable them to find ready employment with other firms or start their own companies at the end of SEED’s five-year life.

There is no expectation that SEED, as an institution, will become a commercial enterprise. SEED recognizes that its mission, particularly as it relates to strengthening the business enabling environment, requires ongoing donor support. However, SEED management has indicated that it expects that some staff will establish commercial enterprises based on the know-how and methods obtained during their employ at SEED.

There are numerous issues that need to be resolved to ensure that SEED continues to focus on meeting its primary mission over the next two years, while paving the way for staff to establish new commercial ventures. SEED should clarify objectives and strategies with respect to commercial spin-offs as soon as possible.¹ In so doing, SEED needs to consider how to deal with the following: create incentives for staff to remain at SEED over the next two years and/or begin to phase out certain services in an orderly manner; resolve the tension between the use of local consultants as a means of building local capacity and the interest of staff to develop their own viable businesses; develop policies with respect to the ownership of the SEED “brand” and other tangible and intangible assets owned by IFC/SEED; and help staff build capabilities based on functional and/or domain expertise, gain experience managing a commercial enterprise, and develop business plans for proposed commercial ventures based on sound market research.

SEED should focus its efforts on a narrower set of activities and provide more intensive services to clients.

SEED has evolved a great deal since its inception in light of actual experience, and continues to refine its role within the mandate given to it by IFC and other donors. The organization recognizes that there is a need to focus efforts and has already taken steps to reduce the scope of its activities. As part of its ongoing strategic planning process, SEED should take into account the following recommendations:

- Place an even greater emphasis on the provision of management consulting services to SMEs, rather than attempting to help companies to secure financing.
- Develop SME training programs that address critical issues within companies based on a thorough analysis of IEP projects.
- Reduce the level of expenditures allocated to broad based efforts to develop local private consultants, and shift resources to using local consultants on SEED client projects in order to provide greater opportunities for on-the-job training as part of more intensive interactions.
- Continue intensive work with selected business associations that offer significant promise, concentrating on efforts to ensure that they expand membership, institute needed members services, and establish a sound financial footing.
- Focus on specific government reforms that have a direct bearing on the performance of SMEs, working with other international donors to ensure that reforms are well-conceived, adopted by legislative and regulatory bodies, implemented within relevant institutions, and carried out in a way that meets the needs of SMEs.
- Consider what role, if any, the organization can play in reducing capital constraints

¹ In June 2000, SEED staff made a related presentation to SEED donors.

faced by SMEs given high collateral requirements.

SEED should consider reorganizing its operations based on countries and practices.

SEED should consider adopting a matrix management structure built around countries and practices. The latter could be defined by type of client (e.g., private business, government, or international donor) or product (e.g., strategic planning, market research, or information system). Matrix management would help promote cross-practice interactions within countries based on country-specific objectives, while also enabling staff to be part of peer groups with shared responsibility for accomplishing objectives related to particular practices.

SEED should reconsider its pricing policy, beginning with a clear articulation of objectives.

SEED operates much like any other private company, competing on the basis of quality and price. However, unlike a for-profit firm, the organization also has explicit development objectives. Before setting prices, SEED should specify the objectives of its pricing policy. These objectives could include one or more of the following: maximizing the use of the service among customers in the target population, recovering the costs of providing the service, exerting downward pressure on prevailing market prices for the service, or maximizing profits.

With objectives defined, SEED should take steps to determine the specific prices for particular services. As part of this process, it needs to consider how customers are likely to respond to different prices, prices charged by other organizations for similar services, and its own cost structure. In addition, the organization should tighten up its policies with respect to what it charges particular companies for services. The magnitude of the subsidy extended to particular firms should be made transparent so that companies will understand the true cost of service delivery.

SEED should continue efforts to strengthen information systems.

SEED has taken significant steps to develop its own information systems to supplement those provided by the SME Department. These efforts should continue. Cost accounting should be a fundamental part of financial management, complementing traditional financial accounting systems.

I. Introduction

Overview

1. Southeast Europe Enterprise Development (SEED) was established in January 2000 by the International Finance Corporation (IFC) and international donors “to help support the development of the private sector” in the Balkan Region.² The facility is managed by the IFC and is sponsored by bilateral institutions from nine countries.³
2. After several months of planning, SEED began operating during the summer of 2000 and officially opened its doors for business in September 2000. SEED initially focused on Albania, Bosnia and Herzegovina (BiH), Former Yugoslav Republic of Macedonia (FYRM) and Kosovo. It subsequently expanded its reach in mid-2001 to the Federal Republic of Yugoslavia, now called Serbia and Montenegro (SCG). SEED is headquartered in Sarajevo, and maintains offices in Tirana, Banja Luka, Belgrade, and Skopje.⁴
3. The organization provides a range of services that are intended to promote the development of individual businesses, strengthen providers of business services, and enhance the environment in which businesses operate in the region.
4. At the time SEED was established, IFC projected operating expenditures of \$36 million over the planned five-year life of the facility.⁵ After allowing for expected fee income of \$2.4 million, net funding requirements for five years were estimated at \$33.6 million. SEED has received commitments of roughly \$25 million from various donors and has used this figure for budgeting purposes.

Purpose of Study

5. The funding agreements between IFC and each of the donors required that a mid-term evaluation be carried out by an independent party. The required mid-term evaluation coincides with a broader study of IFC-managed Project Development Facilities being conducted by IFC’s Operations Evaluation Group (OEG). Thus, the evaluation of SEED serves three principal purposes:
 - Satisfy donor requirements for an independent mid-term evaluation of SEED;
 - Serve as an input into the OEG evaluation of IFC-managed Project Development Facilities; and
 - Facilitate learning within each of the respective organizations and broader development community.

² Originating IFC document.

³ In addition to the IFC, the other nine SEED sponsors are: Austria, Canada, Greece, the Netherlands, Norway, Slovenia, Sweden, Switzerland, and the United Kingdom.

⁴ SEED opened offices in FYRM in February 2001 and in Kosovo in March 2001. It is important to note that SEED was unable to operate in FYRM for roughly six months in 2001 due to open hostilities and associated travel restrictions

⁵ Originating IFC document.

6. This paper presents the principal findings and conclusions of an independent evaluation of SEED. It provides answers to a broad range of questions posed by stakeholders. Although there are numerous lines of inquiry, they can be summarized in the form of five basic questions: Was the original rationale for the establishment of SEED sound? Has SEED provided needed services to companies and institutions in the target population? Are the resources of SEED being used in an efficient manner? Has SEED been successful in achieving intended outcomes? Could particular elements of SEED's services be commercially viable in the future? The report offers recommendations concerning issues that SEED should address in the final two years of its funding cycle.

Methodology

7. The evaluation is based on both quantitative and qualitative methods, drawing on numerous sources of information:⁶
 - **Program documents.** The evaluation team reviewed a number of documents related to SEED, including initial IFC background research on SME activity in the Balkans; various originating IFC documents the SEED Business and Implementation Plan; annual reports and action plans; assessments of various programs; and newsletters, brochures and other marketing materials.
 - **SEED records.** SEED was asked to provide financial and operating data, including information on staffing levels, allocation of staff time, number of consultants broken down by regional origin; direct project expenditures; lists of all projects in each strategic objective undertaken in the evaluation period, including information on services provided and financing arranged; and list of companies that had received training as well as information on relevant training courses.⁷
 - **Interviews with SEED and World Bank Group staff.** The evaluation team met with management and staff of SEED to discuss the evolution of the organization's strategy, programs, and operations over time. In addition, the team met with representatives of the World Bank Group to discuss the role of SEED, issues related to coordination and specific projects in which IFC had invested.
 - **Interviews with government officials and other organizations.** The team interviewed key government officials in Bosnia and Herzegovina, Serbia and Montenegro, Albania, and Macedonia to develop a better perspective of the governments' views of SEED and the role that it has played in the respective countries. In addition, interviews were conducted with business associations, as well as local representatives from the donor agencies. In a separate small-scale survey, donors were asked to render their views and perspectives on SEED's current and future role in the region.

⁶ The study design, including survey instruments and interview guides, is available upon request. A list of people interviewed as part of the evaluation is presented in Appendix G.

⁷ SEED cooperated fully with this effort and attempted to compile all data requested by the evaluation team. In some instances data were unavailable because of shortfalls in information systems. Specific problems with data are discussed in the relevant chapters and appendices.

- **Business client survey.** Companies that completed Investment Service projects and/or received training were the targets of a business client survey. Specifically, the survey was administered to all SMEs that completed an Internal Enhancement Plan (IEP) and/or Investment Plan (IP) project as of 30 September 2002, and a sample of companies that received training as of 30 September 2002. A total of 198 surveys (including 18 that were the subject of more in-depth interviews as discussed below) were completed by the SMEs that completed projects and/or received training (with an effective response rate of approximately 65 percent).⁸
 - **Consultant survey.** A survey was administered to all members of the Consultancy Network—a group of local consulting firms that have been selected by SEED to work with SEED staff on assignments for IS clients—as well as all other organizations that attended training on operating a consulting business or attended train-the-trainer courses through 30 September 2002.⁹ The survey instruments contained closed-ended questions related to firm characteristics, changes in business practices and performance, and the role of SEED. A total of 41 surveys were completed, representing an effective response rate of roughly 68 percent.
 - **In-depth interviews with owners and managers of client companies.** Senior members of the evaluation team visited 18 companies that had completed IS projects.¹⁰ These companies were drawn from two groups of firms – those that SEED staff believed had met project objectives and those that staff felt had fallen short of objectives. Prior to conducting the interviews, the evaluation team reviewed the project documents and other reports prepared by SEED. The interviews followed a standard protocol, which generally mirrored the survey but allowed for follow-up questions to probe for additional detail. The interviews typically lasted two to three hours and included an inspection of the facilities. The viability of the enterprises, the contributions made by SEED, and the clients' environmental and social performance were also explored in these visits.
8. IFC and other donors are particularly interested in determining whether SEED has been successful in improving the performance of SMEs. Estimated impacts are based on participant judgments, judgments by the senior evaluation team, and the results of various statistical analyses.
9. It is important to note that at the time the evaluation report was written, SEED had been in existence for three years. Moreover, its operations continue to evolve in light of changing conditions in the market and other factors. Keeping this in mind, it should be noted that the evaluation addresses activities and performance in the following periods:¹¹
- The assessment of firm-level impacts focuses on companies that completed IS projects and/or received training from the inception of SEED through 30 September 2002;

⁸ It is important to note that the results of both the business client and consultant survey could be biased by non-response. No conclusions can be reached with respect to the companies that either did not respond to the survey or were not surveyed at all due to insufficient contact records.

⁹ A discussion of the sampling strategy and response rates can be found in Appendix H.

¹⁰ An environmental and social consultant also visited seven companies that had received services during the study period.

¹¹ The evaluation focuses on major activities that were completed during the evaluation period. As such, some activities are not covered in this report such as training for financial institutions, the Balkan wild herbal forum, tourism development initiatives, and various studies undertaken by the organization.

- The analysis of operating and financial data covers the period from inception through 31 December 2002; and
- The assessment of SEED's overall strategy and specific role in fostering the development of business associations, local economic development organizations, and the overall business enabling environment covers the period from inception through 30 April 2003 (when all fieldwork was completed).

Organization of report

10. This report presents the principal findings, conclusions and recommendations of the evaluation. It is organized into nine sections. Following this introduction, Section II presents the rationale and role of SEED within the context of the economic conditions in each of the four countries which it serves. The report then turns to an assessment of the activities that SEED has undertaken with respect to investment services, capacity building for SMEs, capacity building for providers of business development services (BDS), and efforts to enhance the business enabling environment. These four strategic objectives are discussed in Sections 3, 4, 5 and 6, respectively. Section 7 discusses SEED's organizational issues, while Section 8 summarizes the major conclusions of the study. A series of recommendations are offered in Section 9.

II. Overview

Rationale

11. SEED's role and subsequent impact in the Balkans should be considered within the context of social and economic conditions in the four countries in which it operates. Recognizing that other organizations were already active in the region, SEED was intended to "complement ongoing and planned World Bank Group, and multilateral and bilateral financial and technical support activities" in the region.¹² Correspondingly, the organization was designed to help achieve a number of objectives set forth in the Stability Pact's *Strategy on Economic Reconstruction, Development and Cooperation*.¹³ Specifically, the Stability Pact highlights the need for "reforms in the economic environment, creation of liberal environment for trade, attracting foreign investments, and encouraging the growth of a private market based economy."¹⁴ Moreover, it underscores that "the stimulus to growth and investment, after a long period of relative stagnation, will come from the creation of new small businesses and foreign investment, from market expansion and from building an efficient public and private infrastructure."¹⁵ Achieving these objectives would involve addressing a "core constraint faced by SMEs in the region", namely the "lack of access to capital and a related limited capacity to efficiently utilize what current capital is available." Though there has been an increase in funding for SME development, a general lack of access to credit and other banking and financial services are still major constraints to SME growth in the region.¹⁶ Other than from international financial institutions (IFI) and targeted donor funded programs, SMEs access to bank-lending is minimal, and is typically associated with high collateral requirements and short-term maturities.¹⁷
12. As summarized below and illustrated in Table 1, SEED's function in the region is affected by the unique set of challenges that each of the four countries faces en route to economic and social reform:
 - **Albania.** Albania has made considerable progress in structural and institutional reforms since 1997, while restoring and maintaining macroeconomic stability.¹⁸ The composition of the Albanian economy starkly contrasts with the other SEED client-countries in that about 50 percent of Albania's economic output is accounted for by the agricultural sector, compared with less than 18 percent in the other SEED countries.

Albania's GDP grew at a rate of 6.5 percent in 2001. While the strong growth in the construction and services sectors and the rapid privatization of land have contributed to recent high growth rates, the large quantity of external assistance, and relatively high amount

¹³ Originating IFC document.

¹⁴ See "Working Table II: Economic Reconstruction, Development and Cooperation," in the *Stability Pact for South Eastern Europe*.

¹⁵ *Ibid.*

¹⁶ *Code of Best SME Finance Practices in South Eastern Europe*, Center for Economic Development, Washington DC, 2001.

¹⁷ See Elisabetta Falcetti, Peter Sanfrey, and Anita Taci; *Bridging the gaps? Private sector development, capital flows and the investment climate in south-eastern Europe*. The European Bank for Reconstruction and Development, Office of the Chief Economist, Working paper No. 80, June 2003. p.9.

¹⁸ See *Country Assistance Strategy: Albania*, The World Bank; South East Europe Country Unit, ECC04, Europe and Central Asia Region. Report No. 24189-ALB, May 28, 2002. p.3.

of workers' remittances (10-12 percent of GDP) have had a marked impact on growth as well.¹⁹

Notwithstanding recent progress in structural and institutional reform, Albania still suffers from "limited financial intermediation, a narrow export base, a relatively poor investment climate, and weak governance and administrative capacity" which hinders the development of SMEs.²⁰ Nonetheless, despite these weaknesses, Albania has, by some measures, exhibited a relatively higher degree of SME activity when compared to FYR Macedonia and Serbia and Montenegro. A European Bank for Reconstruction and Development (EBRD) study in 2000 showed that Albania had 16.5 SMEs per 1,000 inhabitants, whereas the same measure was 14 for FYR Macedonia, and eight for Serbia and Montenegro.²¹ Total domestic credit as a percent of GDP, a somewhat coarse indicator of the overall health of the banking and financial system, stood at 54.5 percent in 2001—higher than any of the other SEED client-countries.²²

- **Bosnia and Herzegovina.** Bosnia and Herzegovina (BiH) is facing the dual challenge of emerging from a devastating war and dealing with the remnants of socially planned economy. Though the creation of a currency board in August 1997 has assisted in both checking inflation and gaining universal acceptance of the Konvertible Marka (KM), larger scale domestic and foreign investment is unlikely to take place until investors develop confidence in the security of their investments and property rights systems are clarified.²³

Bosnia and Herzegovina's relatively high GDP growth rate in 2001 has, in large part, been maintained by a substantial influx of external assistance that is expected to diminish sharply in the next several years, further underscoring the need to attract foreign direct investment and build a vibrant domestic industrial base. Moreover, despite recent high GDP growth, GDP per capita remains at about half of its pre-war level.²⁴ Unofficial data suggest that 45-55 percent of the population live in poverty.²⁵ Moreover, average salaries in the Republic of Srpska (RS) are roughly 27 percent lower than in the Federation of Bosnia and Herzegovina (FbiH).²⁶

At the time of SEED's inception, credit and finance for SMEs in BiH was severely limited. Total domestic credit as a percent of GDP neared 32 percent in 2001.²⁷ An IFC-sponsored study in 2000 found that SME finance in Bosnia and Herzegovina is mainly in the form of credit lines administered by banks and that SMEs demand a further range of financing products.²⁸ Further findings indicated that loans between KM300,000 - KM500,000 were rare

¹⁹ *Ibid.*

²⁰ *Ibid.*

²¹ Data for Bosnia and Herzegovina were unavailable. In the study, SMEs were defined as an enterprise consisting of less than 250 employees. See Elisabetta Falcetti, Peter Sanfrey, and Anita Taci; *Bridging the gaps? Private sector development, capital flows and the investment climate in south-eastern Europe. op. cit.* p.4.

²² Nexus Associates calculation based on the International Monetary Fund's *International Financial Statistics*.

²³ *Bosnia and Herzegovina: Country Strategy Paper: 2002-2006*, European Commission; External Relations Directorate General, Directorate: Western Balkans, p.8.

²⁴ *Bosnia and Herzegovina: Country Strategy Paper: 2002-2006, op. cit.*, p.9.

²⁵ *Ibid.*

²⁶ FbiH and RS Statistical Offices. OHR Newsletter. Vol. 6, Issue 2, May 2003. p.12. In February of 2003 the average net salary in the country (BiH) was 426 KM—the Federation's average net salary was 512 KM, while in RS the average monthly salary level was 372 KM.

²⁷ Nexus Associates calculation based on the International Monetary Fund's *International Financial Statistics*.

²⁸ *IFC SME Financing Needs and Supply Study: Compilation of Findings; Final Report*. NEI BV/Unit Financial Advisory Services and Rabobank International Advisory Services, Rotterdam, September 2000, p.50.

and loan maturities of more than five years were scarce. In addition, there was limited leasing activity due to weak legal institutions.²⁹ In 2000, most banks were considered under-capitalized and possessed many non-performing loans, while also suffering from poor management and weak internal control systems. Aside from the weaknesses in the banking system, a major obstacle to SME development in the country is the pervasive low level of interpersonal business trust as well as a lack of overall “systemic trust.”³⁰

- **Former Yugoslavia Republic of Macedonia.** In FYR Macedonia, the economy contracted by more than four percent in 2001, as armed conflict brought to a halt several years of positive economic trends and reforms.³¹ Production levels fell to below that of 1990 and the number of people living in poverty increased. The periodic closing of trade routes, conflict in particular areas, and a pervasive uncertainty concerning the future have both undermined business confidence in the region and negatively affected export performance.³² Despite a peace agreement in August 2001, real GDP growth in 2002 increased slightly—by less than 1 percent—while unemployment hovered around 33 percent.³³ Macedonia has since tried to reset itself on the road to reform, as exhibited by the abolishment of the tax on financial transactions in December of 2002.

Financing for SMEs in Macedonia consists mostly of credit lines administered by banks. Collateral requirements for SMEs have been reported in the range of 150-200 percent and in some cases as high as 300 percent.³⁴ SMEs have demanded access to other financial products such as trade finance, export credits, supplier credits, venture capital, and leasing instruments.³⁵ Total domestic credit-to-GDP was recorded at 19.6 percent in 2001.³⁶

- **Serbia and Montenegro.** Serbia and Montenegro is much larger in terms of population, overall economic activity and industrial base than the other countries served by SEED. However, ten years of regional conflict and international economic sanctions have devastated the economy. GDP in 2000 was 45 percent of the 1989 level, while per capita income had fallen to between US\$840 and US\$990.³⁷ Furthermore, the country’s total debt stood at 110 percent of GDP in 2001, compared with 20-50 percent for the other SEED countries. This debt burden is likely one of the factors contributing to relatively low gross domestic investment. High public debt can lead to higher interest rates, reducing the credit available to the private sector and subsequently crowding out private investment.

Since 2000, Serbia and Montenegro has sought deep reforms in the financial and industrial sectors, while focusing on creating a “transparent legal and institutional framework for

²⁹ *Ibid.*

³⁰ See *Labor Market in Postwar Bosnia and Herzegovina: How to Encourage Businesses to Create Jobs and Increase Worker Mobility*, The World Bank, Human Development Unit, South East Europe Country Unit, Europe and Central Asia Region, Report No. 24889-BiH, November 04, 2002. p. xiv.

³¹ *FYR Macedonia Country Brief*. The World Bank, Europe and Central Asia Region. p.1.

³² *Former Yugoslav Republic of Macedonia: Transitional Support Strategy*. The World Bank, South East Europe Country Unit, ECC04, Europe and Central Asia Region, Report No. 22628-MK, August 20, 2001. p.4.

³³ *FYR Macedonia Country Brief*. Australian Department of Foreign Affairs and Trade. June 2003.

³⁴ *IFC SME Financing Needs and Supply Study: Compilation of Findings; Final Report*. NEI BV/Unit Financial Advisory Services and Rabobank International Advisory Services, Rotterdam, September 2000. p.16.

³⁵ *IFC SME Financing Needs and Supply Study: Compilation of Findings; Final Report. op. cit.* pp.13-18.

³⁶ Nexus Associates calculation based on the International Monetary Fund’s *International Financial Statistics*.

³⁷ *Federal Republic of Yugoslavia Transitional Support Strategy*, Report No. 22090-YU, South East Europe Country Unit, ECC04; Document of the World Bank, June 26, 2001, p.3.

privatization.”³⁸ The fragile banking system provides limited opportunities for SMEs to access domestic finance. By the beginning of 2002, total commercial bank credit to Serbian enterprises was about US\$3.4 billion or about 30 percent of GDP.³⁹ The minimal commercial skills and low level of institutional capability of the local banks, combined with a shortage of capital, present significant challenges for SME growth and development.⁴⁰

Table 1. Country Profiles (2001)

Indicator	Albania	BIH	FYRM	Serbia and Montenegro
Population, mid-year (millions)	3.2	4.1	2.0	10.7
Population Growth rate (%)	1.0	1.5	0.6	0.1
Urban population (% of total pop.)*	45.6	43.0	62	51.7
Infant mortality (per 1,000 live births)	23.0	15.0	22.0	17.0
Life expectancy at birth (years)	74.0	73.6	73.1	72.6
Poverty rate (% of pop. below national poverty line)*	-	-	22*	15-25**
Illiteracy rate (% of pop. Age 15+)	14.7	-	5.0	-
GNI per capita (current US\$)	1,340	1,240	1,690	930
GDP (Current US\$ billions)	4.1	4.8	3.4	10.9
GDP growth rate (%)	6.5	6.0	-4.1	5.5
Agriculture as a % of GDP	50.2	14.8	10.9	17.6*
Industry as a % of GDP	23.4	30.6	31.1	37.6*
Services as a % of GDP	26.4	54.6	58.0	44.8*
Gross domestic investment/GDP* (%)	19.4	21.3	16.7	13.5
Total Domestic Credit/GDP (%)	54.5	32	19.6	-
Total debt/GDP* (%)	20.4	49.0	41.5	110.0
SMEs per 1000 inhabitants***	16.5	-	14	8

Source: World Development Indicators database, April 2003

* Source: World Bank Development Report (Development Data Group), 2001. Figures are preliminary estimates for 2001.

**Estimated Range originates from 1995-2001, World Bank Development Report (Development Data Group), 2001.

***See footnote 17.

Role and overview of SEED

13. SEED focuses on meeting the needs of small and medium-sized enterprises through the following services:⁴¹

- **Investment Services (IS).** These consulting services entail an analysis of business operations to identify development needs, leading to recommendations for improving the firm’s performance. SEED also works with some companies to help them secure financing for proposed projects.

³⁸ For details of the reforms, see *Serbia and Montenegro: First Review Under the Extended Arrangement*, International Monetary Fund, IMF Country Report, June 2003.

³⁹ *Strategy for the Federal Republic of Yugoslavia*, European Bank for Reconstruction and Development, June 11, 2002, p.16.

⁴⁰ *Strategy for the Federal Republic of Yugoslavia*, European Bank for Reconstruction and Development, *op. cit.*, p.5.

⁴¹ Neither originating IFC documents, nor the business and implementation plan establish criteria for defining SMEs. However, SEED has indicated that it operates in line with the guidelines established by the IFC/WB SME Department. According to these guidelines, SEED’s target population is companies that have 10 to 300 employees, total assets of \$100,000 to \$15 million, and annual sales of \$100,000 to \$15 million.

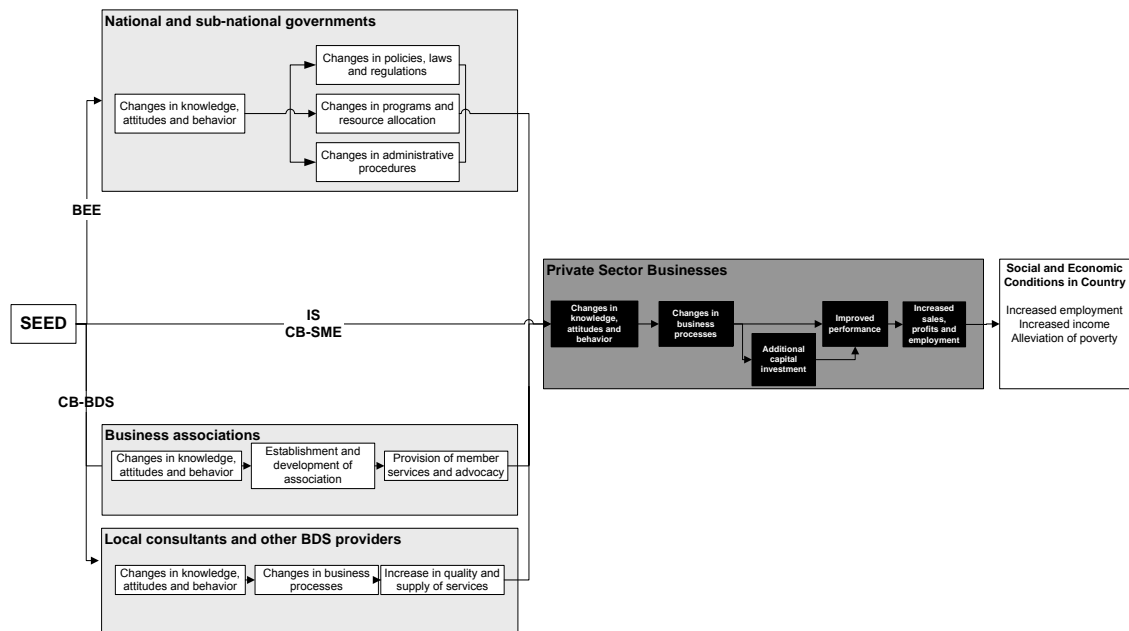
- **Capacity Building-SME (CB-SME).** This includes training programs targeted at SMEs that focus on improving overall business competitiveness. Courses have been provided on topics such as marketing, financial management, and human resource management.
 - **Capacity Building-Business Development Services (CB-BDS).** This includes a variety of initiatives aimed at expanding the “breadth and quality of services offered by business development service providers” in the region.⁴² CB-BDS focuses on building the capacity of local consultants, business associations, and local economic development organizations to provide services needed by SMEs.
 - **Business Enabling Environment (BEE).** SEED also seeks to improve the business environment for SMEs by working with government agencies and international donors on various policy, legal and regulatory reform efforts. In this regard, SEED aims to “help ensure consistent and coordinated efforts on shared priorities” among donors.⁴³
14. As illustrated in the program logic model depicted in Figure 1, private businesses in the regions constitute the principal target of SEED services.⁴⁴ However, as reflected in the model, private businesses can be either the direct or indirect target of particular SEED programs. In the case of investment services (and some capacity building projects), SEED provides services directly to firms to help them improve their performance. In other initiatives, SEED intends to change the behavior and/or performance of intermediary institutions that, in turn, have consequences for private businesses. In fact, a focus on intermediary organizations – business associations, business service providers, financial institutions, and government authorities – has become the hallmark of the international donor community’s new approach to promoting the development of the private sector. As such, the effectiveness of SEED should be judged, in part, on its success in transforming these intermediary institutions to better meet the needs of businesses, particularly SMEs.

⁴² *SEED Annual Report 2001*. The International Finance Corporation in Collaboration with The World Bank, 2001. p. 13.

⁴³ *Ibid.*

⁴⁴ Program logic models link activities to outputs and expected outcomes, noting important causal mechanisms. In so doing, they delineate the sequence of cause-and-effect relationships that are expected to lead to the attainment of stated goals, providing a solid foundation for the development of an appropriate study design.

Figure 1. SEED Program Logic Model



Source: Nexus Associates

15. Through 31 December 2002, SEED had total receipts of US\$24.4 million and expenditures of US\$12.6 million.⁴⁵ According to SEED records, of the US\$12.6 million, SEED had allocated a total of US\$5.8 million to its four strategic objectives: Investment Services (27 percent), Capacity Building – SME (22 percent), Capacity Building – BDS (37 percent), and Business Enabling Environment (14 percent). The remaining funds have been allocated to start-up and ongoing General Management and Administrative expenses.
16. Beginning with 22 employees in BiH, SEED's staff grew rapidly as the organization opened new offices, reaching a peak of 82 by the end of FY02 when all offices were fully operational.⁴⁶ (Employment has remained fairly constant since then.) As of December 2003, the offices in BiH – which includes headquarter operations in Sarajevo – accounted for 51 percent of the entire SEED workforce. The office in Serbia and Montenegro housed 22 percent of the SEED staff, and FYRM and Albania comprise 15 percent and 12 percent, respectively.⁴⁷

⁴⁵ SEED's financial accounts are on a cash basis. Its fiscal year ends June 30th.

⁴⁶ Staff are organized into three teams: investment services (IS), private sector development (PSD) and financial management (FM). Each team, to varying degrees, contributes to all four strategic objectives.

⁴⁷ With the approval of donors, SEED has elected to take a low profile in Kosovo given United Nations control, the extent of international involvement in political and economic matters, the level of development within the region, and SEED's own capabilities.

III. Investment Services

Rationale

17. The overall success of any business is dependent on being able to provide goods or services needed by customers who are willing to pay a price that yields an adequate rate of return. To be successful, SMEs need sound management and capital. Initial planning documents for SEED noted that a significant share of firms in the region lack strong managers and access to financing. With regard to the latter, these documents suggest that financial institutions are more likely to provide long-term financing for particular projects when given reliable information on the overall creditworthiness of the investment project.
18. Therefore, from its inception, SEED has worked with companies to address both financial and non-financial issues through the provision of consulting services. The organization has argued that it fills a gap in the market, by facilitating access to services that SMEs need in order to secure financing and upgrade the knowledge and skills of managers. The rationale for SEED's interventions in the consulting market is two-fold. On the one hand, services needed by companies may not be available at all. On the other hand, even if services are available, companies may not elect to purchase services for a number of reasons, including the lack of knowledge about their own needs, inability to judge the quality of services that they are likely to receive, difficulties finding qualified service providers, and inability to afford services given cash flow constraints.

Role of SEED

19. SEED provides a variety of services under the rubric of Investment Services that are designed to address both financial and non-financial needs of SMEs. These services can be summarized as follows:
 - **Internal Enhancement Plan (IEP).** SEED typically begins work with clients by conducting an assessment of their current operations to determine prospects for growth and identify critical needs. While assessment covers operating and technical issues, to a great extent, the analysis focuses on financial matters, e.g., contribution margins, cash flow, and financing requirements. IEP reports typically contain numerous recommendations that are tailored to the needs of each company. These tend to revolve around suggested modifications in the nature and/or scale of proposed investments, efforts to strengthen marketing and sales, steps to improve specific production processes, adoption of financial controls, and the establishment of information systems. Recommendations are generally organized into three categories:
 - Immediate (A). Issue must be resolved for implementation of Investment Plan (required for financing);
 - Mid-term (B). Issue should be addressed in the next 12 months (likely to be required for financing); and

- Long-term (C). Issue “ought” to be addressed in the next 12 to 20 months (long-term benefits to company).

When the IEP is completed, companies are asked to review the document and agree to implementing the recommendations categorized as “A” as a condition for SEED to continue working with the firm to secure financing, if warranted.

- **Investment Plan (IP).** This service centers on the preparation of an “investment plan“ for submission to a financial institution as part of the loan application or request for equity. While the scope and quality vary, the plans typically describe the nature of the project, existing markets, marketing strategies, major operations, management team, ownership structure, and past operating and financial performance. They also include estimates of project costs and present a financing plan, and *pro forma* financial statements along with a discussion of potential risks. In a sense, they serve as a prospectus for potential investors in the project, disclosing information that financial institutions would find important in making a financing decision. As part of the service, SEED identifies financial institutions that would likely provide financing for the project. In addition to making introductions, SEED staff typically meet with officials from the financial institutions to review the investment plan and discuss financing requirements. In so doing, SEED works with a range of financial institutions, including local and foreign banks.
 - **Post-IEP.** SEED is moving increasingly into management consulting, providing services that are not directly tied to raising capital. Companies can call on SEED for assistance related to any number of functions or processes within their firms. To date, technical assistance rendered by SEED has focused on marketing and sales, financial management, and information systems.
20. At times, SEED staff provide direct assistance based on their own expertise and experience. However, the more typical approach is for SEED staff to serve in a project management capacity, linking clients to qualified third-party service providers. The Business Development Analyst assigned to the project is tasked with helping the company define its needs, laying-out an appropriate course of action, marshalling needed resources, and overseeing the provision of services. Consultants are called on to undertake specific analyses of particular aspects of the business – typically focusing on market assessments – that are subsequently summarized in written reports. In all cases, SEED staff is responsible for the final product.
21. SEED has employed a specialist in environmental and social (E&S) issues from its inception. Based in Sarajevo, the E&S specialist has been responsible for reviewing proposed investment projects and offering recommendations on steps that companies should take to improve performance in these areas.⁴⁸
22. Unlike many other organizations, at the direction of its donors, SEED charges for its services in an attempt to rationalize service delivery and pave the way for sustainable operations.

⁴⁸ The E&S specialist has also participated in various projects carried out under the banner of capacity building and the business enabling environment.

IS clients and activities

23. Through the end of December 2002, SEED had undertaken 104 IS projects with 77 companies.⁴⁹ SEED targets companies that can define their business objectives in terms of “sustained, market-based competition.”⁵⁰ Based upon the results of the survey, IS clients can be profiled as follows:⁵¹
- **Firm size.** Based on the results of the client survey, about 92 percent of clients had annual sales of €15 million or less at the time when they first started working with SEED. On average, the companies that responded to the survey had annual sales of approximately €4.3 million (median = €1.8 million) and employed 117 people (median = 43).⁵²
 - **Ownership.** Based on the results of the survey, approximately 73 percent of IS clients are fully owned by local private investors. Government (including state-owned enterprises) is a minority shareholder in roughly nine percent of SEED clients that responded to the survey. Fifteen percent of survey respondents have some foreign investment, with foreign investors owning a majority interest in nine percent of the companies; one firm that responded to the survey is 100 percent foreign-owned.
 - **Management.** Virtually all (97 percent) of the survey respondents, including majority foreign-owned firms, indicated that the chief executive of the company was a permanent resident of the country. Of all the companies that completed the survey, only one firm reported that its chief executive officer was a woman.
 - **Industrial distribution.** The manufacturing sector accounts for almost 58 percent of the IS clients that responded to the survey.⁵³ Within manufacturing, food processing is the leading industry, accounting for more than 50 percent of manufacturing clients and 30 percent of all clients that received investment.
24. SEED completed 73 of the 104 projects by 31 December 2002; of the remaining 31 projects, five were dropped and 26 projects were still active.⁵⁴ Table 2 shows the split between different types of IS projects.

⁴⁹ This includes three companies that received assistance prior to the opening of SEED’s office in Sarajevo in September 2000. All three companies were located in Kosovo (Hotel Jakova, Galanteria, and ABBA Trade). The geographical distribution of clients and individual projects is shown in Appendix Table A-1.

⁵⁰ *SEED Annual Report 2001*. The International Finance Corporation in Collaboration with The World Bank, 2001.

⁵¹ Findings are based on a client survey administered to companies that completed projects by 30 September 2002. More detailed information on clients obtained through the survey is presented in Figures A-1 and A-2. SEED did not begin tracking data on IS client characteristics until May 2001. At that time, staff were required to complete a Client Data Sheet (CDS) in Microsoft Word. In January 2003, the CDS form was streamlined, transferred to an Excel format, and linked to the organization’s Project Tracking and Management Reporting System (PTRMS). As such, the only data on client characteristics that has been systematically compiled are for clients that have been served since January 2003.

⁵² Two companies had annual sales greater than US\$15 million while one company had annual sales of less than US\$100,000. These companies do not conform to the definition of SMEs adopted by IFC—see footnote 42.

⁵³ SEED’s operating policies state that the organization is open to working with companies engaged in “any productive venture in agriculture, agribusiness, manufacturing, services, tourism, or infrastructure; [however], projects involving tobacco, military products, real estate development, and pure trading operations are not eligible for SEED assistance.”

⁵⁴ Appendix Tables A-2 to A-5 exhibit a full breakout by each quarter of the number of started, active, completed, and dropped IS projects.

**Table 2. Investment Service Project Activity
(Inception through Q2FY03)**

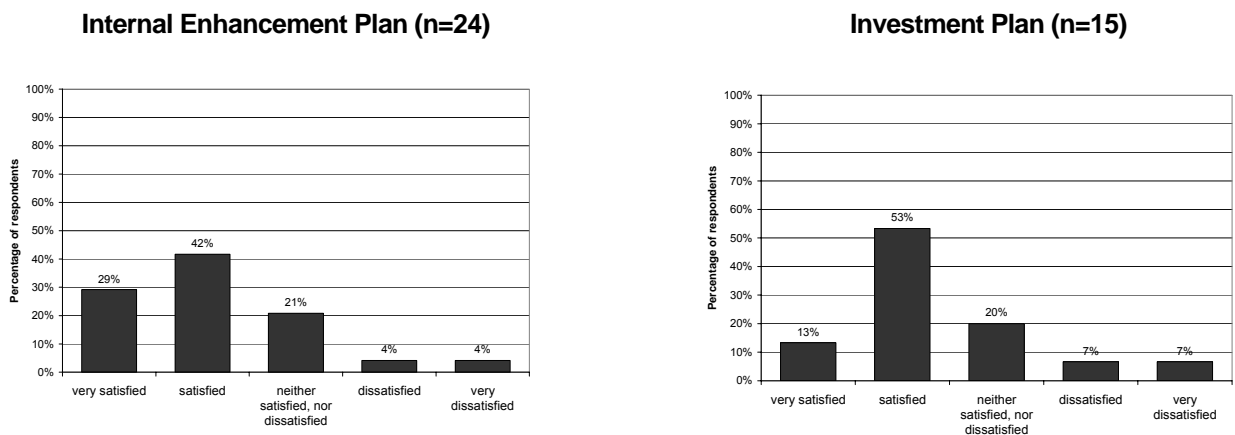
Project type	Total IS Projects	Total IEP Projects	Total IP Projects	Total other Projects ⁵⁵
Started	104	51	29	24
Completed	73	38	25	10
Dropped	5	2	0	3
Active at End of Q2FY03	26	11	4	11

Source: SEED records

Client satisfaction

25. All organizations need to be concerned with the extent to which they are able to satisfy their customers. The degree of satisfaction has a direct bearing on client loyalty, repeat business and the acquisition of new customers. In general, customer satisfaction revolves around expectations. Expectations are a function of explicit promises made through advertising, personal selling, contracts and other communications as well as assurances arising from past experience or word-of-mouth. Clients are satisfied when their perception of the services provided to them is consistent with their expectations.
26. As shown in Figure 2, approximately 71 and 67 percent of IS clients reported that they were "very satisfied" or "satisfied" with IEP and IP services, respectively – suggesting that the services met their expectations. Moreover, in interviews with SEED clients, owners/managers of firms noted the high degree of competency and professionalism among SEED staff. They also called attention to the care with which SEED has treated confidential information.

Figure 2. Degree of Satisfaction with IS Services

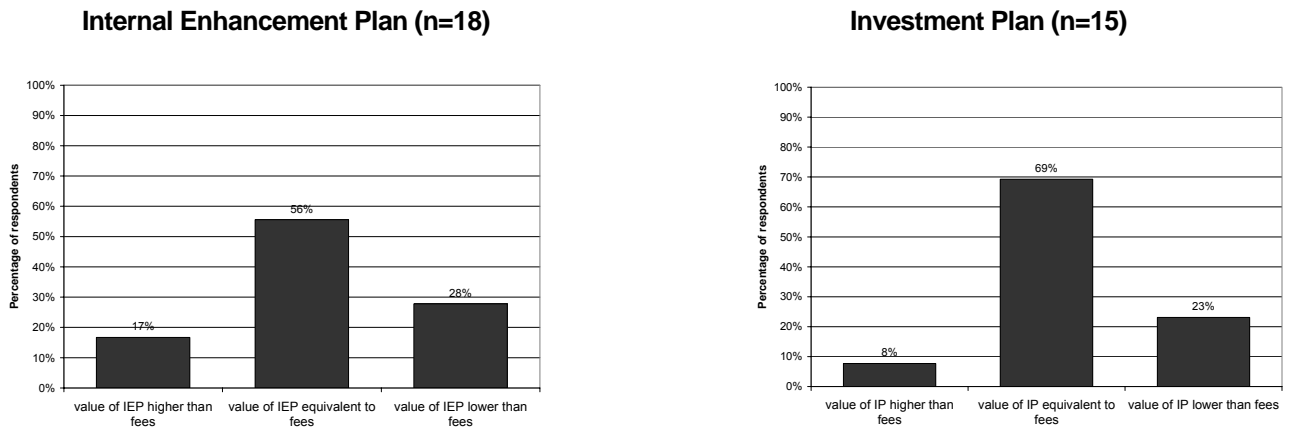


Source: Client survey

⁵⁵These include such activities as: working with a bank to set up a "risk reserve" fund; forming a roundtable meeting in Milan to identify opportunities for developing a shoe cluster in Kumanovo, Macedonia; and developing a plan to support the creation of a number of "Biz Centers"—centers that would act as internet cafes and business service locations. The majority of these other projects were started in the first quarter of FY03.

27. Approximately 8 and 14 percent of respondents indicated that they were “dissatisfied” or “very dissatisfied” with IEP and IP services, respectively. Although dissatisfaction is rare among SEED clients, it is still important to try to understand the reasons why some clients perceived that services fell short of their expectations. The in-depth interviews suggested reasons for dissatisfaction. In some cases, clients harbored unrealistic expectations with respect to SEED’s ability to secure financing for their projects under very favorable terms. When SEED indicated that financing was unlikely to be forthcoming given the firms’ performance or when the companies were faced with collateral requirements or other terms and conditions imposed by financial institutions, companies felt their needs had not been met. In addition, some companies voiced frustration with the lack of ongoing support from SEED, particularly with respect to the implementation of recommendations offered in the IEP report. While the reports were well received, some companies reported that they did not fully understand the recommendations or were unable to implement them given the lack of management skills or conditions within the market. For example, one company visited as part of the evaluation acknowledged the deficiency of its financial controls and accounting systems. However, the owner pointed out he was unable to recruit a qualified accountant or bookkeeper that could be trusted.
28. Satisfaction can also be judged in terms of the perceived value of the services compared to the fees charged to clients.⁵⁶ In this regard, 17 percent of respondents stated that the value of the IEP services provided by SEED was greater than the fees charged as shown in Figure 3. The corresponding figure for IP services was eight percent.

Figure 3. Perceived Value of IS Services Relative to Fees



Source: Client survey

29. Given the degree of subsidy involved in the service delivery, it is important to note that 56 percent of companies that responded to the survey indicated that the perceived value of IEP services was

⁵⁶ Value in this context refers to the value derived by individual clients. It does not refer to the value accruing to society, at large, which may be greater or less than private benefits due to externalities.

equivalent to the fees charged and 28 percent stated that value was lower. Comparable figures for IP services were 69 percent and 23 percent. In light of the fact that a substantial portion of respondents indicate that the value of services was less than or equal to the fees, it would seem difficult for SEED to increase prices for its services without experiencing a decrease in the amount of services demanded.

30. The degree of satisfaction expressed by companies that have received financial advisory services and/or technical assistance signals that the majority perceive that SEED services met their standards of quality. The evaluation team’s review of reports prepared by SEED suggests that IEPs and IPs are generally well prepared, particularly with respect to financial analysis. However, the quality varies. The level of analysis of markets for particular products and technical aspects of operations varies considerably. As such, financial projections, while following generally accepted standards, may not always have solid underpinnings. The evaluation team also noted that some investment plans appear to offer fairly optimistic projections with only limited reference to potential risks. However, not all projects warrant the same level of analysis – the quality of the reports prepared by SEED needs to be considered within the context of the size of the company or particular investment as well as the level of effort expended by SEED staff and external consultants. Many projects do not merit exhaustive assessments given the amount of money involved.

Impact

Availability of alternative sources of advisory services

31. SEED is intended to fill a gap in the market, providing services that are not offered by other companies or organizations in the countries in which it operates. As indicated in Table 3, responses to the survey suggest that SEED has served needs in the market that are not being adequately addressed by other service providers. Approximately 46 percent of IEP clients and half of IP clients that responded to the survey stated that there were *no* other companies or organizations that could have provided services similar to those offered by SEED at the time they sought assistance. Therefore, these companies were not selecting among alternative services providers – they believed that SEED was the *only* organization that could render needed services in the respective countries.

Table 3. Availability of Similar Services from Other Providers

Were there any other companies or organizations that could have provided services similar to an:	Yes	No	Don't know
Internal Enhancement Plan (n=24)	37.5%	45.8%	16.7%
Investment Plan (n=14)	35.7%	50.0%	14.3%

Source: Client survey

32. Approximately 37 percent of IEP and IP clients indicated that there were other options available to them. Some companies noted that there were local consultants operating in the market as well as

major international companies such as BearingPoint and Deloitte Touche Tohmatsu. Others called attention to programs supported by international donors such as USAID, GTZ and EAR.⁵⁷ Therefore, on the one hand there are opportunities for companies to turn to donor-supported organizations to obtain support to develop very basic business plans – these services tend to be oriented toward very small companies that serve local markets. The cost to prepare these reports is well under US\$1,000. On the other hand, some companies are able to draw on high-level international consultants, often provided in conjunction with financing offered by international organizations. These business plans can cost upwards of US\$100,000. Interviews with SEED staff, government officials, and donor organizations suggest that SEED is operating in the middle of the market.

33. As shown in Table 4, when asked to explain the reasons for selecting SEED, most of the companies that suggested that alternative service providers were available (9 IEP clients and 5 IP clients) attributed their choice to the higher quality of SEED’s services, highlighting the professionalism and honesty of SEED’s staff. The IP clients that reported that similar services were available elsewhere reported that in addition to believing that SEED provided higher quality services, they also believed SEED would more rapidly respond to their needs and were less expensive. Other reasons cited by companies for selecting SEED rather than other organizations include the organization’s connection to the IFC and World Bank. This connection provides an imprimatur for SEED’s services and creates expectations of potential IFC financing even though SEED staff inform clients that the organization has no ability to guarantee such funding. Finally, in interviews, some companies highlighted SEED’s ability to provide international consultants at relatively low cost to them.

Table 4. Reasons for Selecting SEED*

Company selected SEED because...	IEP (n= 9)	IP (n=5)
Believed that SEED could provide higher quality services than available elsewhere	6	4
Believed that SEED would respond to our needs more rapidly than available elsewhere	4	4
Believed that SEED’s services were less expensive than available elsewhere	2	3
For other reasons	7	5

*Note: Given the small sample, the figures refer to number of respondents rather than the percentage

Source: Client survey

Access to financing

34. As noted above, one of the principal rationales for establishing SEED was to help companies secure financing. The Investment Plan prepared by SEED is intended to present a solid basis for providing financing to a particular company. In this regard, it is important to note that roughly 53

⁵⁷ While not mentioned by any of SEED’s clients during interviews, there are other programs in the Balkans that provide assistance to SMEs. For example, EBRD’s South East Europe Business Advisory Services Programme provides grants covering up to 50% of the cost of local consultants, with a limit of €10,000. The clients of this program are typically smaller than SEED’s clients.

percent of the IP clients that responded to the survey had approached banks or other financial institutions for financing for the project before seeking help from SEED. Two-thirds of these firms were not able to raise monies from outside sources prior to seeking assistance from SEED. The remaining third (three firms) were able to raise at least some of the needed financing on their own -- these companies came to SEED in order to raise additional capital needed for the projects.

35. According to records provided by SEED, the organization completed 20 Investment Plans from inception through 30 September 2002.⁵⁸ Under the definition employed by all Project Development Facilities (PDFs), an Investment Plan is considered “complete” when a financial institution expresses an interest in providing financing. However, a financial institution’s intent to provide financing does not, of course, ensure that the funds will actually be provided. In reality, financial institutions may withdraw offers or clients may decide not to pursue the financing offered by banks due to collateral requirements, unacceptable terms and conditions, or a variety of other reasons.
36. SEED has followed-up with all companies that completed IP projects to determine whether promised financing was actually secured by clients. SEED records indicate that half of the 20 companies that completed IP projects had actually obtained financing. These 10 companies secured a total of €2.5 million, representing an average of approximately €250,000 per firm. Financing includes € 612,000 in equity and €1.9 million in debt financing (including €110,000 in short-term credit).⁵⁹
37. Equity has been provided by two sources. The largest equity investor has been Horizonte Bosnia-Herzegovina Enterprise Fund. The Fund’s objective is to achieve long-term capital growth by making direct and equity-related investments in a portfolio of small- and medium-sized private or privatized companies exclusively in Bosnia and Herzegovina.⁶⁰ The other source of equity finance tapped by SEED is Volksbank BH. Headquartered in Sarajevo, Volksbank BH is 100 percent owned by Oesterreichische Volksbank AG. The bank took a minority position in Bamcard – a debit and credit card company that serves banks and consumers located throughout BiH.
38. Most loans to SEED clients appear to be in the form of senior debt, fully collateralized by the fixed assets of the company and/or personal property of the owners of the firm. Term loans typically had terms of 36 months with interest rates ranging from eight to 15 percent.⁶¹ SEED turned to five different financial institutions for financing – BOR Banka, Credins Financial Institution, ABS Banka, Interim Credit Unit (ICU) – Kosovo, and Raiffeisenbank Jugoslavija. Two of these institutions merit additional comment.
 - **Interim Credit Unit – Kosovo.** The ICU is a joint project of the European Agency for Reconstruction (EAR) and the World Bank. The main objective of the project is to inject needed credit into Kosovo’s SME sector as rapidly as possible. It was legally established by UNMIK in the fall of 2000 and is licensed by the Bank and Payments Authority of Kosovo (BPK) as a non-bank financial institution, managed by the ICC Bank of Ireland. EAR

⁵⁸ As per the TOR and Study Design, SEED was asked to provide data on IS projects that were completed by 30 September 2002. It should be noted that an additional five IPs were completed during October-December 2003 according to SEED records.

⁵⁹ Appendix Table A-6 provides details of financing secured by SEED clients.

⁶⁰ Investors in the € 15.6 million fund include EBRD, IFC, FMO, IÆ, Hypo-Alpe-Adria Bank AG, Cassamarca, Norfund, Swedfund, OeKB, and Siemens Österreich. Horizonte invested in one firm – a distributor of frozen fish located in Banja Luka, Republic of Srpska.

⁶¹ All loans were made in euros, dollars, or deutschemarks. One loan was made in Kuwaiti Dinar.

contributed the equivalent of €5 million to cover the operational cost of the ICU and provide capital for the revolving fund. The World Bank contributed €5 million to the revolving fund. SEED was asked to review five projects for the ICU – all were subsequently financed.

- **Raiffeisenbank risk reserve fund.** The Austrian Government committed €660,300 as a “risk reserve” to offset potential losses on loans made by Raiffeisenbank Jugoslavija (RBJ) to qualified SMEs in Serbia and Montenegro. Given a 10 percent risk contribution, the reserve fund was intended to cover a loan portfolio totaling €6.6 million. SEED entered into a memorandum of understanding with RBJ in March 2002 to support the implementation of the fund by identifying and qualifying potential customers for the bank. SEED has brought two companies to RBJ for financing since the inception of the fund in spring 2002. One of these companies subsequently secured financing; the other could not satisfy the terms and conditions of the loan. The reserve fund remains underutilized – only 15 percent of the funds have been committed to date.

39. The evaluation team surveyed all of the companies that secured financing. Nine of the ten companies responded to the survey. Five of the nine companies responded that they would have gone ahead with the project had they not received assistance from SEED. Furthermore, four of the nine firms responded that they would have been able to obtain the same amount of financing without SEED assistance.⁶² In explaining the reasons for believing that they could have obtained financing on their own, firms pointed to existing relationships with financial institutions, the availability of financing through donor-supported programs such as the ICU in Kosovo, and/or the conviction that they did not able to obtain financing under any more favorable terms than they would have without SEED assistance. With regard to the latter, some firms suggested that local banks were only concerned with whether the company has sufficient collateral. While the bank may have been more comfortable with providing financing as a result of the IP prepared by SEED, the ultimate decision on whether to offer a loan hinged on the value of property that could be pledged by the company. Interviews with financial institutions in the region support this view and suggest that few, if any, banks adjust terms and conditions for relative risk. Interest rates and collateral requirements are established by policy and applied to customers in a uniform manner.
40. Five of the nine IS clients that received financing *and* responded to the survey indicated that they have already completed the projects for which they sought financing. According to survey results, the average total project cost for companies that have received financing and gone on to implement the project was on the order of €1.1 million (median= €1.5 million) with the largest project representing a total investment of over €2.1million.⁶³ The total investment associated with the five completed projects is on the order of €5.5 million. Three of the remaining four projects are scheduled to be completed within the next year. These represent a total investment of €4.0 million.

⁶² Two firms were common to both groups—respondents from these companies indicated that they could have obtained financing without SEED *and* they would have definitely gone ahead with the project in the absence of SEED assistance. However, not all of the nine companies responded to both questions: two firms did not respond to the question regarding whether they could have obtained financing on their own and two other firms did not offer a response as to whether they would have gone ahead with their respective projects.

⁶³ Companies were asked to estimate the cost of acquisition of fixed assets, interest during construction, other preliminary and pre-operational expenses, and the increase in net working capital (current assets minus current liabilities) required for the project. Results from the survey are comparable to data maintained in SEED files with respect to project costs.

41. One company that received financing with SEED's assistance, however, has postponed the project indefinitely due to the lack of sufficient long-term capital. In this case, the firm was seeking a total of €480,000. While the company was able to secure a three-year €180,000 loan to refinance its outstanding debt, the financing fell €300,000 short of the total needed to fully implement the investment plan. The company has not been able to obtain long-term financing needed to introduce a new variety of agricultural product, purchase new equipment, and develop new processing facilities. At this point, the investment is on hold. Interviews with the chief financial officer suggest that the company's financial position is deteriorating, as such; prospects for the project being carried out appear to be poor.
42. Furthermore, while another company responded that it had completed the investment project, further questioning revealed that it had redefined the investment plan given an inability to secure the rest of the capital needed for its implementation. In this case, SEED helped the company secure more than €760,000 in equity and debt from Horizonte. At the time the deal was signed, Horizonte indicated it would arrange the additional debt financing of approximately €1.4 million needed to complete the project. To date, the company has been unable to raise the capital needed to fully implement the proposed project. The company's request for long-term financing was rejected outright by one bank and the owner refused to accept another offer that he considered onerous (7-year loan at 14 percent with a six-month grace period backed by personal guarantees). While the company has not been able to secure all of the financing needed for the project, it has still gone ahead with the construction of a new distribution center – albeit on a more modest scale – using a combination of proceeds from the financing provided by Horizonte, new short-term loans and additional cash from the owner. However, the owner of the firm indicated that the company was considering renting out the bulk of space at the new facility to other firms, rather than using it for processing and distributing its own line of frozen fish products. While plans may change in the event of additional funding, at the time of the interview, the owner was questioning the whole business rationale for the investment and expressed a desire to sell the facility to a foreign firm.
43. As noted above, ten companies that completed an IP did not secure financing through SEED. When surveyed, three companies indicated that they had postponed their projects, with two citing their inability to secure financing as the principal reason for delay. Another firm cancelled its project entirely because it, too, was unable to obtain needed capital. Two firms, however, stated that they went ahead with their respective projects and expect to complete them within a year.⁶⁴
44. Interviews with some of these companies suggest that the major barrier to securing financing was the lack of collateral. While banks may have expressed an interest in providing financing, companies could not meet collateral requirements – which range from 200 to 350 percent of the loan amount – given the value of tangible property at hand or the owners' unwillingness to secure loans with personal property. For example, one company that specializes in collecting and processing forest products was seeking €1.95 million in equity and €450,000 in debt finance. While no investor stepped up to provide equity, the company did receive an offer from Raiffeisen Bank Jugoslavija to provide the needed loan. However, the company could not satisfy collateral requirements despite the willingness of a risk reserve fund (established by the Austrian

⁶⁴ Two companies did not respond as to whether or not they went ahead with their respective projects.

Government) to cover 10 percent of any loss. As a result, the deal never went through.⁶⁵ A few investments may have fallen through for reasons particular to that project. For example, another firm, a beverage producer, was seeking an equity investor. Horizonte Venture Capital Fund agreed to buy a majority interest (51 percent) of shares owned by the state. While the bid was accepted, due to certain legal obstacles related to Article 36 of the Privatization Law, the deal between Horizonte and the Directorate for Privatization was not completed.

Improved performance

45. SEED provides services other than assistance with securing financing. The intention is to improve the performance of clients with respect to specific business processes and/or the enterprise as a whole. As a result, companies may benefit from investment services (IS) in areas apart from securing credit.
46. In this regard, around 85 percent of the IS clients that responded to the survey reported that employees gained new knowledge or skills as a direct result of SEED's services. Virtually all of these companies indicated that the new knowledge and skills have been put to use.⁶⁶
47. In turn, new knowledge and skills that have been obtained as a result of SEED services have enabled companies to institute a variety of new practices in their firms. More than 80 percent of IS clients stated that they had implemented changes in at least one aspect of their business as a direct result of the services provided by SEED.⁶⁷ In general, the most frequently reported changes made by companies tend to be the kinds of things that one would expect given the subject of the assistance provided by SEED. Companies report shifting their business strategies to focus on different products and/or markets, adopting new marketing approaches, changing their method for sales and distribution, reorganizing the layout of production facilities, tightening quality control procedures, and introducing better accounting systems. Companies were more likely to undertake these changes when they were an objective of the services provided by SEED (as shown in the last column of Appendix Table A-8). For example, while one-third of companies responded that they had changed their business strategy as a result of SEED, almost 85 percent of the companies that received services that were *explicitly intended* to lead to changes in business strategy actually altered their strategy.
48. However, changes in capabilities and practices are a means to an end. The test is whether these changes actually improve performance. In fact, approximately 59 percent of IS clients that responded to the survey reported that their performance improved in one or more ways.⁶⁸
49. As shown in Figure 4, overall, 40 percent of respondents indicated that SEED assistance increased the ability of their company to compete to a "great" or "moderate" extent. Six percent (2 of 33 respondents) stated that without SEED assistance the company could not have survived and would have been forced to cease operations.

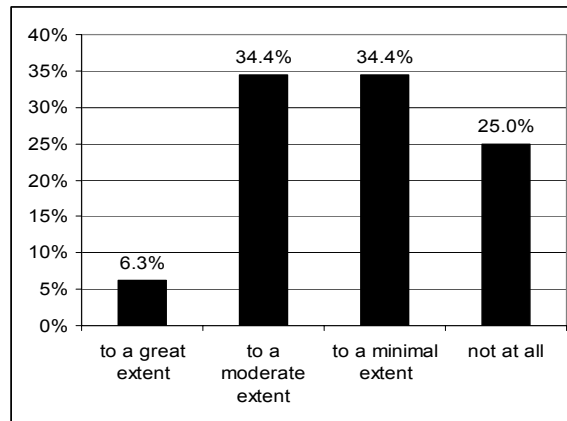
⁶⁵ SEED's annual report indicates that the organization was successful in "raising" financing for both Mobi and Fruktona.

⁶⁶ See Table A-7 in the Appendix for more detail.

⁶⁷ See Appendix Table A-8.

⁶⁸ See Appendix Table A-9.

Figure 4. Impact of SEED on Company Competitiveness
Did SEED Increase the ability of the Company to Compete? (n=32)



Source: Client survey

50. Ultimately, the aim of investment services is to boost the performance of firms in terms of profitability. As demonstrated in Table 5, roughly 30 percent of IS clients that responded to the survey reported that SEED’s assistance resulted in higher annual sales and 36 percent indicated that their net profits were higher due to SEED assistance.

Table 5. Impact on Enterprise Performance

Is your establishment’s performance in the following areas better than it would be without SEED’s assistance? (n=33)	Yes	No	Don’t Know
Annual sales	30.3%	63.6%	6.1%
Net profit	36.4%	51.5%	12.1%

Source: Client survey

51. The survey also asked IS clients to attempt to quantify the impact of SEED services on sales and employment. Specifically, it asked companies to estimate what the level of sales and employment would have been in 2002 in the absence of SEED services. The actual (observed) performance in 2002 was compared to the estimated performance in the absence of SEED services (i.e. the counterfactual) to gauge the impact of SEED services.

52. Only five companies provided sufficient data to calculate the difference in sales and employment attributed to SEED’s intervention. Together, these companies reported a total of €3.3 million in additional sales in 2002 as a direct result of the assistance provided by SEED (mean = €654,227, median = €153,601). In terms of employment, these firms attributed a total of 89 additional employees in 2002 to SEED (mean = 17.8, median = 7).

Development impacts

53. Successful IS clients are contributing to economic development in the region. Impacts on clients ripple throughout the economy, giving rise to changes in value added, employment, and other measures of economic activity. While an analysis of the broad economic impact of SEED is

outside the scope of this evaluation, it is possible to gain some insights into the effects of improved performance among SEED clients:

- **Economic distortions.** About 44 percent of SEED clients believed their financial performance had been impeded to some degree as a result of government policies. Approximately nine percent of clients (3 companies) expressed the view that the company's financial performance was affected *heavily* by tariffs, import restrictions, government subsidies or similar provisions. These three companies indicated that they had been significantly harmed by such regulations. The companies that reported being harmed called attention to custom duties and tax policies, specifically the value-added tax.
- **Exports.** On average, the IS clients that provided information on the extent of their exporting activity in 2002 had annual exports of approximately €413,635. However, the distribution is highly skewed. In fact, 48 percent of companies do not export any of their goods or services. Exports are important for a number of reasons. Beyond the classic rationale of gains from trade when countries focus on products in which they enjoy a comparative advantage, exporting offers a means for companies in countries with relatively small markets to benefit from economies of scale. Exporting is particularly important for companies in the region given small and highly fragmented domestic markets.
- **Competitors.** About three-quarters of the firms that responded to the survey indicated that their competitors were located within the Balkan Region.⁶⁹ Firms in Serbia and Montenegro appear to face more competition from outside the region than firms in the other three nations, with about 43 percent of their competitors residing outside the country's border. To the extent that companies compete with other local companies for a fixed share of the market, there is a chance of displacement, i.e., one firm may gain market share at the expense of another.
- **Backward linkages.** As companies expand, their demand for raw materials and components also expands leading to further economic impacts. Here it is important to note that companies source a significant percentage of purchased inputs from other companies within their respective countries. Approximately 57 percent of the IS clients that responded to the survey purchased more than 75 percent of the raw materials—components and subassemblies used to produce their own goods or services—from other firms within the country where they are located.⁷⁰
- **Use of business services.** There are a number of factors that may limit the willingness and ability of firms to purchase consulting and training services from outside providers. As shown in Table 6, the principal factor that IS clients point to is their inability to afford services. However, they also highlight problems associated with their ability to find service providers and ensure that the quality of services will be adequate. While these constraints exist, 43.3 percent of respondents indicated they were more likely to use private consulting and/or training services in the future as a result of their interactions with SEED. This is significant given SEED's aim to promote the development of a vibrant market for business services.⁷¹

⁶⁹ See Appendix Table A-10.

⁷⁰ See Appendix Table A-11.

⁷¹ A discussion of the role of SEED in strengthening the capacity of local services providers is presented in the section of this report that focuses on capacity building for business development services.

Table 6. Factors Limiting Demand for Consulting and Training Services

Has your establishment experienced any of the following: (n = 29)	% Yes	"Yes" Response n=	If yes, to what extent has this limited your use of consulting and training services?				
			Great extent	Moderate extent	Minimal extent	Not at all	Don't Know
Difficulty affording services	41.4%	12	25.0%	50.0%	8.3%	16.7%	0.0%
Lack information on the quality of services provided by particular providers	34.5%	10	0.0%	40.0%	30.0%	20.0%	10.0%
Difficulty putting recommendations offered by service providers into action	34.5%	10	10.0%	30.0%	0.0%	60.0%	0.0%
Difficulty finding service providers that are qualified to address our establishment's needs	17.2%	5	20.0%	60.0%	20.0%	0.0%	0.0%
Difficulty negotiating a work plan and budget with service providers	13.8%	4	0.0%	75.0%	25.0%	0.0%	0.0%
Difficulty identifying needs	10.3%	3	33.3%	0.0%	33.3%	33.3%	0.0%
Difficulty managing projects with service providers	6.9%	2	0.0%	50.0%	50.0%	0.0%	0.0%

Source: Client survey

- **Demonstration value.** Finally, it is often remarked that the services provided by SEED have demonstration value, i.e., other companies will emulate the actions of SEED clients. As shown in Table 7, the survey results provide some support for this claim. Some companies indicated that they knew of other firms that had followed their lead in making changes in business strategies or operations, undertaking new investments in the country (primarily in the same industries), and providing training to company personnel.

Table 7. Demonstration Effect

Do you know other companies that have followed the lead of your establishment with respect to the following actions:	n	Number responding "Yes"	Percent responding "Yes"
Making changes in business strategies or operations?	29	10	34.5%
Seeking assistance from SEED?	29	8	27.6%
Making or planning new investments in the country?	29	8	27.6%
Providing or arranging training for managers, employees or workers?	29	6	20.7%
Seeking assistance from outside providers of	29	5	17.2%

consulting and training services?

Source: Client survey

Environmental and social issues⁷²

54. A specialist retained under separate contract by OEG conducted an evaluation of E&S issues at SEED. While the report concluded that no clear E&S policy currently exists, it goes on to state that the support provided by SEED has been appropriate. SEED focuses on helping clients to improve their performance by taking realistic steps toward regulatory compliance, starting with the most cost-effective actions. Four of the seven companies visited as part of the assessment have implemented E&S improvements as a result of SEED advice. Minor E&S issues were identified at five of the seven companies. While these companies are currently unlikely to be compliant with local regulations and IFC requirements, most were taking corrective action.

Viability

55. Approximately two-thirds (63.6 percent) of IS clients that responded to the survey reported that their respective companies were profitable in 2002. Twenty-four percent stated that the firm was not profitable. The remaining nine percent did not answer the question or did not know.
56. Approximately 38 percent of respondents revealed that the company had difficulty paying suppliers and approximately 30 percent had significant problems servicing existing debt (Table 8). As a result, roughly 47 percent of companies needed owners to inject additional cash into the firms to maintain operations and more than one of three respondents stated that the company's "survival" was dependent on continued cash contributions from owners. Interviews with managers of companies that had completed projects suggested that some of the cash flow problems stemmed from the fact that project costs (including working capital) were higher than anticipated. In other circumstances, problems related to unexpected loss of customers or various aspects of ongoing operations.

Table 8. Viability of Companies

	n	Number responding "yes"	Percent responding "yes"
Has your establishment had any significant problems paying suppliers in the past year?	29	11	37.9%
Has your establishment had any significant problems paying principal and interest on its debt in the past year?	30	9	30.0%
Has your establishment had to call for additional cash contributions from the owners in the past year other than for new investments?	30	14	46.7%
Is the establishment's survival dependent on continued cash contributions from the owners?	30	11	36.7%

⁷² This section of the report is based on a separate report by Environmental Resources Management, a consulting company. The summary of findings and conclusions for this report is presented in Appendix I. Parties authorized to receive the report may request copies from IFC's Operations Evaluation Group.

Source: Client survey

57. However, almost all companies see better times ahead. Approximately 97 percent of survey respondents expect that sales will increase over the next three years and 87 percent believe that the firm will be profitable three years hence as shown in Table 9.

Table 9. Business Outlook

Outlook	n	Number responding "yes"	Percent responding "yes"
Do you expect that the establishment's annual sales in FY2005 will be higher than they were in FY2002?	31	30	96.8%
Do you expect to be profitable three years from now?	31	27	87.1%

Source: Client survey

IV. Capacity Building – SMEs

Rationale

58. The ability of companies to compete effectively is based to a significant degree on the capabilities of their management. SEED determined that there was a need to upgrade the skills of managers of SMEs in various areas and that existing training institutions were not meeting this need. As such, SEED entered into the training market and began providing services directly to SMEs.⁷³

SEED's role

59. SEED has identified subjects that may be of interest to owners and/or managers of SMEs and has drawn on a number of sources to determine which courses to offer, including several sector studies commissioned by IFC and SEED as well as informal feedback from clients. The organization has taken the approach of offering a wide variety of training courses both in terms of their content, format, and duration. However, in each case, SEED has tried to emphasize skills that can be readily applied by participants in their own business.
60. SEED staff and outside consultants have shared responsibility for developing curricula and providing course instruction. In one instance, SEED drew on materials developed by another PDF in designing its own training programs: materials from the Mekong Project Development Facility (MPDF) were used as the basis for the development of SEED's human resource (HR) training programs.

Activities

61. SEED has offered 50 courses from its inception through 31 December 2002. Courses have dealt with a variety of subjects, including general management, financial management, strategic planning, and marketing. Some of these courses are designed to last four hours, while others provide more than 20 days of classroom training extending over several months.⁷⁴
62. Two intensive courses were designed for SME executives:
- **General Management Development Program (GMDP).** Taught by faculty from the American College of Thessaloniki, the course was presented in six four-day sessions carried out over a six-month period. The sessions covered financial management, marketing and sales, production and operations, human resources, and strategic planning. The first five sessions were held in Belgrade; the last session was held in Thessaloniki, Greece. The latter included visits to local businesses.
 - **Chief Financial Officer (CFO) Development Program.** The program was designed to upgrade the skills of financial managers. The nine-month course included 28 modules with each module ranging from two to eight hours in duration. The topics covered in the training

⁷³ In addition to providing services directly to SMEs, SEED has worked with intermediary organizations to boost their capacity to deliver services to companies in the region. This topic is dealt with in the next section.

⁷⁴ Details of training seminars are provided in the Appendix in Table B-1.

sessions were central to financial management, including accounting standards, auditing, time value of money, risk management, capital budgeting, and financing. Participants were invited to attend one or all of the sessions.

Training participants

63. According to SEED records, a total of approximately 1,952 participants have attended SEED training programs that have been directed to SMEs.⁷⁵ These participants have come from at least 200 companies.⁷⁶ Based on the results of the survey, companies that have participated in training programs can be characterized as follows:⁷⁷

- **Firm size.** On average, companies that responded to the survey had annual sales of approximately €2.4 million (median = €230,000) and employed 49 people (median=15). Virtually all (97 percent) met the WBG's SME definition, calling for sales to be no more than €15 million and employment to be no more than 300.
- **Ownership.** Approximately 77 percent of the companies that responded to the survey are fully owned by local private investors and roughly 86.5 percent have at least some local private investment. State enterprise/government owns an interest in only 8.3 percent of the responding companies and is a majority owner (more than 50 percent equity) in only 3.1 percent of the companies. Nine of the responding companies (9.4 percent) reported foreign investment – eight of those are fully owned by foreign investors.
- **Management.** Nearly all (96.9 percent) of the companies that responded to the survey are headed by permanent residents. In addition, 84.4 percent of respondents reported that the chief executive or joint chief executives were male; 15.6 percent reported that the chief executive or joint chief executives were female.
- **Industry distribution.** Based on survey results, it appears that the majority of firms sending participants to the capacity building for SME (CB-SME) training courses are engaged in either manufacturing (34 percent) or services (34 percent).⁷⁸
- **Geographical distribution.** The SMEs participating in SEED's training programs are spread fairly evenly among the four countries, though Serbia and Montenegro has accounted for a somewhat larger share than the others.⁷⁹

⁷⁵ Training programs directed toward SMEs have been classified under CB-SME and CB-BDS in the accounting system.

⁷⁶ For the survey effort, SEED was asked to provide a list of companies that received training during the study period. The list contained 219 companies. However, the exact number of companies that have participated in training programs offered by SEED is unknown.

⁷⁷ More detailed information on clients obtained through the survey is presented in Appendix Figures B-1 and B-2. SEED does not capture data on the characteristics of companies that have participated in training programs.

⁷⁸ Within manufacturing, food products and beverages comprise the largest sector, accounting for a total of 19 percent of SEED training clients. Representation in the service sectors is more spread out, with 5 percent of SEED training clients in computer and related service activities, and 19 percent in other business service activities. SEED has also provided training services to companies in construction, trade, and agriculture.

⁷⁹ See Appendix Table B-2.

Availability of alternative providers

64. Although some other organizations and companies provide similar training, SEED still fills an unmet need for most of the companies served. Of 91 companies responding to a question about the availability of alternative training service providers, approximately 41 percent reported that there were other companies or organizations that could have provided similar training services at the time they sought assistance from SEED. Respondents further reported that these other providers typically charge approximately €123 per participant per day (eight hours) of training.⁸⁰
65. When asked to provide an explanation for selecting SEED rather than other training service providers, more than half of respondents that were aware of other training providers reported that they believed that SEED could provide higher quality services than available elsewhere (Table 10). In addition, 46 percent of respondents reported that they believed that SEED would respond to their needs more rapidly than other service providers. Nearly thirty percent reported that they based their selection, in part, on price. Others indicated choosing SEED because of the particular subjects addressed by SEED seminars.

Table 10. Reasons for Selecting SEED for Training

Establishment selected SEED because... (N=37)	Agree	Disagree	Don't know
Believed that SEED could provide higher quality services than available elsewhere	54.1%	35.1%	10.8%
Believed that SEED would respond to our needs more rapidly than available elsewhere	46.0%	46.0%	8.1%
Believed that SEED's services were less expensive than available elsewhere	29.7%	59.5%	10.8%
Other reasons	40.5%	48.6%	10.8%

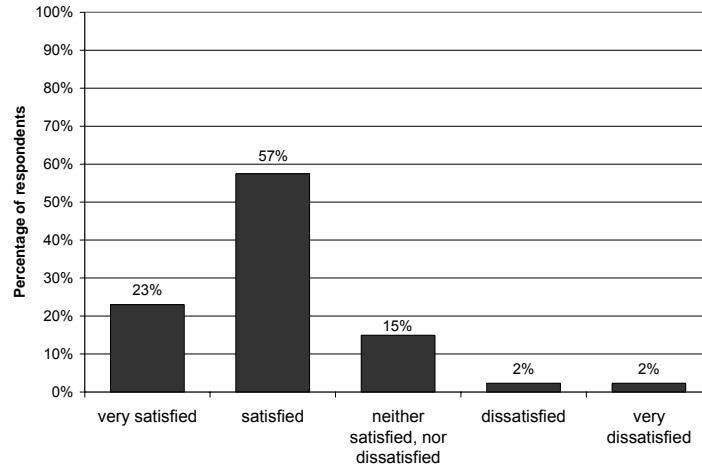
Source: Client survey

Satisfaction

66. As far as the companies that sent employees for training are concerned, approximately 80 percent of respondents reported that they were "very satisfied" or "satisfied" with the training services provided by SEED as shown in Figure 5. Fifteen percent were neutral in their opinion, and four percent were "dissatisfied" or "very dissatisfied" with the training services provided by SEED.

⁸⁰ Fifteen respondents provided training cost estimates from which this figure was calculated.

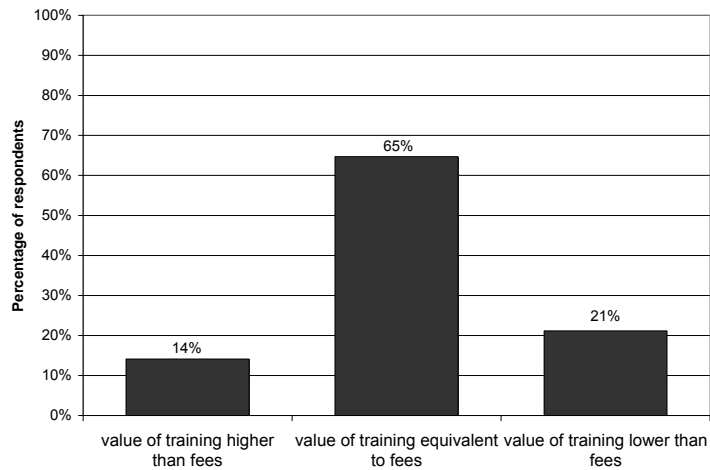
Figure 5. Satisfaction with SEED Training Services (n=87)



Source: Client survey

67. As shown in Figure 6, in terms of value for money, fourteen percent of respondents stated that the value of the training was greater than the fees charged, 65 percent indicated that the value was equivalent to fees, and 21 percent stated that the value was less than the training fees.

Figure 6. Perceived Value of SEED Training Services (n=85)



Source: Client survey

Impact of Training on SMEs

68. Most survey respondents reported value added from SEED training programs: approximately 87 percent of survey respondents indicated that they or their employees gained new knowledge or

skills as a result of the SEED training programs as shown in Table 11. Of these, 90 percent reported that the new knowledge or skills had been put to use at their establishment.

Table 11. Impact of SEED Training on Knowledge, Skills and Behavior

Changes in skills, attitudes, behavior, practices and new knowledge resulting from training services provided by SEED	n	Number responding "Yes"	Percent responding "Yes"
Did you or your employees gain new knowledge or skill as a direct result of the training services provided by SEED?	96	83	86.5%
Have the new knowledge or skills obtained as a direct result of the training services provided by SEED actually been put to use at your establishment?	83	75	90.4%

Source: Client survey

69. Eighty-four respondents (88 percent) stated that they had implemented changes in at least one aspect of their business as a direct result of the training services provided by SEED.⁸¹ In general, the most frequently reported changes are those that are directly associated with the training areas in which SEED focuses: marketing and sales, and financial management. In addition, approximately 46 percent of respondents noted improved performance along at least one dimension.⁸²
70. Overall 77.1 percent of respondents indicated that the training received from SEED increased the ability of the company to compete.⁸³ In some cases, improved competitiveness appears to have been manifest in enterprise-wide performance gains. Roughly 22 percent and 18 percent of respondents indicated that SEED's assistance resulted in higher sales or net profits, respectively, as shown in Table 12.

Table 12. Impact of SEED Training on Enterprise Performance

Is your establishment's performance in the following areas better than it would be without SEED's assistance?	(n=94)	Yes	No	Don't Know
Annual sales		22.3%	63.8%	13.8%
Net profit		18.1%	51.1%	30.9%

Source: Client survey

71. The survey also asked respondents to attempt to quantify the impact of SEED training on sales and employment. Specifically, it asked companies to estimate what the level of sales and employment in 2002 would have been if they had not received training services from SEED. The actual (observed) performance in 2002 was compared to the estimated performance in the

⁸¹ See Appendix Table B-3.

⁸² See Appendix Table B-4.

⁸³ Five companies indicated that without SEED assistance, the establishment would have gone out of business.

absence of SEED training services (i.e. the counterfactual) to gauge the impact of SEED's training services. As shown in Table 13, companies that responded to the survey indicated that training boosted their sales in 2002 by an average of about €1,300 (median = € 0) for a total of €46,800. With respect to employment, while the average reported gain was six workers, 73 percent of respondents reported no employment impact whatsoever. Across all respondents, companies reported employing 516 more workers as a result of SEED.

Table 13. Estimated Impact of Training on Sales and Employment

	n	Median	Mean	Std dev.	95% confidence interval	
Change in annual sales	36	0	1,300	4,500	-240	2,800
Change in employment	86	0	6	25.2	0.63	11.5

Source: Client survey

Future Expectations

72. Looking ahead, 84 percent of survey respondents expected that annual sales would be higher three years from now and approximately 77 percent expect to be profitable in three years.⁸⁴ However, a significant number of companies reported current cash flow problems, requiring owners to inject money into the firm for survival.

Development Impacts

73. Impacts on companies that have participated in training programs offered by SEED have implications for the broader economy:⁸⁵
- **Economic distortions.** Nearly 40 percent of SEED clients (38 out of 96 respondents) expressed the view that their financial performance had been “harmed” or “significantly harmed” by tariffs, quotas, government subsidies, or similar provisions. Approximately half (51 percent) of SEED’s training clients reported that they neither benefited nor were harmed by tariffs, quotas, government subsidies, or other special arrangements. Very few respondents (3.1 percent) reported that they had benefited from such arrangements.
 - **Exports.** SEED’s training clients tend to ship most of their products within their own countries. Over 93 percent of training respondents reported that they ship 70 percent or more of their products within their own country; two-thirds ship 100 percent of their products within their own country. More detailed information on the value of exports was provided by 60 of the respondents. On average, these clients had annual exports equal to approximately €143,000 (median = €0).

⁸⁴ 7.5 percent of respondents expect sales to be the same three years from now, 6.4 percent expect sales to be lower, and 2.1 percent responded that they did not know. See Appendix Table B-5.

⁸⁵ As noted in the section dealing with investment services, exporting increases national income and offers a means for companies in relatively small markets to benefit from economies of scale. With respect to competitors, to the extent that companies compete with other local firms for the same market there is a chance that one firm may gain market share at the expense of the other.

- **Competitors.** Most respondents reported that the majority of their competitors were located in their own country. Specifically, 100 percent of respondents in Albania (n=13) reported that all of their competitors were located in Albania. Figures of the other three countries are as follows: 83 percent for BiH (n=24); 75 percent for Serbia and Montenegro (n=28); 81 percent for FYMR (n=26).
- **Demonstration value.** It is often remarked that the training services provided by SEED have demonstration value, i.e., other companies will emulate the actions of SEED clients. As shown in Table 14, the survey results support this claim. Some respondents indicated that they knew of other firms that had followed their lead in seeking assistance from SEED or other outside providers of consulting and training services, and making changes in business strategies or operations, providing training to company personnel, and undertaking new investments in the country.

Table 14. Demonstration Effects

Do you know of other companies that have followed the lead of your establishment with respect to the following actions:	n	Number responding "Yes"	Percent responding "Yes"
Seeking assistance from outside providers of consulting and training services?	96	45	46.9%
Seeking assistance from SEED?	95	26	27.4%
Making changes in business strategies or operations?	96	26	27.1%
Providing or arranging training for managers, employees or workers?	96	23	24.0%
Making or planning new investments in the country?	95	21	22.1%

Source: Client survey

V. Capacity Building for Organizations that Serve SMEs

Rationale

74. SEED has undertaken various initiatives designed to help other organizations to develop and/or strengthen services aimed at small and medium-sized enterprises. Rather than SEED continuing to deliver services directly to companies in the target population, the intention is to build the capabilities of intermediary organizations that serve SMEs. In so doing, the aim is to develop the infrastructure needed to support a vibrant private sector, leveraging additional resources and avoiding potential distortionary impacts on markets.
75. To some extent, this effort grows out of a broader movement among donors to promote the development of business development services (BDS). Analogous to accepted best practice in the field of microfinance, the BDS approach stresses the importance of the commercial orientation and financial sustainability of service providers. Interventions are expected to be short term, with a clear exit strategy defined from the outset.⁸⁶

SEED Activities

76. Through the end of December 2002 (Q2FY03), SEED devoted slightly more than 75 percent of its total capacity building expenditures for business development services to local consultants, business associations, and local economic development organizations.⁸⁷ The following sections discuss SEED activities and associated impacts in each of these areas.

Development of Local Consultants

Rationale

77. From its inception, SEED has been interested in fostering the development of local consultants to help meet the needs of SMEs in the countries in which it operates. The development of local consultants is seen as a means to expand the reach of SEED and pave the way for the establishment of a sustainable market for consulting services.
78. According to SEED, local firms typically lack experience in managing consulting practices and do not offer services of sufficient quality to attract and retain clients. To help address this deficiency, SEED has provided a broad spectrum of classroom and on-the-job training to local consultants.

Role of SEED

79. The responsibility for these capacity building efforts is divided among all three strategic-objective-operating teams within SEED.

⁸⁶See Committee of Donor Agencies for Small Enterprise Development, *Business Development Services for Small Enterprises: Guiding Principles for Donor Intervention, 2001 Edition*, World Bank Group, SME Department, February 2001.

⁸⁷ SEED has provided training to five financial institutions under the rubric of CB-BDS. See Appendix Table C-1.

80. The IS team is responsible for developing the capacities of local consultants by integrating them in SEED's work on assignments for IS clients. It focuses its efforts on sixteen local consulting firms selected to form SEED's Consultancy Network.
81. SEED has offered eleven courses that address various business issues in consulting firms.⁸⁸ Led by the PSD team, these efforts have included a series of three-day training seminars entitled, "Development of Consulting as a Business." The seminars cover the stages of development of a consulting practice and issues related to general management, human resource management, and financial management. The courses have been taught by instructors from FIRMA 2000, a private consulting company in Poland that specializes in training consultants and providing consulting services to SMEs. They have also included courses designed to enhance the marketing capabilities of consulting firms. According to SEED records, 353 participants have attended these courses.
82. SEED has also provided 11 train-the-trainer courses for consultants.⁸⁹ According to SEED records, there have been 153 participants at these courses. The aim of the train-the-trainer courses is to train consultants so that they can deliver standardized training programs developed by SEED to their own clients. While SEED staff have taught some classes, responsibility for curriculum development and actual instruction typically lies with consultants retained by SEED expressly for this purpose. Subjects have covered executive management, strategic planning, marketing, human resource management, and accounting. The Financial Management (FM) team is also responsible for providing a number of training courses under the Entrepreneurship - Faculty Development Program. Aimed at professors and students at universities throughout the region, the intention of the program is to foster entrepreneurship, enhance adult education, and strengthen services available to firms. Finally, some consultants have also attended courses offered for owners and managers of SMEs.

Description of participating consulting firms

83. As noted above, the Consultancy Network consists of 16 companies. The Consultancy Network was launched in Macedonia in June 2001. Twenty-six firms applied for the program. SEED developed a short list consisting of seven firms following a training workshop for applicants, and subsequently signed Partnership Agreements with three firms in Macedonia that were deemed to be the strongest. Since then, the Consultancy Network has been expanded to include 16 firms selected through a competitive process. These firms are located in all four countries in which SEED operates. An additional 48 consulting firms have participated in one or more training programs offered by SEED.
84. Most of the companies that have participated in the Consultancy Network or various training programs sponsored by SEED offer a mix of consulting and training services.⁹⁰ The majority of these firms were established after 1995, while one-third of the firms were founded within the past three years.⁹¹ Members of the Consultancy Network tend to be newer than other organizations that have participated in SEED programs— about 44 percent of the Consultancy Network was

⁸⁸ See Appendix Table C-2.

⁸⁹ See Appendix Table C-3.

⁹⁰ See Appendix Table C-4.

⁹¹ See Appendix Table C-5.

founded in the period from 2000 through 2002, while about a third was founded prior to 1995. In contrast, almost half of the non-network consultants i.e., those consultants that attend training, were founded prior to 1995, with only 24 percent founded since 2000.

85. As a group, companies that receive services from the CB-BDS team tend to be quite small. On average, companies that responded to the survey employed 13 people (median = 6). Respondents reported average annual revenues of approximately €103,500 (median = €59,000).⁹² The largest firm, in terms of revenues, reported annual sales of just under €900,000 in 2002. Companies indicated that they typically charge €36 per hour (median) for consulting services and €247 (median) per participant-training day for training services.⁹³
86. While small, 44 percent of the consultants that responded to the survey maintain some type of affiliation with an international counterpart.⁹⁴ These affiliations tend to be informal. International firms have an equity interest in only three of the firms that responded to the survey – in all three cases, international firms hold a controlling interest in the companies. Two of these three particular firms were members of the consultancy network.
87. Services deal with a broad range of subjects. However, there are differences between members of the Consultancy Network and other firms. For example, while 94 percent of the members of the Consultancy Network offer services related to finance and financial management, only 16 percent of non-network companies offer services in the same area. Similarly, 75 percent of the Consultancy Network members provide strategic planning services, whereas 48 percent of the non-network companies offer services that deal with this subject. Firms that are not part of the Consultancy Network are more likely to offer services related to information systems—56 percent as compared to 25 percent for members of the Consultancy Network.⁹⁵
88. In terms of clientele, as illustrated in Table 15, the majority of the companies report that they provided services to SMEs prior to their interaction with SEED.

Table 15. Services Provided to SMEs Prior to Interaction with SEED

	Did the company provide consulting or training services to small and medium-sized enterprises prior to its involvement with SEED?		
	Yes	No	Don't know
All respondents (n=41)	75.6	14.6	0.0
Consultancy Network (n=16)	87.5	12.5	0.0
Non-network Clients (n=25)	68.0	32.0	0.0

Source: Consultant survey

⁹² It should be noted that some of these consultants offer consulting services on a part-time basis or have other lines of business. As such, they are not dependent solely on consulting revenues.

⁹³ See Appendix Table C-6 for further detail regarding employment and revenue.

⁹⁴ See Appendix Table C-7.

⁹⁵ For further detail on the types of consulting and training services offered by these firms, see Appendix Table C-8.

89. Moreover, SMEs represent a significant segment of the total volume of business.⁹⁶ On average, SMEs accounted for almost 35 percent of the total revenue in 2002, while large firms accounted for about 22 percent of revenues. Approximately five percent of respondents (two firms) indicated that all of their clients were SMEs.

Satisfaction with assistance provided by SEED

90. Approximately two-thirds of the companies that responded to the survey expressed some degree of satisfaction with the assistance provided by SEED (Table 16).

Table 16. Satisfaction with Services Provided by SEED

Response	All Respondents (n=41)	Consultancy Network (n=16)	Non-network Clients (n=25)
Very satisfied	22.0%	6.3%	32.0%
Satisfied	43.9%	62.5%	32.0%
Neither satisfied, nor dissatisfied	24.4%	31.3%	20.0%
Dissatisfied	2.4%	0.0	4.0%
Very dissatisfied	2.4%	0.0	4.0%
Don't know	4.9%	0.0	8.0%
Total	100.0%	100.0%	100.0%

Source: Consultant survey

91. In general, companies see SEED as an organization that is interested in collaboration as opposed to competing head-on.⁹⁷ Four companies (25 percent) of the Consultancy Network reported that they considered SEED both a collaborator and a competitor. On the one hand, these companies serve as subcontractors on SEED assignments; on the other hand, these companies recognize that they vie with SEED for consulting and training business in their respective markets.

Impact of SEED's assistance on participating consulting firms.

92. As indicated in Table 17, most consulting companies reported that there were no other organizations that could have provided assistance that was similar to that offered by SEED.

⁹⁶ See Appendix Table C-9.

⁹⁷ See Appendix Table C-10. There was no statistically significant difference with regard to the perception of SEED as a collaborator and/or competitor between consultancy network firms and non-network firms.

Table 17. Presence of Service Providers Similar to SEED

	Were there other companies or organizations that could have provided assistance to your company similar to the assistance provided by SEED?		
	Yes	No	Don't Know
All (n=41)	36.6%	61.0%	2.4%
Consultancy Network (n=16)	43.8	56.2	0.0
Non-network Clients (n=25)	32.0	64.0	4.0

Source: Consultant survey

93. SEED has had an impact on the consulting firms that are members of the Consultancy Network by sheer virtue of hiring them as subcontractors on assignments for SEED clients. In this regard, SEED has negotiated lower rates for services offered by members of the network. Roughly 88 percent of these companies indicated that the fees that SEED pays for services are, on average, 41 percent lower — than the fees that they receive from other clients. The remaining 12 percent reported that fees were the same. Moreover, 75 percent of the firms reported that profit margins were, on average, 37 percent lower on assignments with SEED compared to those for other clients.
94. So why do companies agree to participate in the network? First, while fees for SEED assignments may be lower, companies may elect to work with SEED given excess capacity – the opportunity cost of working with SEED may be virtually nil. Second, since SEED serves as the prime contractor, the transaction costs and risks otherwise borne by consulting firms may be reduced. Finally, companies may believe that their involvement with SEED will lead to additional sales down the line as a result of the imprimatur granted by SEED and/or actual experience gained through their interactions with SEED. As discussed below, all of these statements have some truth.
95. Interviews with companies suggested that some firms are struggling to keep staff fully employed on consulting and/or training assignments. As such, the work provided by SEED represents a net addition to these companies' annual revenues. For the companies that reported revenues in 2002, on average, roughly €3,300 was earned on assignment for SEED. Correspondingly, the average share of SEED-generated revenue in 2002 for these firms was about 5 percent, while the median was about one percent.
96. Furthermore, companies report that SEED has reduced the cost of doing business and associated risks. For example, approximately half of the members of the Consultancy Network indicated that their interactions with SEED has led to reductions in the cost of identifying potential clients and led to reductions in the likelihood of nonpayment.⁹⁸
97. Moreover, seven members of the Consultancy Network (44 percent) indicated that one or more of SEED's clients subsequently hired their firm to provide consulting and/or training services independent of SEED. These companies, on average, sold services to roughly two of SEED's

⁹⁸ See Appendix Table C-11.

clients – conceivably, the cost of client acquisition in these instances was lower than it would have been given the familiarity that the customers gained by working with the consulting firm on previous assignments sponsored by SEED.

98. In addition, almost two-thirds of all respondents reported that the company had provided services to their own clients based on the content and/or techniques taught by SEED. However, there is a marked difference between members of the Consultancy Network and those firms that only participated in the training programs offered by SEED.⁹⁹ Whereas almost 94 percent of members of the Consultancy Network reported using SEED materials with their own clients, only 44 percent of the other clients (non-network) indicate doing so, despite the fact that many of these companies participated in train-the-trainer courses offered by SEED.
99. To date, 23 of the 26 companies that reported using SEED content and/or techniques with their own clients have used these materials with an average of roughly 10 clients. However, the results are highly skewed. Fifty percent of these 23 firms report using what they learned from SEED with three or fewer clients. Some reported greater success – several firms reported that they had delivered services based on SEED training to 20 or more of their own clients. The median number of clients for which SEED content was employed by Consultancy Network members was five – twice the number reported by other organizations.¹⁰⁰
100. As noted above, most companies report that they worked with SMEs prior to the interactions with SEED. Despite their previous work with SMEs, most respondents (61percent) reported that they “gained greater knowledge of the needs of SMEs” through their interactions with SEED.¹⁰¹ However, while more than half of the members of the Consultancy Network indicated that they introduced new products designed specifically for SMEs as a direct result of working with SEED, only 28 percent of the organizations that just received training from SEED reported doing so.
101. Responses to other questions in the survey present a similar picture. Almost all of the respondents (88 percent) stated that they had implemented changes in at least one aspect of their business as a direct result of their interaction with SEED. The most frequent change carried out by companies was “developing new or improving existing services” – approximately 81 percent of firms that responded to the survey reported making such changes. Of the firms that reported that the objective of SEED assistance was to develop new or improve existing services, 94 percent actually carried out such changes.¹⁰²
102. In addition, roughly 42 percent of respondents indicated that they changed their approach to marketing and sales and half reported adopting a new method of after sales service. About 42 percent of companies also reported changing the manner in which they carry out projects. The most marked differences between members of the Consultancy Network and other firms revolved around changing the range of services offered and entering new markets. While almost 63 percent of the Consultancy Network reported that they had changed the range of services offered as a result of SEED interaction, only 20 percent of non-network firms reported they had made such changes. This difference may correspond to differing objectives with respect to the interactions that companies had with SEED. Whereas 63 percent of companies that participate in

⁹⁹ See Appendix Table C-12.

¹⁰⁰ See Appendix Table C-13

¹⁰¹ See Appendix Table C-14.

¹⁰² More details are provided in Table C-15.

the Consultancy Network responded that changing the range of services offered was an objective of involvement with SEED, 28 percent of other firms reported that this was an objective of their SEED interaction. With respect to entering new markets, about 44 percent of Consultancy Network members reported carrying out changes in this area, while in contrast, 16 percent of non-network members entered new markets as a result of their interactions with SEED. This difference is significant given that roughly the same percentage of firms expressed that this was one of the objectives of working with SEED.

103. Approximately 76 percent of respondents noted improved performance along at least one dimension of their operating performance.¹⁰³ Members of the Consultancy Network were less likely to report improved performance than firms that only participated in training programs offered by SEED.
104. As indicated in Table 18, just under 44 percent of respondents reported that the assistance provided by SEED resulted in higher annual sales and 39 percent reported higher profits due to their involvement with SEED.¹⁰⁴

Table 18. Impact of SEED Assistance on Sales and Profits of Consulting Firms

Response	All Respondents (n=41)	Consultancy Network (n=16)	Non-network Clients (n=25)
Higher annual sales	43.9%	37.5%	48.0%
Higher net profits	39.0%	31.3%	44.0%

Source: Consultant survey

105. Companies that responded to the survey and attempted to quantify the impact of interaction with SEED on revenue indicated that SEED's assistance boosted their sales in 2002 by an average of roughly €2,800 (median = 0).¹⁰⁵ While a smaller percentage of Consultancy Network members reported a sales impact than other firms, the magnitude of the sales impact is higher. On average, members of the Consultancy Network reported that their sales in 2002 were roughly €5,300 (median = €480) higher than they would have been in the absence of SEED. In contrast, non-network clients reported an average impact of about €647 (median = 0).¹⁰⁶ In interpreting this finding, it is important to remember, however, that members of the Consultancy Network received payment directly from SEED for services delivered in 2002.

¹⁰³ See Appendix Table C-16.

¹⁰⁴ The difference between members of the Consultancy Network and other companies is not statistically significant.

¹⁰⁵ See Appendix Table C-17.

¹⁰⁶ The respective p-values for sales impacts for the different groups are as follows: *all respondents*, p=0.02 (statistically significant); *consultancy network*, p=0.01 (statistically significant); and *other organizations*, p=0.24 (not statistically significant). The difference in additional revenues between members of the network and non-network firms of about €4,655 is statistically significant. The p-value for the test of a difference in the means between these two groups is 0.02 (statistically significant).

Sustainability of consulting firms and the provision of services to SMEs

106. As shown in Table 19, roughly 46 percent of respondents believe that SEED had a great or moderate impact with regard to the expansion of the demand as well as the supply of consulting and training services.

Table 19. Extent to which SEED’s Activities Have Resulted in a Permanent Expansion of the Market for Consulting Services

Market Impacts	n	Extent			
		Great extent	Moderate extent	Minimal extent	Not at all
Permanent expansion in the <i>supply</i> for consulting and training services	41	14.6%	31.7%	36.6%	17.1%
Permanent expansion in the <i>demand</i> for consulting and training services	41	12.2%	34.1%	29.3%	24.4%

Source: Consultant survey

107. Several factors limit the growth of consulting firms in the region, particularly with respect to the SME market. According to those surveyed, the overarching constraint on the development of the market is the unwillingness or inability of SMEs to pay for services at current prices. As shown in Table 20, more than eight of ten consultants responded that SMEs were not willing or were unable to pay for services. Of these respondents, almost 95 percent suggested that this factor had limited the growth of their firms to a “great” or “moderate” extent. Significantly, the growth of consulting firms is limited by difficulty in finding qualified staff. Here, 61 percent of consultants that responded to the survey reported difficulties in finding qualified staff and 88 percent of these firms indicated that this factor had limited the growth of their firms to a “great” or “moderate” extent.

Table 20. Factors Limiting Growth of Consulting/Training Firms

To what extent does this factor limit the growth of the consulting and training services your company provides to SMEs?

Factor	Breakdown of “Yes” Respondents						
	% Yes	“Yes” response n=	Great extent	Moderate extent	Minimal extent	Not at all	Don’t know
SME are not willing or able to pay for services at prevailing prices	82.9%	34	55.9%	38.2%	5.9%	0.0%	0.0%
Higher returns for delivering services to large enterprises	78.0%	32	12.5%	18.8%	18.8%	15.6%	34.4%
Difficulty getting paid for services	63.4%	26	34.6%	38.5%	26.9%	0.0%	0.0%
Difficulty finding qualified staff	61.0%	25	44.0%	44.0%	8.0%	4.0%	0.0%
High costs in identifying potential clients	51.2%	21	38.1%	61.9%	0.0%	0.0%	0.0%
Legal or regulatory barriers	22.0%	9	33.3%	22.2%	44.4%	0.0%	0.0%

Source: Consultant survey

108. When asked to comment on the factors that contribute to the reluctance of SMEs to use consulting services, firms pointed to a broad range of issues as shown in Table 21. About 93 percent of respondents reported that the main factor limiting SME demand for consulting services is that SMEs have difficulty identifying their needs; roughly 95 percent of these respondents believed that this issue limited demand for services to either a “moderate” or “great extent.” Respondents reported that another significant issue limiting the demand for consulting services by SMEs is the lack of information on the quality of services provided by particular providers. In this case, all of these respondents believed that this factor limited the demand for services to either a “moderate” or “great extent.”

Table 21. Factors Limiting Demand for Consulting/Training Services by SMEs

Small and medium-sized enterprises...	n=41		Breakdown of “Yes” Respondents				
	% Yes	“Yes” response n=	Great extent	Moderate extent	Minimal extent	Not at all	Don’t know
Have difficulty identifying their needs	92.7%	38	52.6%	42.1%	2.6%	2.6%	0.0%
Lack information on the quality of services provided by particular providers	85.4%	35	54.3%	45.7%	0.0%	0.0%	0.0%
Have difficulty managing consulting or training projects	78.0%	32	50.0%	43.8%	6.3%	0.0%	2.4%
Have difficulty putting recommendations offered by service providers into action	75.6%	31	32.3%	58.1%	3.2%	6.5%	0.0%
Have difficulty affording services	73.2%	30	73.3%	23.3%	0.0%	0.0%	3.3%
Have difficulty negotiating a work plan and budget with service providers	73.2%	30	53.3%	33.3%	10.0%	3.3%	0.0%
Have difficulty finding service providers that are qualified to meet their needs	68.3%	28	39.3%	57.1%	3.6%	0.0%	0.0%
Are unaware that there may be service providers that could address their needs	63.4%	26	61.5%	38.5%	0.0%	0.0%	0.0%

Source: Consultant survey

109. Nonetheless, virtually all (97.6 percent) of the companies that responded to the survey indicated that they plan to continue to offer consulting and/or training services to SMEs in the future as

shown in Table 22. All of the firms that offered services to SMEs prior to SEED's assistance reported they would continue to do so. Moreover, interaction with SEED seems to have encouraged some consulting firms to offer services to SMEs. Of the 24 percent of companies that indicated that they had not offered consulting and training services to SMEs prior to their involvement with SEED, 90 percent said they plan to offer such services to SMEs in the future.

Table 22. Plan to Offer Consulting /Training Services to SMEs

	Offered Consulting/Training to SMEs Prior to SEED Interaction (%)	Plan to continue offering Consulting/Training Services to SMEs Subsequent to SEED Interaction (%)
All (n=41)	75.6	97.6
Consultancy Network (n=16)	87.5	100.0
Non-network Clients (n=25)	68.0	96.0

Source: Consultant survey

110. Moreover, the majority indicated that they plan to use materials developed by SEED in future assignments with their own clients as shown in Table 23.

Table 23. Future Use of SEED Content and Techniques with Clients

	Yes	No	Don't Know
All (n=41)	85.4%	14.6%	0.0%
Consultancy Network (n=16)	93.8%	6.2%	0.0%
Non-network Clients (n=25)	80.0%	20.0%	4.0%

Source: Consultant survey

111. Finally, with respect to sustainability, it is important to note that most of the companies that responded to the survey are growing and 87 percent of companies indicated that the firm was profitable in 2002. Of the 61 percent of firms that reported revenues for 2001 and 2002, the median growth rate in sales was 17.6 percent.

Development of Business Associations¹⁰⁷

Rationale

112. Business associations are a recent phenomenon in the region.¹⁰⁸ Heretofore, chambers of commerce served as the officially sanctioned voice of business in all four countries. The chambers

¹⁰⁷ This section of the report draws on interviews with SEED staff and representatives of business associations as well as written reports prepared by Canadian Manufacturers & Exporters.

tend to be dominated by large, state-owned enterprises and are not seen as being particularly aggressive in serving the needs of private firms. Business associations may offer a vehicle for establishing quality standards, undertaking group marketing efforts, purchasing products and services at discounts, delivering training services, and advocating the interest of members.

113. While laws have been passed in the region that make it easier to establish business associations, these organizations typically lack the experience and capacity to provide services to members or contribute effectively to policy debates within their countries.¹⁰⁹ In most cases, the associations tend to have few members and fees are not sufficient to support permanent secretariats. Associations need support to build their membership base, establish member services, and develop the capability to advocate member interests within the halls of government.

Role of SEED

114. SEED has been active in promoting business associations. It has advocated for changes in government policy, produced various publications, and held seminars related to business associations. With regard to the latter, in June 2002, SEED, in cooperation with Lex International, made five presentations in different parts of BiH (Sarajevo, Mostar, Tuzla, Zenica and Banja Luka) on how to establish a business association in BiH under the new law. The presentation noted the potential benefits of business associations and highlighted key elements of the new law, particularly with respect to registration.
115. However, the bulk of SEED's efforts has centered on working with selected business associations in four countries. The initial work in this arena dates back to late 2000. SEED, in conjunction with the IFC-SME Department, retained Canadian Manufacturers & Exporters (CME) – a business association headquartered in Ottawa – to undertake a pilot project with the following recently established business associations in BiH:¹¹⁰
- Employers' Confederation of the Federation of Bosnia and Herzegovina,
 - Employers' Confederation of the Republic of Srpska,
 - Association of Women Entrepreneurs (UNA),
 - Association of Textile Entrepreneurs (UNOTEX¹¹¹); and
 - Association of Wood Processors and Furniture Manufacturers of the BiH (DVRO).
116. Field work was carried out over an 18-day period in December 2000 by two CME representatives. The two met in a series of working sessions with association representatives, government officials, and the media in Sarajevo and Banja Luka. The meetings focused on membership development, fund raising, public relations, and policy formulation and advocacy.

¹⁰⁸ Until recently, membership in the chambers was compulsory for all businesses in BiH. Fees were based on the number of employees and were paid to a central Payments Bureau within the government, which in turn handed them to the local Chamber. In fact, according to SEED management, the organization played a role in ending mandatory membership by working with IBRD to include this reform as a condition of the Business Adjustment Credit (BAC) and through subsequent discussions with the OHR (The Office of the High Representative) and government officials.

¹⁰⁹ For example, the Parliamentary Assembly of Bosnia and Herzegovina (BiH) passed the *Law on Associations and Foundations of Bosnia and Herzegovina* in 2001 (effective January 5, 2002). The Law provides the regulations pertaining to the establishment, registration, and operations of associations, including business associations in BiH.

¹¹⁰ CME was known as the Alliance of Manufacturers & Exporters Canada until October 2000.

¹¹¹ Both UNA and UNOTEX maintained informal organizations in both the Republic of Srpska and the Federation of Bosnia and Herzegovina.

117. The final report issued in February 2001 presented an overview of the environment for business association in Bosnia and Herzegovina, identified issues that needed to be addressed to strengthen associations, presented action plans for each of the associations, and offered recommendations to SEED concerning the continued role that it might play in this regard.¹¹² The report noted that the organizations needed significant assistance, particularly with respect to membership development and advocacy work. It suggested that SEED continue to work with each of the business associations on specific issues and, in general, promote the development of association in BiH. Specifically, the report contained recommendations for SEED to follow-up in six areas:

- Assist in the dissemination of reports, documents and other written materials to members and other parties;
- Support the implementation of communication strategies, including media plans;
- Provide advice on speakers and help arrange logistical support for meetings;
- Provide recommendations related to advocacy and help arrange meetings with appropriate government officials;
- Provide training to association management and staff ; and
- Discuss the findings of the consultancy report with other organization such as USAID that have an interest in the success of new business associations.

118. With the exception of the Employers Confederations, SEED has not provided further assistance directly to individual business associations in BiH. Moreover, even in the case of the Employers Confederations, follow-up assistance was not provided until October 2002 – some 20 months after the submission of the CME report – when a new effort was taken to revitalize SEED’s efforts in this field.¹¹³

119. Renewed efforts to promote the development of business associations began with an assessment of the capacity of existing business associations in the region. Working with staff of IFC’s Private Enterprise Partnership (PEP), SEED conducted interviews with roughly 30 associations in four countries to gauge their potential for becoming effective business organizations. SEED selected six associations that were seen as showing the “most promise” of developing into key players in the development of their countries and becoming long term partners of SEED.¹¹⁴ The associations selected for the initiative are listed in Table 24 along with an assessment of the stage of development of the organizations at the project’s inception. It is important to note that two of the associations – Association of Bee Keepers and Association of Mushroom Growers – were considered fledgling organizations. While the prospects for these organizations may have been more

¹¹² The report also contained documents and information of use to the associations. Included were: draft association brochures, example of an annual media contact plan, example of a constitution and by-laws for an association, and an example of an inter-association agreement.

¹¹³ SEED management explains that the delay in following-up on the initial work was due to a number of factors. First, SEED did not promise to continue to work with the associations. Second, SEED found out that proposed work plans were not being adopted when it contacted the associations roughly six months after the report was issued. Third, in the interim, SEED had turned its attention to developing and rolling-out seminars on the process of registering a business association. Fourth, a great deal of effort during this time was devoted to opening new offices. Finally, it took time to organize and launch the new business association initiative in concert with PEP.

¹¹⁴ In practice, SEED selected eight associations, but subsequently dropped two.

uncertain, given the importance of these agricultural products to the regional economy and the interest expressed by members in strengthening their respective organizations, PEP and SEED believed that investment in these associations was warranted. While a number of international organizations were working with business associations in the four countries, for the most part, none have provided support to the specific associations that SEED has elected to assist.¹¹⁵

Table 24. Business Associations Chosen for CME Assistance

Name of Association	Country	Stage of Development
Association of Bee Keepers	FYR Macedonia	Fledgling
Association of Mushroom Growers	FYR Macedonia	Fledgling
Association of Small and Medium Private Enterprises and Entrepreneurs, Vrsac	Serbia and Montenegro	Fledgling to nascent
Employers Confederation, Republic of Srpska	Bosnia and Herzegovina	Nascent
National Construction Business Association	Albania	Mature
Union Cacak 2000	Serbia and Montenegro	Fledgling to nascent

Source: CME report

120. Following the selection process, SEED and the SME Department contracted CME in October 2002 to assist the six associations to develop plans aimed at increasing their effectiveness with respect to membership growth, member services and advocacy. The objective of this assignment was “to help create action plans for the associations to increase their capacity to represent the business community and to become long term, stable partners for SEED.” In the fall of 2002, the six associations participated in training seminars designed by CME to help organizations increase their operational capabilities. Held over three or four days, the seminars focused on helping each association develop a vision and mission statement, delineate specific business objectives, and draft detailed plans and operating budgets. Each association developed short and long-term strategic plans aimed at increasing effectiveness in the fields of advocacy, membership growth, and member services.¹¹⁶ SEED staff actively participated in these meetings.

121. Following the training program, SEED entered into “partnership agreements” with these associations based, to a great extent, on the plans developed during the seminars and delineated in the final CME report.¹¹⁷ Under the agreement, SEED has committed funds on a matching basis to support specific activities designed to increase membership, provide member services, and

¹¹⁵ The Employers Confederations in the Federation of Bosnia and Herzegovina and in the Republic of Srpska both received support in their initial stages of development from USAID; this assistance ended in June 2001. The Center for International Private Enterprise (CIPE), an affiliate of the U.S. Chamber of Commerce, has been working with associations in the region with support provided by USAID. However, it has not worked with the associations selected by SEED.

¹¹⁶ See *Business Association Capacity Building in South East Europe*, Canadian Manufacturers & Exporters, 26 November 2002.

¹¹⁷ SEED may want to consult with IFC’s Legal Department regarding the use of the term “partnership agreement.”

advocate member interests in various fora. Where needed, this has been coupled with further technical assistance.

Impact

122. Based on interviews with SEED staff and representatives of the business associations, it is fair to say that the impact of SEED's work in BiH in late 2000 and early 2001 was minimal in terms of increasing the capacity of the associations to attract members, provide needed services, and advance the interest of SMEs within various policy forums. While the initial training efforts in BiH were well received, there was virtually no further assistance provided to the organizations. Faced with a limited membership base, modest financial resources, and having to rely on volunteers, most of the business associations in BiH remain as informal organizations with little effect in terms of serving members or influencing policy. This conclusion appears to be supported by SEED's own decision to refrain from providing further support to any of the organizations with which it has previously worked, except the Employers Confederations in the Republic of Srpska under its new initiative. For example, UNA and UNOTEX still have neither a permanent secretariat, nor dues-paying members. Their activities center on occasional meetings of companies in conjunction with the Star Network – a USAID-sponsored organization that works with women from business, political parties, trade unions and government.
123. Based on the lessons learned from these initial activities, SEED redesigned its approach to working with business associations and launched a new initiative. While this new phase of work had only just begun when the fieldwork for the evaluation was undertaken, it had already met with some success. The evaluation team reviewed project files and met with senior representatives of four associations that have received SEED support. These associations represent all four countries in which SEED operates and span the range from fledgling to mature organizations. Each of the associations highlighted the role that SEED played in helping to develop strategic plans and mount membership campaigns. In all four cases, membership has increased and the associations are beginning to provide greater services to companies. Still, given the number of members and current dues structure, the financial viability of most associations appears questionable. SEED, however, is continuing to work with these associations to strengthen their operations and establish a more solid foundation for future growth.¹¹⁸

Local Economic Development Strategies in Bosnia and Herzegovina

Rationale

124. The ability of companies to compete effectively is dependent, in part, on conditions within local communities. The nature of local infrastructure and services, labor markets, and government policies and regulations affect the ability of companies to start, survive and prosper.
125. Communities can promote the development of firms by adopting economic development strategies that respond to the needs of companies and take advantage of opportunities afforded

¹¹⁸ A profile of each of these associations together with an assessment of the role and impact of SEED is presented in Appendix Tables C-18 through C-21.

by the comparative advantages of the region. However, local governments in the region have little experience in fostering the private sector; they lack the tools needed to identify needs and opportunities, define clear objectives, and fashion an appropriate strategy.

126. In response, SEED initiated a pilot effort to work with entrepreneurs, government officials and other civic leaders in selected municipalities in BiH to develop and implement coherent economic development strategies targeted toward SMEs.

Role of SEED and activities

127. SEED began working with municipal governments in BiH soon after its inception. A chronology of major events is presented in Table 25.

Table 25. Chronology of SEED work with Municipal Governments in Bosnia and Herzegovina

Date	Event
Late 2001	Initial interviews and workshops with municipal leaders
March 2002	Partnership Agreement signed with Prijedor and Zenica
July 2002	Final reports submitted – Phase 1 completed
March 2003	Work on Phase 2 initiated

Source: Project files and interviews

128. Following a series of interviews with local officials, entrepreneurs and other civic leaders, SEED, in conjunction with a specialist from the World Bank, held a workshop in the RS and in the FBiH to discuss factors constraining the growth of the private sector and steps that local communities could take to address these issues. The latter was based, in part, on case studies of local economic development initiatives in England, Slovenia, and Bosnia. The Bosnia case studies were based on work undertaken by the EU Quick Impact Facility (QIF). SEED also outlined its plans to assist local economic development efforts of municipalities as part of a pilot program. Municipalities were asked to submit a one-page application for assistance, laying out the proposed initiatives.
129. According to SEED, representatives from 20-30 municipalities in the two entities attended the workshops. After 15 days or so, SEED had received six or so proposals from municipalities in BiH; however, none of the proposals dealt with local economic development efforts. Rather, the proposals addressed the needs of returnees, the construction of kindergartens and other aspects of the social infrastructure.
130. In response, the project manager at SEED drafted a proposal focusing on strategy development and circulated it among the municipalities that had submitted applications. The proposal prepared by SEED outlined an approach for assessing the needs of entrepreneurs, conducting a SWOT (Strengths-Weaknesses-Threats-Opportunities) analysis, creating a vision for the community, and identifying priority projects to promote the development of SMEs. Municipalities were asked to pay US\$10,000 and provide additional in-kind contributions valued at US\$25,000 or more. This could include the time of two to three municipality employees that would be dedicated to the

project, office space and equipment, and logistic support to different events (workshops, seminars, roundtables, etc).

131. According to the SEED program manager, all of the municipalities expressed an interest in participating in the program. However, SEED only had resources available to commit to two municipalities and selected Zenica (FBiH) and Prijedor (RS) for a pilot project. These are both relatively large municipalities that had witnessed substantial layoffs in mining and industrial sectors. Both were dependent on several large companies for the bulk of employment and these firms were operating well below their pre-war capacity and struggling to stay afloat. However, both communities were seen as having a substantial base on which to build and leaders, particularly Mayors, who were committed to local economic development.

132. Work with both of the municipalities began in March 2002. Early activities centered on establishing an executive committee and working groups, along with specific work plans. As part of the process, numerous roundtables and workshops were conducted in each municipality. The meetings were used to elicit people's feelings about the needs of entrepreneurs as well as educate them with respect to the options available to address these needs. As part of this process, SEED commissioned the preparation of a survey of entrepreneurs in each municipality. In both cases, the survey was conducted by consultants drawn from the faculty from the Business Development Center, Ljubljana University (Zagreb).¹¹⁹ The consultants were also charged with the responsibility for facilitating meetings and preparing a report summarizing the results of Phase 1.¹²⁰ The report presented a proposed vision statement for the municipality and identified a series of projects deemed to be high priority by the respective working groups as shown in Table 26. As noted, the vision statement and priority projects are similar for both municipalities.

Table 26. Vision and Priority Projects for Selected Municipalities

	Municipality	
	Zenica	Prijedor
Vision statement	In ten years, Zenica will become a dominant business center in BiH	Prijedor will become the center of development activities of the north-west part of BiH.
Priority projects	<ol style="list-style-type: none"> 1. One-stop-shop/development agency 2. Financial support fund 3. Business incubator 4. Business zones 5. Scientific/technological park 6. Development projects in agriculture 7. Promotion of entrepreneurship 8. Education and training 	<ol style="list-style-type: none"> 1. One-stop-shop / development agency 2. Financial support fund 3. Business incubator 4. Business zones 5. Development of projects in agriculture 6. Education and training.

Source: Consultant reports

¹¹⁹ The consultants hired to work on the studies included a professor from the Center for Entrepreneurship Development Ljubljana University; a gentleman from the Business Development Center, Kranj, and a professor from the University of Zagreb and Sinergija d.o.o. (a consulting company).

¹²⁰ See *Analysis of Competitive Advantages, SWOT Analysis, Development Vision, and Priority Development Projects* prepared for Zenica and Prijedor.

133. The publication of the final reports in July 2002 signaled the end of the first phase of the project. However, Phase 2 did not begin until March 2003. According to the project manager, the eight-month delay was caused by internal debates within SEED – “senior management was not sure that it [local economic development] should be a focus of SEED because they were unsure that it would have tangible benefits within the near term.”

Impact¹²¹

Zenica

134. Before working with SEED, the municipality had already launched a major planning project addressing physical, social and economic needs within the community. The municipality had retained the services of the Faculty of Mechanical Engineering at the University of Zenica to prepare the plan – Global Strategy for Zenica. Work began in November 2001; a draft report was issued in November 2002.
135. The SEED project ran in parallel to the broader “Global Strategy” and focused on creating a better environment for SMEs. Interviews with members of the planning team (including the Mayor) suggested that the initial motivation for working with SEED was financial. According to municipal officials, “not a single international organization was working in Zenica. USAID provided some funding to renovate the lobby of city hall, but for all practical purposes we weren’t receiving any support from the US or EU.” Officials saw SEED as a way to attract international resources to the community. Said one official, “Essentially, we thought that the SEED project would attract financial support for projects that we wanted to undertake” such as the industrial zone and business incubator which were contemplated long before SEED became involved with the community.
136. Regardless of the initial motivation, people interviewed as part of the evaluation stated that members of the team “learned a great deal” during the SEED project. They pointed to the participatory planning process, SWOT methodology, and knowledge gained about the needs of firms in the area. In addition, they came to recognize the importance of stakeholder participation to subsequent implementation of strategy.
137. In fact, according to the Mayor, the terms of reference for the Faculty of Mechanical Engineering was amended to reflect the SEED approach – seminars, workshops and roundtables. As a result, over 100 people have participated in the Global Strategy roundtables.
138. When visited in April 2002, the working group indicated that they wanted to develop business plans for three projects identified in their strategy: economic development agency, industrial zone, and business incubator. Said the Mayor, “Let’s be honest, the three projects are not just the result of the SEED project, we had been talking about them for a long time.” The process “confirmed conclusions that we had already reached.” In the beginning of 2001 (before any contact with

¹²¹ As of April 2003 when the evaluation team visited both municipalities, neither had yet implemented any of the projects identified in Phase 1. Subsequent correspondence with SEED staff indicated that Prijedor was moving ahead with the establishment of the one-stop-shop (OSS) development agency. It is expected to be operational in October 2003. Another municipality with which SEED has been working – Dobojski Istok – is scheduled to open a one-stop-shop in late November. The OSS is intended to enable the municipality to increase efficiency, improve control over the administrative processes, and reduce time needed for delivery of services to the private sector.

SEED), the municipality took title to the land and facilities at the *Zenica Steelworks* and *BH Steel* with the intention of developing the site as an industrial zone.

139. At this point, the community has reached a consensus on the projects that it would like to pursue and is waiting for financial support needed to implement them. They were expecting that SEED would sponsor a donors' meeting in June 2003 to present the projects and solicit international support for all three projects.

Prijedor

140. This project represented the first attempt by the municipality to take stock of its current situation and decide on an appropriate course of action. Interviews with members of the working group called attention to the participatory process as being particularly beneficial – it provided a vehicle for people to voice their concerns and interests.
141. They also noted that the project provided an opportunity to learn new approaches to assessing the structure and performance of the local economy. Referring to the report prepared by the consultants, one of the people in attendance at the interview indicated that “the economy cannot be developed by relying on old state enterprises; it needs to be based on market economics.” In general, the group indicated their support for SMEs. However, some indicated that the emphasis on this sector might be misplaced, noting the potential for growth in agriculture and the need to absorb returnees into the local economy.
142. As of April 2002, the working groups indicated that they needed to finalize work on the strategy, complete business plans for each of the proposed projects, and secure required financial support from an international donor. Some at the meeting voiced a fair degree of frustration with the process. As one put it, “people don't need to know what the problems are – they live them everyday. What we really need to do is simply begin.”

VI. Business Enabling Environment

Rationale

143. From its inception, SEED recognized that the success of SMEs was dependent on favorable conditions within the business environment, particularly with respect to laws and regulations that have a direct bearing on the ability of firms to compete effectively in markets.
144. While various international organizations are involved in this arena in all four countries, SEED felt that it could play a role in specific areas, building on the expertise of its own staff as well as the experience of IFC. In defining its role, SEED acknowledged that it has had limited resources to commit to efforts to improve the business enabling environment and, given the activities of other international organizations, felt it prudent to focus on support ongoing efforts in specific niches rather than engage in major new initiatives.

Role of SEED

145. The role that SEED plays can take a variety of forms. These include undertaking research to define the nature of the problem confronting businesses and outline potential reforms, assistance with drafting legislation and regulations, efforts to convince policy-makers to adopt needed reforms, and help with implementation. In many cases, SEED has convened meetings to foster greater dialogue among business people, government officials, civic leaders and international donors.
146. Many of the issues concerning the business environment revolve around specific policies, laws and regulations. Decisions on how best to approach reforms require in-depth knowledge of the particular field. SEED relies on outside consultants for expertise in fields relevant to the particular issues under consideration. For example, the organization has retained consultants with expertise in leasing and credit guarantees. SEED also has a few people on staff with policy and legal expertise that are called upon to render advice based on their own knowledge.

Activities

147. Under the rubric of BEE, SEED has engaged in a broad range of relatively small, discrete projects. However, most projects can be classified in four categories: financial intermediation, SME strategy, legal and regulatory reform, and studies. SEED activities and associated impacts related to the first three categories, which account for 35 percent of the BEE budget, are discussed below.

Financial intermediation

148. SEED has undertaken a number of projects designed to increase the flow of capital available to SMEs in the region. These projects have focused on drafting legislation to enable the establishment of leasing companies, collateral lending, and assessing the feasibility of credit guarantee institutions.¹²² The discussion that follows focuses on SEED's role in the development and enactment of leasing legislation in Macedonia and the Republic of Serbia.
149. From SEED's perspective, the main purpose of introducing leasing in a particular country is to enable SMEs to acquire needed capital equipment. The banking system in the region is conservative and requires high levels of collateral – usually two to three times the amount of the proposed loan, and in the form of land and buildings – before extending credit to an SME. Many SMEs cannot provide the required collateral, yet may have a strong trading position and growth prospects. Even when credit is available, it is usually in the form of short-term loans which are inappropriate for equipment purchases. As a result, business growth is frustrated and economic development opportunities are lost.
150. Leasing is intended to overcome this problem. Leasing companies purchase equipment on their own account and lease it to SMEs under suitable terms and conditions. Leasing arrangements can be beneficial from the perspective of the lessor and lessee. From the perspective of the lessor, the main advantage is that it enables the institution to extend more credit to reliable SMEs that are already at the limit of their ability to provide the collateral on ordinary loans. Leasing also enables institutions other than banks to participate in financial markets, encouraging financial product diversification and the development of secondary markets. From the perspective of the lessee, leasing provides another source of financing.

Leasing in FYR Macedonia

151. SEED has supported the development of leasing legislation in FYRM over the past 18 months by providing a technical review of proposed legislation and undertaking an outreach campaign with potential leasing companies.
152. It is important to place SEED's activities within the context of other efforts -- some of which were initiated prior to SEED's involvement. The origin of the leasing legislation in FYR Macedonia traces back to an IFC-funded feasibility study undertaken in 1998 as illustrated in Table 27. The study recommended the establishment of a leasing law in Macedonia based on positive experiences in other emerging economies. Soon thereafter, the Ministry of Finance (MOF) - which was committed to pursuing the concept - held talks with Financial Services Volunteer Corps (FSVC) about obtaining assistance to draft appropriate legislation. However, the involvement of FSVC was postponed as a result of the conflict in Kosovo and its repercussions for Macedonia. During this period FSVC was subject to a travel ban, which prevented them from bringing any consultants into the country to help the MOF with drafting of the law.

¹²² SEED completed a feasibility study for the establishment of a credit guarantee institution in BiH. SEED concluded that the concept was not feasible as envisioned and recommended that credit guarantee be offered directly through existing banks rather than through a new institution. In relation to collateral lending, SEED prepared a handbook on secured financing on Albania, and worked on a pledge registry in Kosovo.

Table 27. Key Milestones in the Establishment of the Leasing Law

Date	Event
1998	IFC funded feasibility study for a Leasing Law
August 2001	SEED retained consultant to work with government on legislation Initial draft of leasing legislation prepared by Ministry of Finance (MOF)
September 2001	Consultant provided comments on iterative drafts
October 2001	Consultant issued final report
December 2001	Final draft of legislation prepared
January 2002	Leasing legislation adopted
March 2002	GTZ sponsored study visit to Germany for MOF officials
Mid 2002	Leasing licenses issued to two companies, mainly dealing with the leasing of motor vehicles
October 2002	Seminar on the Leasing Law sponsored by SEED, attended by 22 financial and other organizations
January 2003	The Minister of Economy, in presenting the entrepreneurship action program, requested support from IFC to establish a number of leasing companies.
June 2003	Amendments to the current Law to be presented for approval by Parliament
(Planned) 2003	Establishment of leasing companies with IFC and/or EBRD support Publicity campaign targeted at potential lessors and at SMEs

153. Due to the delay in obtaining external assistance, MOF officials began to work on legislation based on the recommendations contained in the IFC report and a subsequent review of laws in other countries. SEED held a number of discussions with government officials and indicated that it was willing to provide assistance to the government to draft legislation. To this end, SEED retained the services of the consulting firm (Amembal and Gilyeart) who had worked on the original IFC study to review materials prepared by MOF and suggest ways in which proposed legislation might be strengthened.¹²³ It was felt that the consultant had sufficient background information to make it possible for him to undertake the work without traveling to Macedonia. SEED secured funding (US\$29,450) for the consultancy from the CIDA Trust Fund and coordinated the work from within FYRM. The report prepared by the consultant contained a large number of detailed recommendations, based on international experience.

154. The recommendations provided by the consultant were made available to the MOF during the process of drafting the version of the legislation that was sent to Parliament. At the time the legislation was passed, government officials recognized that it would require further amendment pertaining to certain tax and accounting provisions in order to provide incentive for the establishment of leasing companies. In addition, the Government is considering extending the law – which currently applies to only equipment and other moveable goods (such as vehicles) - to real estate. As part of the on-going work on the law and its implementation, three officials from

¹²³ According to the report prepared by the consultants, “The consulting firm of Amembal and Gilyeart has been retained by SEED to conduct a desk review of the Draft [Law on Financial Leasing]. The purpose of the desk review is to arrive at a final draft of a law on financial leasing that the MOF would submit to Parliament.”

the MOF undertook a study tour to Germany – arranged and funded by GTZ – to meet with a major leasing company and the German Leasing Association.

155. The first two licenses to operate under the new legislation were granted by the MOF in the first half of 2002. Both applications were from companies whose main intention was leasing of motor vehicles for consumers. One further license has since been issued for a company involved in leasing air conditioning equipment. For leasing to be launched in a substantial way, the banks will need to get involved. Although three leasing licenses have been issued by the Ministry of Finance to organizations other than banks (under the Macedonian law banks do not need licenses to operate as leasing institutions), these have been for operations which are peripheral to the priority needs of SMEs. The issuing of licenses, therefore, provides a useful testing ground for the law, but will not help much to fulfill its main objective.
156. SEED has discussed the need for support for implementation with MOF. One result of these discussions was a seminar for prospective leasing institutions organized by SEED in November 2002. This was attended by 27 people representing 22 institutions, indicating a high level of interest in the concept. The MOF did not attend because it felt the charge of \$150 per participant was inappropriate.
157. MOF officials have sought further assistance from SEED and the IFC. They have asked SEED to provide training for a small number of MOF officials in the supervision of lessors, and they would like help to undertake a publicity campaign aimed at potential leasing organizations (to stimulate supply) and SMEs (to stimulate demand). While SEED is supportive of the publicity campaign (though not committed to funding it), it has doubts about the value of training staff of MOF to supervise leasing institutions, preferring to see this responsibility rest with Central Bank in keeping with its ongoing supervision of the financial sector.
158. In January 2003, the Minister of Economy launched the Entrepreneurship Program, prepared by the SME Department in the Ministry as an implementation plan for the SME strategy produced in early 2002 (with SEED assistance). The Entrepreneurship Program includes a number of measures to support SMEs and entrepreneurship, including the leasing law. The Minister's announcement included a request for support from the IFC in establishing a number of leasing companies. SEED is in the process of responding to this request based on discussions with both the IFC and EBRD.
159. There are two main outstanding issues that need to be addressed as soon as possible:
 - **Amendments to existing law.** Some of the concerns that banks expressed may have implications for other laws. For example, some banks believe that assets acquired for leasing purposes may increase their fixed asset/equity ratio beyond the level permitted under the banking law. This issue needs to be resolved as quickly as possible. It is crucial that the Ministry of Finance and the banks receive consistent and fully informed advice on how best to deal with these issues. For example, EBRD considers the bank's concern about the impact of leasing on their ratios to be misplaced, since the International Accounting Standards – which Macedonia has formally adopted – explicitly exclude leases from consideration as fixed assets. Also, there is a danger that the Ministry will receive contradictory advice from different donors. For example, the advice of the IFC consultant was that MOF supervision of leasing institutions was unnecessary, or at least should be minimal; on the other hand, the recommendations obtained from GTZ appear to favor a stronger supervisory role for MOF.

- **Institutional development.** Active promotion of the opportunities presented by the legislation is needed to encourage financial institutions to establish leasing programs, particularly for capital equipment. Both EBRD and IFC are already in discussions with banks concerning potential investments in leasing operations. There appears to be an element of competition between the organization and some differences of opinion entering the process. In particular, IFC favors the creation of a leasing company as a joint venture between IFC (with a minority stake), a local bank and an international technical partner (primarily to provide technical support and training). In contrast, EBRD favors working with a bank directly as the lessor, with EBRD providing medium-term funding for the leasing activity (since the banks have mainly short term deposits, their ability to engage in leasing will otherwise be constrained). In practice, these differences of approach may be beneficial as they may lead to both IFC and EBRD playing substantive but different roles, leading to the creation of different types of leasing institutions in Macedonia.

160. SEED intends to maintain an active role in relation to both of these issues. The organization plans on convening a working group consisting of representatives of the MOF and Ministry of Economy, as well as legal and financial experts in Macedonia, to identify the areas in requiring amendment and agree with the changes. It also plans to work with IFC in developing proposals to establish a leasing institution and to encourage EBRD to provide funding for a local bank to launch a leasing program.

Leasing in the Republic of Serbia

161. As noted above, SEED has also been working with the Ministry of International Economic Relations (MIER) in the Republic of Serbia to draft leasing legislation. This process has been informed by lessons learned in FYRM. After reaching agreement with MIER on how best to proceed, SEED retained the services of Amembal and Gilyeart to review existing laws and materials prepared by the MIER. The consultant provided a detailed report to the inter-ministerial group led by MIER. The report – issued in June 2002 – contained a comparative analysis of leasing legislation and practices in different countries, a review of leasing activities in Serbia and Montenegro, and detailed comments on each article included in the legislation along with suggested revisions. SEED also retained the services of a regional consultant to address a number of specific tax, customs and accounting issues.
162. SEED also organized a series of roundtables with representatives of ministries, financial institutions and international organizations, including the IBRD, to discuss the leasing legislation. During this period, the MIER organized other meetings in which SEED participated as an active member of the working group. According to MIER officials, these roundtables and meetings were instrumental in advancing the legislation. They enabled people to flag concerns and suggest potential ways to address them. Said the Special Legal Advisor to the Minister, “there were a lot of compromises made along the way” with respect to such issues as paid-in capital, cross-border transactions, and eligible assets. In regard to the latter, initially leasing was to be limited to equipment and property used for commercial purposes; however, under pressure from financial institutions, the Ministry made the decision in April 2003 to extend the law to consumer goods, including automobiles. The legislation was passed by Parliament on 27 May 2003. It authorizes the creation of independent leasing companies with minimum capital of €100,000. According to a press release issued at that time, five banks are already in the process of setting up leasing companies.

163. SEED has continued to support efforts to establish a leasing industry by conducting a number of workshops and seminars targeted to financial institutions as well as potential customers. The organization also provided support to the Ministry of Finance to help revise tax laws to create incentives for the establishment of leasing companies.
164. The Special Legal Advisor to the Minister stated, “We have been more than satisfied with the performance of SEED.” She also indicated that “the big difference between SEED and other organizations is that they were willing to work with us to ensure that the leasing law reflected local conditions.”

SME Strategy Development

165. SEED worked with local partners to formulate a strategy for promoting the development of SMEs in the Serbian Republic.¹²⁴ The effort focused on drafting a document in concert with the Serbian Parliament, specifically the Committee for Development and Foreign Economic Relations.
166. The effort dates back to a meeting held in the spring of 2001. USAID invited the co-chair of the Committee for Development and Foreign Economic Relations to attend a meeting sponsored by SEED to discuss coordination of donor activities. Following the meeting, the co-chair had a number of conversations with SEED staff on the need for various programs directed toward SMEs. In fall 2001, the Committee invited donors, members of parliament and government officials to discuss the status of SMEs and the needs for a comprehensive SME development strategy. According to the co-chair, government representatives who attended the meeting indicated that the help of the Committee would be appreciated. Soon thereafter, the Committee began work to formulate such a strategy with support provided by SEED.
167. Principal responsibility for the development of the strategy rested with the Balkan Investment and Development Company (BIDCO) – a private consulting firm based in Belgrade – retained by SEED for this project.¹²⁵ BIDCO collected and analyzed data concerning the SME sector, organized a series of public meetings, made various presentations, and drafted the final report. SEED provided support as needed. According to SEED staff, the organization “preferred to stand aside and let local people take the lead and assume ownership of the process.”
168. The final report prepared by BIDCO highlighted a number of factors constraining the development of the SME sector in Serbia, delineated a set of strategic goals, and offered a series of recommendations. In this regard, it contained a long litany of specific measures to promote the development of SMEs, grouped under five broad categories:
- Laws and regulations affecting SMEs;
 - Education and training with respect to entrepreneurship;
 - Consulting and training services targeted toward SMEs;
 - New financial institutions and programs; and

¹²⁴ SEED also worked with the government in FYRM to develop an SME strategy. Interviews with government officials suggested that the work was well received.

¹²⁵ Other organizations involved in the work included SIGMA – a business association – and G17 Plus. G17 Plus was a non-governmental organization, serving as a think tank for economic and policy reformers. The organization registered as a political party in December 2002.

- Local development organizations.

169. The final document was formally endorsed by the Committee on 10 June 2002. In its statement, the Committee urged the Government to take the recommendation offered in the report into “consideration during the development of its strategy for development of small and medium enterprises.” After publication of the final report, SEED took steps to disseminate it through business publications.
170. Roughly one month before the work of the Committee was finalized, the Ministry of Economy and Privatization began work on an SME Strategy with the support of the European Agency for Reconstruction (EAR) and the World Bank.¹²⁶ A new Assistant Minister was appointed in April 2001 to head the Department for Development of Small and Medium-sized Enterprises within the Ministry of Economy and Privatization. This department is tasked explicitly with monitoring and analyzing the performances of SME's, suggesting measures for promoting the development of SME's, and recommending measures for stimulating investment in SME's, and fulfilling other assignments prescribed by law. The SME Department is intended to work closely with both the Agency for the Development of Small and Medium-Sized Enterprises and Entrepreneurship and the SME Advisory Board.¹²⁷ The Ministry of Economy and Privatization released the five-year national SME Strategy in January 2003 – roughly six months after the Committee's endorsement of the SEED/BIDCO report. The strategy lays out a broad framework for fostering growth in the number of SMEs and strengthening their performance.
171. Even though the Government started from scratch in formulating its strategy; the co-chair feels that the work of the Committee was not wasted. In fact, he believes that the process “encouraged debate” and went a long way to “educating and preparing members of the parliament to take action on key legislation.” Some elements of the Government's strategy are mirrored in the SEED/BIDCO report.
172. The fact that there were two independent efforts to formulate an SME strategy for the Republic of Serbia – one in Parliament supported by SEED and the other in the Ministry of Economy and Privatization supported, in part, by the World Bank – caused some confusion among various parties. World Bank representatives acknowledge problems with coordination, but in any event felt that SEED efforts were misplaced. Said the IBRD Country Director, “Neither knew what the other was doing. This didn't make the bank look good. [Moreover] the Parliamentary Committee was just the wrong place to do this work.” The IBRD Country Director further noted that the government has the primary responsibility for developing and implementing policy. The co-chair saw this differently. He was interested in fostering a dialogue within different branches of government and the business community on the needs of SMEs.
173. IBRD accepts some responsibility for miscommunication and ensuing tensions, noting the lack of resources within the Belgrade office. “We now have two people at the bank who interact with SEED and SEED's efforts are now incorporated directly into work plans.”

¹²⁶ As part of this support, the World Bank organized a mission to Serbia to discuss SME development issues and offered the services of a consultant to assist in the formulation of the national strategy.

¹²⁷ The SME Agency was established by law in 2001 as the executive agency responsible for implementing the government's SME strategy, informing Government on SME issues, promoting the SME sector, and supporting regional SME organizations. The SME Advisory Board is intended to serve as a national forum where Government and SME representatives can work together on issues affecting SMEs.

Legal and regulatory reform

174. SEED has also been involved in efforts to remove various legal and/or regulatory constraints to SMEs. As noted above, it appears that most of these efforts have revolved around the preparation and implementation of the World Bank's Business Environment Adjustment Credit (BAC) in BiH, particularly with respect to streamlining the business registration process. As discussed below, SEED has provided technical assistance based on the expertise of its own staff and promoted an ongoing dialogue among interested parties with respect to specific elements of the BAC. In this regard, SEED played a role in fostering discussions concerning steps needed to streamline the business registration process within the two entities.
175. It is important to place SEED within the broader context of activities undertaken by the World Bank and other international donors in this arena as illustrated in Table 28 and explained below.

Table 28. Chronology of Events Related to Business Registration

Date	Event
March 2001	FIAS Report
March 2001	Initial BAC mission
May 2001	Post-Mission Report
May to October 2001	Meetings of business registration working group
October 2001	DFID and Norwegian Embassy present note on proposed technical assistance project
May 2002	Approval of BAC by World Bank
June 2002	BAC signed in BiH

176. The Foreign Investment Advisory Service (FIAS) has been actively involved in efforts to improve the investment climate in BiH for the past five years. In 1998, the organization helped draft the foreign investment policy law; two years later it provided assistance to develop an institutional framework for the newly established Foreign Investment Promotion Agency (FIPA). As a continuation of this work, FIAS issued a report in March 2001 that documented various administrative barriers to foreign investment in BiH.¹²⁸ The report included an assessment of the business registration process, noting the complexity, cost, and time involved in starting-up a new firm in the RS and FBiH. The FIAS report estimated that 31 days were required, on average, to register a business in the RS and 80 days were needed in the FBiH. The report called on the government to harmonize laws and procedures between the two entities and simplify the overall business registration process.
177. The recommendations offered by FIAS with respect to the registration process and other constraints to investment were subsequently refined and incorporated into the World Bank's Business Environment Adjustment Credit (BAC). Work to prepare the BAC officially began soon after the FIAS report was published. In March 2001, the World Bank conducted a mission to BiH to lay the groundwork for the BAC. Significantly with respect to the evaluation of SEED, the 11-

¹²⁸ "Bosnia and Herzegovina: Commercial Legal Framework and Administrative Barriers to Investment," FIAS, March 2001.

member team included two employees of the organization. The post-mission report prepared by the consultants retained by the World Bank presented an assessment of the business environment in BiH and offered a series of recommendations on needed legal and regulatory reforms.¹²⁹ With respect to simplifying the business registration process, the report contained a series of recommendations that were “informed” by previous papers prepared by the European Commission and the OECD.¹³⁰

178. The mission conducted in March 2001 was the starting point for the development of the BAC.¹³¹ However, more work was needed to define specific elements of the proposed credit, including the precise actions that the Government needed to take as a condition of the loan. As part of the process of preparing the BAC, SEED assumed responsibility for organizing and supporting a working group to consider steps to simplify the business registration process.¹³² The working group was chaired by the Minister without Portfolio, Federation of BiH. It included representatives from key ministries at the State and Entity levels, OHR, and international donor agencies as well various experts.¹³³ SEED staff provided support to the working group.
179. The working group met seven times between May and October 2001. All but one of the meetings was held in FBiH; the sixth meeting in September 2001 was held in Banja Luka. The meeting in Banja Luka represented the first time that representatives of the Republic of Srpska were involved in activities of the working group. Following that meeting, the Minister of Foreign Economic Relations was appointed co-chair; however, he did not attend the next and last meeting of the working group in the following month.
180. While the working group brought greater attention to the problems of business registration in the two entities, discussions with the chairperson and a review of the minutes of the working group suggest that the accomplishments made by the group during its six-month tenure were minimal. Hard progress was stymied due to a number of factors. These included the lack of a specific mandate and approach to guide the activities of the working group, inadequate representation from the RS, lack of authority of members to make decisions on behalf of their respective

¹²⁹ Business Environment Adjustment Credit Preparation Mission, Post-Mission Report on the Commercial Legal Framework and Enforcement Regime in Bosnia and Herzegovina, Dewey Ballantine LLP, May 2001.

¹³⁰ European Commission Recommendation on Improving and Simplifying the Business Environment for Business Start-Ups, C(97) 1161 (April 22, 1997) and the OECD’s General Principles of Company Law for Transition Economies. The report contained the following recommendations with respect to business registration: establish a “one-stop” office for business registration; introduce a single business registration form; eliminate duplicative or unnecessary steps; require each office involved in the registration process to share information with others; use private sector professionals and lower level administrative court personnel to assist judges; enforce and expand the “deemed approved” system as allowed in existing laws; simplify the process of amendment and eliminate the need for re-registration; Encourage government employees to deliver high-quality service; implement a single business identification number system for all administrative purposes; harmonize the laws of business registration across entities; and consider granting amnesty to companies operating in the informal sector as an incentive to register.

¹³¹ In May 2002, the World Bank approved a \$44 million Business Environment Adjustment Credit (BAC) for Bosnia-Herzegovina to support efforts by the government to improve the investment climate to attract domestic and foreign investors. The BAC was signed by the BIH Minister of Foreign Trade and Economic Relations and by the Director of Office of the World Bank in BiH in June 2002. The proposed reforms combine legislative and administrative measures for enhancing the investment climate in the near term. The credit provides financial support to the State and Entity budgets. It will be disbursed on standard IDA terms and will be repayable in 35 years, including a 10-year grace period, upon fulfillment by the Government of agreed actions. The BAC calls attention to the need to facilitate “business entry through the creation of a simplified and transparent countrywide approach to business registration” and outlines necessary reforms as a condition of the loan.

¹³² In fact, the Aide Memoire for the World Bank Mission (March 6-20, 2001) indicated that “IFC’s Southeast Europe Enterprise Development (SEED) facility is expected to play a key role in supporting implementation of the reforms.”

¹³³ See Table D-1 in the Appendix for a list of working group members.

organizations, irregular attendance by certain members, and a general lack of resources. As a result, few concrete recommendations were forthcoming.

181. Members of the group came to recognize that there was a great deal of work that needed to be done with respect to amending particular laws, modifying specific steps in the registration process, and reassigning responsibility for certain tasks to new institutions as well as designing and implementing the single registry system itself (hardware and software). By October, individual members of the working group were actively considering ways to obtain needed technical assistance. To this end, DFID and the Norwegian Embassy advanced a proposal for revamping the business registration system. The €500,000 proposal included the re-design of the business registration process and the development and installation of a new system. Specifically, the Project Concept Note (PCN) prepared by DFID delineated the planned outputs of the project as follows:¹³⁴
- Confirmation of the problem and statement of objectives as defined in the FIAS report;
 - Specification of a revised system for business registration reflecting European best practice;
 - Changes to laws and regulations to give legislative expression to the proposals;
 - Implementation of the system across BiH; and
 - A business plan for revenue generation based on data in the registration system.
182. While DFID has assumed direct responsibility for working with the government to revise the business registration process, SEED continues to provide support – one staff member is currently devoting a few days per month to this effort, providing the team with legal expertise.¹³⁵ DFID funding has been committed, contractors have been retained, and a pilot effort in two municipalities has been planned. Still, two years after the FIAS report was issued, there has been little change in the business registration process in BiH.
183. The chairperson of the working group stated that SEED has played an important role in the process through its “authority to convene meetings” derived from its relationship to the World Bank. He noted that this was the “first instance when Ministers of Justice from both Entities sat at the same table.” SEED management echoes this sentiment. SEED wanted to create a working group composed of representatives from government, private sector and international donors, and, in so doing, foster local ownership of the reform process. While local ownership of the process was not realized, SEED perceives the process itself as an important breakthrough.
184. In terms of the role of SEED in the reforming the business registration system, it is important to note that the organization is one of many players that are active in this arena. It is difficult to identify the contributions of specific individuals or organizations to the reform effort. As one senior official in the Ministry of Justice – RS put it, “To be honest, there are so many international agencies involved in the process, I cannot recall who is doing what.”

¹³⁴ Project Concept Note – Bosnia and Herzegovina: Project for Reform of Business Registration, 31 October 2001.

¹³⁵ While DFID and the Norwegians envisioned that the working group would continue to operate in a consultative capacity with responsibility for detailed oversight passing to a smaller committee, the working group has not yet reconvened

VII. Cost of Service Delivery and Commercial Viability

Overview

185. Table 29 presents a summary of receipts and expenditures in FY00, FY01, FY02, and the first six months of FY03.¹³⁶ As noted above, SEED took in approximately US\$24.4 million during this period and spent US\$12.6 million. The balance of US\$11.8 million is held in cash reserves. SEED will need to draw on reserves to cover its operations over the next two years.

Table 29. Summary of SEED Receipts and Expenditures (Cash Basis, US\$)

	FY00	FY01	FY02	FY 03 Q1 and Q2	Total (FY00- Q2FY03)	% of Total
Receipts						
Core donor funding (grant)	8,444,739	4,370,844	6,762,754	2,317,620	21,895,957	89.6%
Project-specific donor funding (grant)	0	53,606	102,901	520,285	676,791	2.8%
Client-paid fees for service	0	17,030	209,808	137,238	364,076	1.5%
Investment income	48,790	563,735	613,726	264,170	1,490,421	6.1%
TOTAL RECEIPTS	<u>8,493,529</u>	<u>5,005,215</u>	<u>7,689,188</u>	<u>3,239,313</u>	<u>24,427,245</u>	<u>100.0%</u>
Expenditures						
Investment services	NA	524,407	744,657	288,073	1,557,136	12.3%
Capacity Building - SME	NA	212,673	808,113	249,157	1,269,942	10.1%
Capacity Building – BDS	NA	409,917	1,065,270	713,747	2,188,935	17.3%
Business Enabling Environment	NA	243,736	389,002	176,745	809,483	6.4%
General management and administration	NA	1,545,164	3,384,324	1,191,674	6,121,163	48.5%
Start-up expenses	685,894	0	0	0	685,894	5.4%
TOTAL EXPENDITURES	<u>685,894</u>	<u>2,935,897</u>	<u>6,391,367</u>	<u>2,619,395</u>	<u>12,632,553</u>	<u>100.0%</u>

Source: SEED records

186. Funding from donors (core funding and project-specific funding) totaled almost US\$22.6 million or 92.4 percent of total receipts. The organization has generated roughly US\$364,000 in fee-for-service incomes and US\$1.5 million in interest on account balances.

187. The IFC Board Report projected fees-for-service over the five-year life of the facility at \$2.4 million. However, this was based on donor funding of \$33.4 million which was subsequently scaled back to \$25 million. Assuming that fee collection proportionate to donor funding, this would suggest projected total fees of roughly \$1.8 million. SEED would need to earn more than \$1.4 million over the remaining part of the project's life to meet this target.

188. On the expenditure side, roughly 46.1 percent of the total US\$12.6 million expended through 31 December 2002 has been allocated to programs. General management and administration

¹³⁶ SEED's fiscal year ends June 30th.

accounted for 48.5 percent of total expenditures during this period and start-up (non-recurring) expenses accounted for the remaining 5.4 percent. SEED has estimated that 14 percent of the cost of general management and administration are “a result of being part of the IFC structure” – this represents roughly \$857,000 of the total \$6.1 million in allocated overhead.

Investment services

189. Table 30 shows that SEED spent roughly US\$3.2 million from inception through the end of December 2002 on Investment Services, including direct IS project expenses, indirect IS program expenses, and allocated SEED overhead.¹³⁷ During the same period, SEED generated US\$153,000 in client-paid fees.

Table 30. Investment Service Receipts and Expenditures (US\$)

	FY01	FY02	FY 03 Q1 and Q2	Total	% of Total Expenditures
Receipts					
Client-paid fees	\$8,726	\$72,844	\$71,656	\$153,227	4.8%
Expenditures					
Direct project expenses	195,230	326,246	184,352	705,828	22.1%
Indirect program expenses	329,177	418,411	103,720	851,308	26.7%
Sub-total IS direct and indirect expenses	<u>524,407</u>	<u>744,657</u>	<u>288,072</u>	<u>1,557,136</u>	<u>48.8%</u>
Allocated SEED overhead	582,638	838,086	240,445	1,636,167	51.2%
Total IS expenditures	<u>1,107,045</u>	<u>1,582,743</u>	<u>528,517</u>	<u>3,193,303</u>	<u>100.0%</u>

Source: SEED records

190. The cost structure has changed over time as the organization has expanded its operations and increased the volume of business. Indirect program expenses and allocated overhead, while growing, have dropped as a percentage of total expenditures as these fixed costs are amortized over a larger volume of business. In FY01, indirect program expenses and allocated overhead represented 82.4 percent of total IS expenditures; during the first six months of FY03, this figure had dropped to 65.1 percent.

191. A review of project-level data provided by SEED reveals a wide variation in the cost of delivering investment services to individual companies. Differences in cost reflect the nature and complexity of projects as well as the involvement of outside consultants. According to SEED’s records, the direct project expenses for completed IS projects ranged from \$47 to more than \$71,000 with an average of \$8,264 (median \$8,910). Typically, the IS team conducts an IEP before undertaking

¹³⁷SEED did not break down expenses by program areas until FY01. Direct project expenses include consultant costs, staff costs and other expenses incurred by individual projects. Indirect program expenses include product development, business development and other expenses associated with the IS program. SEED general and administrative overhead is allocated based on a strategic objective’s proportion of total expenses. A list of SEED’s IS project-cost data is presented in Appendix Table E-2.

work on an IP with clients.^{138,139} On average, the total direct project expense for a combined IEP and IP project was \$14,800. Once indirect program expenses and allocated overhead are factored into the cost of service delivery, the total cost to complete an IEP and subsequent IP is on the order of US\$67,000 (Table 31).¹⁴⁰ Consultant fees and staff salaries account for approximately 54 percent and 29 percent of direct project costs, respectively.

Table 31. Average Cost Per Completed IS Project (US\$)

	Consultant	Salary	Travel	Other	Direct Project Expenses	Fully Burdened Cost
All IS Projects	\$4,482	\$2,389	\$1,253	\$141	\$8,264	\$37,388
Combined IEP and IP	\$7,259	\$4,828	\$2,470	\$284	\$14,841	\$67,144
IEP Only	\$6,261	\$2,065	\$1,337	\$134	\$9,798	\$44,328

Source: SEED records

192. The IS team has increased its productivity in terms of the number of active projects per staff member from 1.5 to 2.4 per quarter over the evaluation period. For FY02 as a whole, the number of active projects per IS staff member was 6.7.¹⁴¹ The number of completed projects per staff member has increased over the period as well, from 0.4 in the second quarter of FY01 to 0.9 in the second quarter of FY03.¹⁴² In FY02, the number of completed IS projects per staff member was 2.6. Assuming that projects have not changed much in their nature and quality, this would suggest that SEED staff has become more efficient over the course of its operating tenure. In addition, the greater volume of business has enabled SEED to amortize indirect costs (including overhead) over a larger base of projects.

193. The organization has not sought to recover the full cost of service delivery. The pricing policy adopted by SEED and endorsed by the donors states that fees will be charged at “commercial viable rates according to local market conditions” with the intention of covering 100 percent of “local” costs – the latter include local consultants, SEED staff and other direct expenses.¹⁴³ Fees have increased dramatically over the past two and a half years – if the current trend continues, revenues for FY03 will double those earned in FY02. However, the organization is still far from covering direct project expenses. During the first six months of FY03, SEED generated fees of US\$71,600 versus direct project expenses of US\$184,400. As a result, client-paid fees still accounted for less than 40 percent of direct project expenses as shown on in Table 32. If indirect

¹³⁸ In 20 instances, SEED completed an IEP without progressing to an IP (at least within the study period).

¹³⁹ The cost and revenues associated with the IEP and IP for a particular client are often included under one WBS element for accounting purposes, i.e., SEED does not close a WBS at the end of an IEP and open a new WBS for the IP.

¹⁴⁰ If the component of SEED costs attributed to being part of the IFC structure were to be eliminated, the total cost to complete an IEP and subsequent IP would drop by roughly 7.5 percent to US\$62,000.

¹⁴¹ Appendix Table E-3 presents the number of *active* projects per staff member from September 2000 to the end of December 2002.

¹⁴² Appendix Table E-4 presents the number of *completed* projects per staff member from September 2000 to the end of December 2002.

¹⁴³ SEED Annual Report 2001.

program expenses are factored into the equation, the cost recovery rate drops to 25 percent. Finally, client-paid fees as a percentage of total IS expenditures – including allocated overhead – was less than 14 percent in the first two quarters of FY03. On average, during the latest six month period, SEED would have needed to increase its fees by roughly 150 percent to cover direct project expenses and by almost seven times to cover the full cost of delivering investment services to clients.

Table 32. IS Cost Recovery

	FY01	FY02	FY 03 Q1 and Q2	Total
Client-paid fees as a percent of <i>direct</i> project expenses	4.5%	22.3%	38.9%	21.7%
Client-paid fees as a percent of <i>direct</i> project expenses plus indirect program expenses	1.7%	9.8%	24.9%	9.8%
Client-paid fees as a percent of total IS expenditures, including allocated overhead	0.8%	4.6%	13.6%	4.8%

Source: SEED records

194. The decision as to what to charge clients for particular services is at the discretion of SEED staff.¹⁴⁴ According to SEED, this affords a great deal of flexibility, enabling the organization to adjust fees based on what particular clients can afford. A review of data provided by SEED suggests that cost recovery on particular IS projects has varied from less than two percent to more than 200 percent of direct project expenses.¹⁴⁵ For the firms that completed an IP prior to the end of Q1 FY03, SEED generated \$49,478 in income (client-paid fees), representing approximately 4.3 percent of total cost of service delivery once indirect program expenses and allocated overhead costs are included.¹⁴⁶ Cost recovery for this subset of IS projects ranges from less than two percent to 14 percent.¹⁴⁷

Capacity Building -- SMEs

195. According to SEED records, SEED has allocated a total of roughly US\$2.6 million to CB-SME, including direct project expenses, indirect program expenses, and allocated SEED overhead as shown in Table 33.¹⁴⁸

¹⁴⁴ SEED management reviews project proposals, including budgets and fees, as part of the approval process.

¹⁴⁵ It appears that SEED is able to recover a higher percentage of the cost of smaller projects than larger projects.

¹⁴⁶ Project cost data is not available for three firms.

¹⁴⁷ The correlation coefficient (ρ) between client-paid fees and SEED project expenditures for the portfolio as a whole is 0.37, while for the 17 completed IP projects, $\rho=0.75$.

¹⁴⁸ Direct project expenses include consultant costs, staff costs and other expenses incurred by individual projects. Indirect program expenses include product development, business development and other expenses associated with the CB-SME program. SEED general and administrative overhead is allocated based on a strategic objective's proportion of total expenses. A complete list of individual CB-SME projects and their associated costs is presented in Appendix Table E-5.

Table 33. Expenditures on CB-SME Programs (US\$)

	FY01	FY02	FY 03 (Q1 and Q2)	Total (FY01-Q2FY03)	% of total Expenditures
Receipts					
Client-paid fees	3,605	78,157	19,510	101,272	3.9%
Direct project expenses	45,029	502,617	119,551	667,197	25.6%
Indirect program expenses	167,644	305,495	129,606	602,746	23.1%
Sub-total direct and indirect expenses	<u>212,673</u>	<u>808,112</u>	<u>249,157</u>	<u>1,269,943</u>	<u>48.8%</u>
Allocated SEED overhead	236,289	909,504	207,963	1,334,397	51.2%
Total CB-SME expenditures	<u>448,962</u>	<u>1,717,617</u>	<u>457,120</u>	<u>2,604,339</u>	<u>100.0%</u>

Source: SEED records

196. Comparing total CB-SME expenditures to the number of participants that have attended training programs directed toward SMEs suggests that the direct project expenses per participant is on the order of US\$1,330 or US\$5,200 if indirect expenses and allocated overhead are included.¹⁴⁹ The total cost per participant-training hour works out to roughly US\$55. However, many of these costs are one-time expenditures associated with curriculum development. As such, the cost of training can be expected to be amortized over a larger base assuming that the courses are continued.¹⁵⁰

197. SEED has generated a total of US\$101,000 in client-paid fees for training services provided under the rubric of CB-SME through 31 December 2002. As shown in Table 34, SEED has recovered approximately 15 percent of direct project expenses associated with CB-SME training programs and almost four percent of total expenditures, including indirect program expenses and allocated overhead. SEED would need to boost prices by more than 500 percent to cover direct project expenses.

Table 34. CB-SME Cost-Recovery

	FY01	FY02	FY 03 Q1 and Q2	Total
Client-paid fees as a percent of <i>direct</i> project expenses	8.0%	15.6%	16.3%	15.2%
Client-paid fees as a percent of <i>direct</i> project expenses plus indirect program expenses	1.7%	9.7%	7.8%	8.0%
Client-paid fees as a percent of total CB-SME expenditures, including allocated overhead	0.8%	4.6%	4.3%	3.9%

Source: SEED records

¹⁴⁹ However, this figure may significantly understate actual training costs. The costs presented in the table are based solely on WBS elements that SEED has allocated to CB-SME. However, SEED has also used WBS elements included under CB-BDS for training programs directed to SMEs. The problem of disentangling these costs is further exacerbated by the use of one WBS for both types of training, i.e., training directed toward SMEs and training directed toward consultants are included under the same WBS.

¹⁵⁰ SEED has offered many of these courses since December 2002 and is in the process of turning over courses and materials to business school faculty and other consultants.

Capacity Building – Business Development Services

198. As shown in Table 35, SEED spent roughly US\$4.5 million on activities designed to build the capacity of organization that provide services to SMEs in the region. These expenditures include direct project expenses, indirect program expenses, and SEED allocated overhead.¹⁵¹

Table 35. Total Receipts and Expenditures on CB-BDS (US\$)

	FY01	FY02	Q1 and Q2 FY 03	Total	% of total expenditures
Receipts					
Project-specific donor-funding ¹⁵²	53,605	0	515,214	568,819	12.7%
Client-paid fees	4,699	58,805	41,816	105,320	2.3%
Sub-total receipts	<u>58,304</u>	<u>58,805</u>	<u>557,030</u>	<u>674,139</u>	<u>15.0%</u>
Expenditures					
Direct project expenses	177,390	791,901	611,681	1,580,972	35.2%
Indirect program expenses	232,527	273,370	102,066	607,962	13.5%
Sub-total direct and indirect expense	<u>409,917</u>	<u>1,065,271</u>	<u>713,747</u>	<u>2,188,934</u>	<u>48.8%</u>
SEED allocated overhead	455,435	1,198,926	595,742	2,300,031	51.2%
Total CB-BDS expenditures	<u>865,352</u>	<u>2,264,196</u>	<u>1,309,490</u>	<u>4,488,966</u>	<u>100.0%</u>

Source: SEED records

199. Table 36 breaks down the receipts and expenditures into four categories:

- **Consultant development.** From inception through 31 December 2002, SEED had spent approximately \$922,000 on direct project expenses related to the development of local consultants. Given the proportionate share of CB-BDS program expenses and SEED allocated overhead, the total cost of efforts to enhance the capacity of local consultants is on the order of US\$2.6 million. The cost of this initiative can be spread out over the 64 companies that have participated in the Consultancy Network or various consultant training programs described above. This works out to approximately US\$41,000 per participating company. (This does not include any fees paid directly to consultants under subcontract to SEED.) SEED has generated fees of roughly \$75,000, representing about three percent of total expenditures.

¹⁵¹ Project expenses include consultant costs, staff costs and other direct project expenses. Other program expenses include business development and other expenses attributed to the CB-BDS program. SEED general and administrative overhead is allocated based on the proportion of total program expenses accounted for by CB-BDS. Some of the CB-BDS projects were undertaken with funding provided through the CIDA Trust Fund; SEED has indicated that all associated costs are reflected in the project expenses as reported in the table. Appendix Table E-6 presents the individual projects and their associated costs.

¹⁵² See Appendix Table E-7.

- **Business associations.** From inception through 31 December 2002, SEED had spent approximately \$121,000 on direct project expenses related to the development of business associations. Given the proportionate share of CB-BDS program expenses and SEED allocated overhead, the total cost of efforts to enhance the capacity of business associations is on the order of US\$343,000. As designed, there is no intention to recover costs. Funding for SEED's work with business associations in the region has been drawn primarily from the CIDA Trust Fund.¹⁵³ It should also be noted that SEED has continued to work with associations in the region under Phase 2 of the initiative. The additional costs associated with Phase 2 were incurred after 31 December 2002 and are not reflected in the figures cited above.
- **Local economic development organizations.** According to data provided by SEED, a total of \$113,000 has been spent on direct project expenses associated with local economic development efforts. When indirect program expenses and allocated overhead are factored in, the total cost rises to US\$321,000. The two municipalities paid SEED approximately \$20,500 for services rendered, representing almost 20 percent of direct expenses and six percent of total expenditures. According to SEED, this was the first time that a municipal authority had paid for consulting services. Finally, it should be noted that SEED has continued to work with municipalities in the region since 31 December 2002. The cost of this follow-in work is not reflected in the figures cited above.
- **Other CB-BDS.** The total cost of other CB-BDS projects, including direct project expenses, indirect program expenses and allocation overhead is on the order of \$1.2 million. The bulk of these expenses have been associated with the Investment Service Linkages initiative and the establishment of SeeBIZ.net.¹⁵⁴

¹⁵³ In addition, the SME Department has assigned staff to oversee the CIDA Trust Fund and individual projects. These costs are not included in the figures cited above.

¹⁵⁴ The Investment Service Linkages initiative consists of various tools and methods to encourage larger corporations in the region to source a greater percentage of their inputs from local SMEs. *SEEBIZ.net* is a website that is intended to serve as a regional business portal targeted toward local SMEs and BDS providers.

Table 36. CD-BDS Project Expenses through 31 December 2002

WBS Element Description ¹⁵⁵	(US\$)
Consultant development	
Client-paid fees	74,795
Direct project expenses	922,222
Share of indirect program expense	354,640
Share of SEED allocated overhead	1,341,668
Total consultant expenditure	<u>2,618,530</u>
Business associations	
Client-paid fees	227
Direct project expenses	120,975
Share of indirect program expense	46,521
Share of SEED allocated overhead	175,997
Total business association expenditure	<u>343,493</u>
Local economic development organizations	
Client-paid fees	20,534
Direct project expenses	113,163
Share of indirect program expense	43,517
Share of SEED allocated overhead	164,632
Total local economic development expenditure	<u>321,312</u>
Other CB-BDS	
Client-paid fees	9,766
Direct project expenses ^(a)	424,612
Share of indirect program expense	163,284
Share of SEED allocated overhead	617,734
Total expenditure on other CB-BDS	<u>1,205,631</u>

Note; (a). The "OEG Income Statement Template" and the CB-BDS Project Portfolio" list provided by SEED showed a discrepancy of US\$53,606 in total direct project expenses. The evaluation team allocated this difference to "other CB-BDS" in the table above.

Source: SEED records

Business enabling environment

200. As shown in Table 37, SEED has spent roughly US\$1.7 million on activities designed to strengthen the business enabling environment, including direct project expenses, indirect program expenses, and SEED allocated overhead.¹⁵⁶

201. SEED management and donors are not expecting the organization to be able to generate sufficient revenues to cover the cost of services in this arena. Funds for these activities have come from core donor contribution and project-specific funding provided by individual donors. This includes funding provided through the CIDA Trust Fund. Since its inception, SEED has

¹⁵⁵ A WBS (Work Breakdown Structure) element captures revenue and expenses associated with a project in the World Bank accounting system used by SEED.

¹⁵⁶ SEED did not break down expenses by program areas until FY01. Project expenses include consultant costs, staff costs and other direct project expenses. Other program expenses include business development and other expenses attributed to the BEE program. SEED general and administrative overhead is allocated based on the proportion of total program expenses accounted for by BEE. Appendix Table E-8 presents the individual BEE projects and their associated costs.

earned less than US\$4,300 in fees for the services that it has rendered to government and other parties.

Table 37. Total Receipts and Expenditures on BEE (US\$)

	FY01	FY02	Q1 and Q2 FY 03	Total	% of total expenditures
Receipts					
Project-specific donor-funding	0	102,901	5,070	107,971	6.5%
Client-paid fees	0	0	4,255	4,255	0.3%
Sub-total receipts					
Expenditures					
Direct project expenses	53,487	348,333	138,577	540,398	32.6%
Indirect program expenses	190,249	40,669	38,168	269,086	16.2%
Sub-total direct and indirect expense	<u>243,736</u>	<u>389,002</u>	<u>176,745</u>	<u>809,484</u>	<u>48.8%</u>
SEED allocated overhead	270,801	437,809	147,524	850,568	51.2%
Total BEE expenditures	<u>514,538</u>	<u>826,811</u>	<u>324,269</u>	<u>1,660,051</u>	<u>100.0%</u>

Source: SEED records

202. The following presents the breakdown of BEE receipts and expenditures into four categories:¹⁵⁷

- **Financial intermediation.** From inception through 31 December 2002, SEED had spent approximately US\$131,000 on direct project expenses related developing new financial services, including leasing. Given the proportionate share of BEE indirect program expenses and SEED allocated overhead, the total cost of efforts to enhance financial intermediation is US\$402,000.
- **SME strategy.** From inception through 31 December 2002, SEED had spent approximately \$38,000 on direct project expenses in this area and a total of US\$116,000 once indirect program expenses and allocated overhead are factored in.
- **Legal and regulatory reform.** According to data provided by SEED, a total of \$22,000 has been spent on direct project expenses associated with legal and regulatory reforms. When indirect program expenses and allocated overhead are factored in, the total cost rises to US\$69,000.
- **Studies and other BEE activities.** The total cost of studies and other BEE activities, including direct project expenses, indirect program expenses and allocation overhead is on the order of \$1.1 million.

¹⁵⁷ Appendix Table E-9 presents the evaluation team's classification of individual BEE projects into these four categories. A breakdown of expenditures and receipts for these four categories is presented in Appendix Table E-10.

VIII. Organizational issues

Strategy

203. The objectives and strategy reflected in project planning documents were quite broad in scope. Essentially, SEED set out to promote the development of the private sector in three countries (later extended to four) by providing services directly to SMEs, building the capacity of organizations that serve SMEs, and taking steps to remove legal and regulatory constraints to the development of businesses.
204. In keeping with its broad mandate, SEED has undertaken numerous activities since its inception. There has been some degree of experimentation as the organization has worked to define its appropriate role in the different arenas in which it operates. In a conscious decision, SEED has undertaken a wide range of projects, particularly with respect to capacity building and the business enabling environment, with the notion of refining the strategy based on actual experience.
205. SEED has modified its strategy in light of lessons learned. For example, approaches to working with business associations and private consultants have changed considerably over time. In addition, new initiatives have been launched in certain areas such as business linkages, while others have been dropped such as tourism development. This evolution can be expected given the early stage of development of the organization and the changing circumstances within the countries in which it operates.

Organizational structure

206. The organizational structure is currently based on three teams – investment services (IS), financial management (FM), and private sector development (PSD). Each employee is assigned to one team which operates across offices; staff are responsible to the head of the team rather than a director of a particular office. This has two principal benefits. First, it has enabled the organization to address common problems and opportunities across the region, taking advantage of the knowledge of team members. Second, it affords economies of scale by enabling SEED to develop services that could be offered in multiple markets.
207. Discussions with SEED staff, however, suggest that this approach may not facilitate working relationships and knowledge sharing among different teams within offices (and across offices). For example, knowledge gained by the IS team in working directly with companies does not appear to be fully utilized by FM or PSD in carrying out their respective activities.

Integration with World Bank Group and other PDFs

208. SEED has participated in the development of country assistance strategies (CAS) and specific credits provided by the World Bank to governments in the region. Its involvement has been primarily informal based on ongoing discussions with IBRD representatives. Inputs provided by SEED have been well received.
209. SEED has also called on various experts from the IFC, the World Bank and other PDFs to work on some projects. With regard to the latter, SEED has called upon MPDF and SPFF staff to

advise on particular IS projects. In addition, as noted above, SEED has drawn on materials from MPDF in developing one of its training courses. SEED (and the SME Department) are endeavoring to increase the extent of knowledge sharing among the PDFs.

Coordination with Government and Donors

210. For the most part, SEED appears to have a good relationship with government agencies and other international donors throughout the region. Government officials interviewed as part of the evaluation spoke highly of SEED and indicated that the organization has been useful in terms of both advancing the interests of the private sector and providing useful services.
211. With respect to donor coordination, SEED has taken the lead in some countries to bring donors together to discuss issues related to SMEs and private sector development. According to a representative of one organization, in the past, these meetings have tended to center on “simple recitations of the plans” of each participating organization. However, donors are beginning to move toward more “focused conversations among key actors” to address coordination in service delivery. In part, this is being driven by a need to ensure that donors, to the extent possible, speak with one voice in advancing an SME agenda in particular countries.¹⁵⁸

Use of local consultants.

212. As discussed in more detail in the following section, SEED has competing objectives of building local capacity of existing consultants and supporting the efforts of staff to spin-off commercial ventures. On the one hand, SEED is interested in fostering the development of local consultants; on the other hand, SEED management needs to ensure that staff resources are well utilized and address the concerns that local staff have concerning the creation of potential competitors.¹⁵⁹ This has led to some conflict within the organization. For example, the IS team does not necessarily see the Consultancy Network as capacity-building effort – rather they view their involvement with consultants purely as a business relationship. While SEED has adopted a policy to use local consultants on IS projects, staff are not enthusiastically supportive. As one staff member expressed, “we are forced to use local consultants on every project, but some of my peers have been avoiding doing this over the past few months.”
213. Local staff are increasingly less interested in employing local consultants on projects for four reasons:
- Staff feel that consultants do not provide added value to projects. They are often late in delivering work products and the quality of work tends to be low.

¹⁵⁸ A recent evaluation of EBRD’s South East Europe Business Advisory Services Programme considers that the IFC and EBRD programs are not in competition with each other but suggests that there have been some tensions between the two. It recommends increased cooperation. See Investissement Développement Conseil, S.A., “EBRD/TMG South East Europe BAS Programme, Independent Operational Review,” June 2003.

¹⁵⁹ In correspondence with the evaluation team, SEED noted, “There was also a management decision that given budget constraints we were facing that we continue to optimize SEED staff resource utilization as much as possible (in line with skills/expertise needed on projects) and change our split between staff and consultant usage.” Data provided by SEED on actual usage of consultants suggest that the use of local consultants may be declining. See Appendix Figure F-1.

- At the same time, local consultants add additional costs to the project. Since staff are judged, in part, in terms of cost-recovery and their ability to complete projects within budget this poses a problem.
- Staff are concerned about developing competitors given the possibility that SEED will cease operation in FY05.
- Finally, local staff perceive that they are paid less than local consultants, contributing to some degree of resentment.¹⁶⁰

Information systems

214. SEED primarily relies on accounting and other information systems provided by the World Bank and IFC. Oriented toward the needs of a large financial institution, these systems have been insufficient for project management, reporting, cost accounting, and responding to the needs of multiple donors.¹⁶¹ In addition, certain elements of the system pose problems in implementation. While procedures for opening and closing a Work Breakdown Structure (WBS) element were put in place in FY03, the definitions of strategic objectives and individual projects used in the accounting system (WBS element) are not always clear or consistently applied. Moreover, data on individual projects are often aggregated at a level that makes analysis difficult.
215. SEED has made substantial progress in building its own information systems, including the development of the Project Tracking and Management Reporting System (PTMRS). This work has been done in-house in an effort to create a system that links various databases and is capable of generating reports needed by project managers, team leaders, the SME Department and donors. There are still areas that warrant attention. In particular, SEED's own database on training events, companies, and participants could be better designed and maintained, and linked more closely to the financial accounting system.
216. SEED has also taken steps to strengthen monitoring and evaluation systems. According to SEED, the organization currently surveys clients to obtain baseline data and gauge satisfaction at the end of every project and training seminar. In FY03, SEED began to survey training participants three months after the training was completed to assess impacts. The organization plans on conducting a similar follow-up impact survey of all IS clients six and 12 months after project completion. Because of the varied nature of BEE projects, evaluating their impact is necessarily project specific and long-term. The current plan is to evaluate BEE projects one year after they begin and every year after that as long as it remains "useful" to do so.

¹⁶⁰ It is worth highlighting that this is a perception of staff and is not necessarily accurate when one considers total compensation (salary and benefits) of SEED staff as well as the additional overhead costs that consultants carry, including unbilled days of work.

¹⁶¹ The deficiency of information system for the PDFs and other Donor Funded Operations (DFO) has been recognized by senior management of the World Bank and IFC. The organization recently approved a \$2.5 million initiative to "improve the effectiveness, efficiency and clarity of Donor Funded Operations as an integral part of IFC's business. "

IX. Conclusions

The original rationale for the establishment of the SEED remains sound.

217. In the aftermath of the disintegration of Yugoslavia, the private sector in each of the four countries faces significant hurdles resulting from undeveloped markets, unfavorable laws and regulations, limited access to capital, and inadequate management skills. SEED was seen as providing a vehicle for helping to spur the development of the private sector by providing needed services directly to SMEs, building a sustainable local capacity to continue to meet the needs of SMEs in the future, and pushing for desired government reform. In so doing, SEED was intended to complement the activities of other bilateral and multilateral organizations that were active in the region.
218. Survey results and interviews point to the limited availability of high-quality services at prices that companies can afford in all four countries. They also highlight the reluctance of companies to pay for services given uncertainties with respect to potential benefits. SEED has responded to needs in these markets, increasing the level and quality of consulting and training services available to SMEs at a price that clients are willing to pay.
219. In so doing, SEED is responding to conditions in markets that limit private investment. First, some of the services that SEED provides, particularly those related to the business enabling environment, may be considered public goods which are traditionally provided by government or civil society.¹⁶² However, most of the services that SEED provides are essentially *private* goods. Here, the argument for SEED intervention in markets is more complex, revolving around market failures and equity concerns. The basic argument is that the current level of services in the market is inadequate from a social perspective as a result of one or more of the following:
- **Imperfect information.** Efficient markets depend on people making informed decisions. However, people cannot make wise choices if information is unavailable, incomplete, overly complex or misleading. Particular problems arise if there are either significant transaction costs in obtaining the necessary information about the quality of a good, or if quality can only be judged after purchase and/or consumption as in the case of “experience” goods. Surveys conducted as part of this evaluation suggest that SMEs are unwilling to purchase consulting or training services at market prices, in part, because they have difficulty identifying their own needs, lack information on the quality of services offered by providers, and have difficulty in managing projects. While these companies may be interested in maximizing profit, the lack of information and associated transaction costs constrain their purchases. SEED takes steps to address this type of market imperfection by providing better information on services, reducing transaction costs, and lowering customers’ exposure to risk through the provision of subsidized services. Similarly, financial institutions may be reluctant to provide financing to SMEs and/or insist on high collateral requirements because they may not be able to assess

¹⁶² Public goods have two unique properties. First, consumption of a public good by one consumer does not affect the ability of other consumers to benefit from it (*non-rivalry*). Another way of describing this characteristic is that the good can be provided to additional consumers at virtually no additional cost. Second, it is impossible to stop people from benefiting from the good even if they are unwilling to pay for it (*non-excludability*). Because of these properties, there is little economic incentive for private companies to provide public goods.

risk appropriately and/or are uncertain about their ability to recoup losses in the event of default. SEED has tried to address this constraint, in part, through the preparation of business plans to support loan applications.

- **Externalities.**¹⁶³ The argument can be made that the prevailing market price for the types of services offered by SEED does not reflect the additional value that *other* companies or society as a whole derives as a result of the provision of services to particular customers. For example, survey results point to spillovers in the form of additional purchases of inputs resulting from the growth of SEED clients. They also highlight demonstration effects in which some companies are following the lead of SEED clients in effecting changes in their business operations. As such, the actions taken by SEED to stimulate demand for services, including the provision of subsidies, results not only in benefits to individual clients, but also additional benefits that flow to other firms and society at large.
- **Equity concerns.** Imperfect information and externalities both deal with allocative efficiency. However, SEED may also be concerned with equity. To a great extent, the existing distribution of income and wealth is determined by initial endowments of land, capital and labor skills in the country. Those who possess resources benefit more from the operations of the market. SEED's involvement in the provision of services can help ensure greater fairness by committing resources to under-served constituencies. For example, the subsidized work with women entrepreneurs, mushroom growers and other constituencies might be justified on equity grounds.

220. The findings of this evaluation generally support the original rationale for the program and suggest that it remains valid. However, while the original rationale for the establishment of SEED highlighted the importance of financing to the growth of companies stating, "the major constraint faced by the SMEs is the lack of access to capital," the value of working with companies to secure financing given *existing* conditions in financial markets is debatable.¹⁶⁴ This is not to say, that the availability of capital under acceptable terms is not an issue. Credit – particularly in the form of long-term loans – remains scarce and is accompanied by high collateral requirements. However, SEED's ability to help SMEs secure needed capital is constrained by existing bank policy: firms that lack collateral cannot access debt finance even with a solid business plan developed by SEED. As a result, SEED has placed less emphasis on helping companies to secure financing and greater emphasis on improving the management capabilities of firms and upgrading business operations. The results of the evaluation support the decisions that SEED has made in this regard. The question of how best to address capital constraints, however, remains open.

221. Finally, in terms of relevance of SEED's activities, the evaluation did not find evidence to suggest that SEED had crowded out commercial suppliers of comparable services. Approximately 81 percent of the consultants that responded to the survey perceive SEED as a collaborator rather than as a competitor. Moreover, the evaluation found that SEED had not duplicated efforts of other international organizations.

¹⁶³ Externalities arise when the production (or consumption) of a good or service affects parties other than those directly involved in the transaction. As a consequence, these spillover effects are not fully reflected in market prices. The issue of externalities is particularly important given ambiguous property rights and/or high transaction costs.

¹⁶⁴Originating IFC document.

SEED is providing services to companies and institutions in the target population.

222. SEED has provided services to SMEs, consulting firms, business associations, financial institutions and government agencies. As noted above, all of the entities were designated as targets of SEED's intervention in the IFC Board Report and subsequent business plan.
223. SEED defines the target market to include virtually all companies in the region. In practice, based on the results of the client survey, about 96 percent of clients had annual sales of US\$15 million or less at the time when they first started working with SEED, and thus would qualify under IFC's definition of SMEs. The majority of these clients have been private firms controlled by local investors.

SEED has made progress toward achieving intended outcomes.

SEED has done a great deal in a relatively short period of time.

224. Since its inception in mid-2000, the organization has established offices in four countries, built a highly professional staff, launched numerous initiatives, and established a good reputation among entrepreneurs, government officials and international donors.
225. SEED has provided services that are not widely available to companies or organizations in the four countries. Moreover, it does not appear to have crowded-out private consulting firms. In this regard, most consultants that responded to the survey do not consider SEED as a competitor and approximately two-thirds of clients that responded to the survey were unaware of other companies or organizations that could provide services similar to those offered by SEED.

Most clients are satisfied with the services provided by SEED and perceive value greater than or equal to fees paid.

226. An important determinant of success for any program is the degree of satisfaction among clients. In this regard, of the survey respondents, roughly 69 percent of IS clients and 80 percent of companies that participated in training were satisfied with the services provided by SEED. Similarly, 75 percent of IS clients and 79 percent of training clients believe that the value that they derived from SEED services was equal to, or greater than, the fees charged by SEED.

Most clients made changes in their businesses and reported improved performance, however, in most cases, these gains have yet to be reflected in higher sales, profit or employment.

227. Approximately, 82 percent and 88 percent of IS clients and training clients, respectively, reported making some change in their strategy or operations as a result of SEED services. As a result of these changes, 59 percent of IS clients and 46 percent of training clients reported improved performance along at least one dimension. However, only one-third of IS clients reported higher sales as a result of SEED services and 22 percent of training clients indicated that their sales increased as a result of SEED. In terms of net profits, the proportion of clients reporting gains is approximately 36 percent and 18 percent of IS clients and training clients, respectively.

228. IS clients that responded to the survey reported a total of approximately €3.3 million in additional sales in 2002 as a result of SEED services (mean=€654,000 and median=€154,000). The total sales impact reported by training clients was on the order of €47,000 (mean=€1300 and median=€0). With respect to employment, IS clients reported a total of 89 additional employees in 2002 as a result of the services provided by SEED (mean=18 and median= 7). The number of additional employees reported by companies that participated in training programs was 516 (mean=6 and median=0). As can be seen, reported impacts are highly skewed; a few companies account for the bulk of aggregate sales and employment gains.¹⁶⁵
229. While most companies report making changes, it is apparent that these changes have not yet translated into substantial gains in sales, profits or employment. This may be due to a variety of reasons. First, companies may not have implemented changes in an appropriate manner. Interviews with some companies indicate that they may have difficulties implementing recommendations offered in the IEP due to inadequate management capabilities and/or inability to secure needed resources. Second, since companies have only made these changes recently (within the past two years), it may simply take longer for performance impacts to be realized. Third, companies may need to carry out additional changes in order to achieve higher levels of performance, i.e., the changes that they have made are necessary but not sufficient to yield higher sales, profits and/or employment. Finally, it is possible that the changes that are being made are not relevant to these objectives.
230. Most companies appear to be able to meet financial obligations without infusions of cash from owners and enjoy some degree of profitability. However, some face difficulties given unfavorable market conditions, persistent operating problems, existing financial difficulties and/or lack of management capabilities. Moreover, the success of businesses, in general, in each of the countries in which SEED operates is threatened by the political and economic factors outside their control.

SEED has helped arrange approximately €2.5 million in debt and equity for ten companies, but not all believe that SEED played an essential role in this process.

231. SEED has completed investment plan projects with 20 companies. Ten of these firms were able to secure some or all of the financing needed for planned investments. Eight of the companies have already completed or plan to complete investment projects within the next year, representing a total investment of €9.5 million. One of the projects has been indefinitely postponed and the status of the other is unknown.
232. However, not all of the companies believe that SEED played an essential role in this process. Four of the companies that received financing believe that they could have done so on their own. Five of the firms that received financing believe they would have gone ahead with their respective projects without SEED's assistance.

¹⁶⁵ It is important to keep in mind that the estimated impacts on both sales and employment are based upon a different number of respondents from IS and CB-SME clients respectively. Since CB-SME had a higher number of respondents, this is likely the reason that the number of total additional employees reported is higher as well.

SEED has enhanced the capacity of local consultants, business associations, and local economic development organizations to deliver services to SMEs; however, thus far, the impact on SMEs appears limited.

233. The role and impact of SEED varies according to the type of service provider:

- **Local consultants.** SEED has carried out a broad spectrum of classroom and on-the-job training targeted at member of the Consultancy Network or other services providers in the region. One objective of SEED has been to encourage consulting firms to develop and deliver new services aimed at SMEs. So far, it appears that SEED has been more successful in enhancing the capacity of firms that are part of the network. In this regard, 94 percent of the network firms report that they offer services based on content or techniques obtained through SEED. In contrast, 44 percent of companies outside of the network are providing services based on SEED materials, though 80 percent intend to do so in the future. The reason for the marked difference between the two groups is due foremost to the fact that members of the network work on investment service projects with SEED staff. They may also be better able to absorb and apply the techniques obtained from SEED given their skills and nature of their business. Many of the non-network firms that attended train-the-trainer courses appear to focus on services not related to SEED training.

While the market for services may expand in the future, thus far, half of the survey respondents that have used SEED materials have done so with three or fewer of their clients. This could be due in part to local market conditions. More specifically, according to survey respondents, the overarching constraint on the development of the consulting market is the unwillingness or inability of SMEs to pay prevailing rates for services.

There is some evidence that SEED is helping to lessen this constraint. For example, 43 percent of SMEs that respond to the survey indicated they were more likely to use private consulting and/or training services in the future as a result of their interactions with SEED.

- **Business Associations.** SEED has worked with a number of business associations in the region since late 2000, providing training, technical assistance, and, in some cases, funding for specific activities. As a result of initial efforts with business associations that had little impact, SEED changed its approach. A new initiative launched in the fall of 2002 has already met with some success. SEED has helped six associations to develop strategic plans, define member services, and increase their membership.

With one noted exception, associations have not yet assumed a strong advocacy role. SEED's expectations concerning the ability of the associations to become an effective voice for businesses may be unrealistic. The political process is fluid and some associations do not want to assume this role until they establish a stronger membership base.

Moreover, in order to be sustainable, organizations need to have a strong financial foundation. In this regard, the financial viability of some associations is questionable.

- **Local Economic Development.** Since March 2002, SEED has been working with two municipalities – Zenica and Prijedor – to develop strategies to promote SMEs and foster economic growth in the local regions. In working with SEED, community members indicated they had learned a great deal about analytical methods and participatory planning processes. Both communities have drafted preliminary strategies, which included four priority projects:

one-stop-shop development agency, financial support fund, business incubator, and business zones.

In March 2003, when the evaluation team conducted its fieldwork, the municipalities were beginning to refine plans for specific projects. However, the source of funding to implement these projects was not clear and the municipalities were looking to SEED to help arrange funding from international donors. (The evaluation team was recently informed that Prijedor opened a one-stop-shop in October 2003.)

SEED has contributed to specific reforms aimed at enhancing the business environment.

234. SEED has undertaken a number of projects targeted toward legal and regulatory reform. In some cases, the assistance provided by SEED and ensuing dialogue have led to changes in specific laws and regulations. The major success in this regard has been related to the introduction of legislation dealing with leasing in FYRM and Serbia and Montenegro. In both instances, SEED marshaled technical expertise to deal with substantive issues related to proposed reforms. It has also dealt directly with key decision-makers within ministries that have direct responsibility for the formulation and implementation of policy. However, while legislation has passed, the impact on SMEs has yet to be felt. It will take some time for leasing companies to be established, particularly firms that focus on capital equipment rather than consumer goods.
235. SEED has participated in policy discussions with government official and international organizations and taken steps to foster greater dialogue among key stakeholders on the needs of SMEs. As part of this process, SEED contributed to the formulation of the Business Adjustment Credit in BiH. The results of the effort of SEED and other parties to help reform various regulations and administrative procedures, such as those dealing with business registration, have yet to be realized.

While it is too early to judge the overall efficiency of SEED, some activities are more cost-effective than others.

236. Through 31 December 2002, SEED had spent US\$12.6 million. Roughly 46.1 percent of this amount has gone to programs. General management and administration accounted for 48.5 percent of total expenditures and start-up (non-recurring) expenses accounted for the remaining 5.4 percent. The activities and outcomes described above need to be considered within the context of these expenditures.
237. However, it is important to recognize that this is a mid-term evaluation. SEED officially began operations in September 2000. A good deal of effort and resources during the first two years of operations was committed to establishing offices in four countries, building staff capabilities, developing products and services, experimenting with various approaches, and building a name for the organization throughout the region. In many respects, it is too early to judge whether the monies invested in SEED have been well spent – there is an inherent mismatch in the timing of costs and benefits; while a significant share of costs are front-loaded, many of the outcomes that SEED is attempting to achieve are best considered over a longer horizon.

238. With this in mind, the following comments should be seen as an initial take on the cost-effectiveness (efficiency) of SEED. They are intended to prompt discussion, rather than stand as definitive conclusions:

- **IS.** In assessing the efficiency (cost-effectiveness) of investment services, it is important to keep mind that the survey only included companies that completed IS projects up to the end of Q1FY03. As such, impact should be compared to program expenditures in the same time frame. SEED spent roughly US\$3.0 million from inception through Q1FY03 on Investment Services, including direct project expenses, indirect program expenses, and allocated SEED overhead.¹⁶⁶ Only five clients provided an estimate of the impact of the program on annual sales and employment. These companies attributed a total of €\$3.3 million (or US\$3.1 million) of additional sales and 89 additional employees in 2002 to the assistance that they received from SEED.¹⁶⁷ Gains made by companies are likely to continue for some time to come. It is also important to recall that other clients reported gains in sales and employment, but were unable to quantify the impact. As such the figures cited above likely represent a lower bound on the impact of investment services on sales and employment.

With respect to the cost of securing financing for clients, SEED spent approximately US\$526,000 (including indirect program expenses and allocated overhead) on IEP and IP projects with seven clients to secure US\$1.86 million in financing. In addition to the financing raised, companies reported other benefits from the services provided by SEED.¹⁶⁸

- **CB-SME.** SEED spent roughly US\$2.4 million from inception through Q1FY03 on CB-SME, including direct project expenses, indirect program expenses, and allocated SEED overhead. Of the companies that received training and responded to the survey, 36 firms provided an estimate of the impact of the program on annual sales and 86 companies gave an estimate of additional employment. These companies attributed a total of €47,000 (or US\$45,000) of additional sales and 516 additional employees in 2002 to the assistance that they received from SEED.¹⁶⁹ For the reasons cited above, these figures are likely a lower bound on the impact of training programs.
- **CB-BDS.** SEED spent roughly US\$4.5 million from inception through Q2FY03 on CB-BDS, including direct project expenses, indirect program expenses, and allocated SEED overhead. Approximately 58 percent, 8 percent and 7 percent of these monies have been committed to efforts to promote the development of local consultants, business associations, and local economic development organizations, respectively. The remaining 27 percent has gone to a variety of projects.

As noted above, the organization has made progress in enhancing the capacity of local consultants, business associations and local economic development organizations. The relatively small amount of resources invested in business associations (US\$343,000) and local economic development organizations (\$321,000) may yield significant social and

¹⁶⁶ The overhead allocation rule applied to this period is the same as used throughout the report.

¹⁶⁷ The US\$ figure is based on an average exchange rate of US\$0.95 per €1.00 in 2002.

¹⁶⁸ Cost data for three of the ten companies -- Galanteria, Hotel Jakova, and ABBA Trade -- that secured financing were unavailable. For the 17 firms that completed an IP prior to the end of Q1FY03, total SEED expenditures are estimated at US\$1.16 million. These companies paid SEED a total of roughly US\$49,000 for services provided. Therefore, the net cost to SEED was roughly US\$1.1 million.

¹⁶⁹ The US\$ figure is based on an average exchange rate of US\$0.95 per €1.00 in 2002.

economic benefits in the years to come.¹⁷⁰ With a better defined direction and an expanded membership base, business associations are in a better position to provide services to hundreds of companies in the region and serve as an effective advocate for member interests. At a minimum, working with local communities has fostered greater dialogue among government, the private sector and the general public. It is also leading to some actions, albeit modest, to provide better services to local firms.

The cost-effectiveness of activities designed to promote the development of local consultants is less apparent. As noted above, SEED has spent upwards of \$2.6 million on these efforts when direct project expenses, indirect program expenses, and allocated SEED overhead are taken into account. Based on responses to the survey, interviews with consultants and discussions with SEED staff, it is hard to conclude that results – in terms of developing local consultants that can provide high quality services to a significant number of SMEs – have been commensurate with this level of investment. In particular, the train-the-trainer courses provided by SEED do not appear to have led to the widespread use of SEED training materials by local consultants. In fact, according to SEED management, SEED decided to adjust its approach to building local capacity following an internal assessment. SEED concluded that consultants were unlikely to offer courses to their own clients based on what they had learned at these sessions. At the time of the evaluation, SEED was taking steps to adopt a new approach that focuses on building the capability of faculty at universities to establish ongoing training programs for SMEs.

- **BEE.** Through Q2FY03, SEED had invested a total of US\$1.7 million in efforts to strengthen the business enabling environment. Some of these activities have resulted in concrete reforms such as the establishment of leasing legislation in the Republic of Serbia and FYRM. Others, while yet to yield specific changes in laws and regulations, have led to exchange of ideas among representatives of international donors, government and the private sector. Like much of the reform efforts in the Balkans, there is long way to go before the reforms to which SEED has contributed are fully implemented and have a significant impact on the performance of SMEs.

Given its current cost structure, the services offered by SEED are not commercially viable.

239. SEED was established to promote the growth of the private sector in four countries by providing a range of services aimed at developing individual businesses, strengthening providers of business services, and enhancing the environment in which businesses operate in the region. While the organization has charged for some of its services, it was never intended that SEED recover the full costs of its operations from client-paid fees. As originally designed, SEED was expected to generate roughly seven percent of its total operating budget through fees over its five year life. It was anticipated that these fees would be derived primarily through enterprise-level services. Table 38 presents actual cost recovery through Q2FY03.

¹⁷⁰ Figures include direct project expenses, indirect program expenses and allocated overhead.

Table 38. Client-paid fees as a percent of Expenditures

	Direct Project Expenses	Total Expenditures
Investment services	21.7%	4.8%
CB-SME	15.2%	3.9%
CB-BDS	6.7%	2.3%
BEE	0.8%	0.3%
Total	10.4%	1.5%

240. Commercial viability means that an organization obtains revenue from the sale of services sufficient to cover *total* costs. Services offered under CB-BDS and BEE are not expected to be commercially viable. However, the potential for offering services to companies on commercial basis is being actively considered.¹⁷¹

241. While cost recovery has increased, SEED is still far from generating sufficient fees to cover the *direct project expenses* associated with IS and CB-SME services. When indirect program expenses and allocated overhead are included, the gap increases significantly. For the current services to be commercially viable, SEED would need to reduce costs and/or increase prices dramatically without a significant decrease in the volume of business.¹⁷² However, given that the majority of clients state that the value of SEED services is equivalent to fees charged, the prospects of being able to raise prices without experiencing a drop in demand is unlikely. From a cost perspective, SEED would need to reduce *direct project expenses* while still providing the same quality of services. It would *also* need to take steps to reduce the fixed cost of operations beyond the 14 percent attributed to being part of the IFC structure.

242. This is not to say that it is impossible for SEED staff to leave the organization and establish commercially viable consulting firms based on know-how and materials developed under the auspices of SEED. These spin-off firms would need to redefine services based on their own expertise, establish lower cost operations, and adopt an appropriate pricing strategy. It is unlikely that a commercial venture based on brokering the services of third-party experts can be viable without support from international donors.

¹⁷¹ SEED staff presented ideas for spinning off services on a commercial basis to donors in June 2003.

¹⁷² SEED cannot cover total costs by increasing volume given that current fees do not cover variable (direct) costs of projects.

X. Recommendations

Donors should explicitly state whether they intend to continue funding SEED beyond FY05.

243. Donors' commitments are based on the originally planned five-year life of SEED which ends in FY05. The organization has funding in place for the next two years. However, it is not clear what donors expect to happen beyond this point. Uncertainty with respect to future funding places the organization in a difficult position. For example, without a clear commitment of ongoing support, staff are likely to begin to seek alternative employment. Furthermore, companies and organizations may be unwilling to invest in building partnerships with SEED not knowing whether SEED will be in existence two years from now. As a result, the ability of SEED to achieve its objectives over the next two years may be compromised.
244. A statement concerning donor expectations is needed. As noted above, the original rationale for SEED still applies – there are still numerous constraints to the development of a thriving private sector in all four countries. As such, donors should address the prospects for continued support and any conditions under which such support would be provided. They should also address issues related to potential commercial spin-offs (see below).

SEED should define its objectives with respect to spinning-off commercial ventures and formulate an explicit strategy.

245. One of the goals of SEED has been to “leave a legacy of sustainable consultant and training capacity” in the region.¹⁷³ SEED management (and the SME Department) have interpreted “capacity” to include members of SEED staff as well as local firms. SEED has expected that staff would gain sufficient skills and experience to enable them to find ready employment with other firms or start their own companies at the end of SEED’s five-year life. Members of the staff have been discussing the potential for spinning-off commercial operations for some time.¹⁷⁴ Some staff have already expressed an interest in leaving to set up their own consulting firms; however, interest seems contingent on being able to secure a contract with SEED for ongoing work, e.g., local economic development.
246. According to SEED management, there is no expectation that SEED, as an institution, will become a commercial enterprise. SEED recognizes that its mission (particularly as it relates to strengthening the business enabling environment) requires ongoing donor support. However, SEED management has indicated that it expects (and hopes) that some staff will establish commercial enterprises based on the know-how and methods obtained during their employ at SEED.
247. There are numerous issues that need to be resolved to ensure that SEED continues to focus on meeting its primary mission over the next two years, while paving the way for staff to establish

¹⁷³ Originating IFC document.

¹⁷⁴ For example, the SEED’s Annual Report (2002) contains the following statement, “Those staff involved in commercial projects have formed a regional working group to develop a business plan for their eventual spin-off from SEED into a private consultancy.”

new commercial ventures. SEED should clarify objectives and strategies with respect to commercial spin-offs as soon as possible.¹⁷⁵ In so doing, SEED needs to consider how to deal with the following:

- Create incentives for staff to remain at SEED over the next two years and/or begin to phase out certain services in an orderly manner.
- Resolve the tension between the use of local consultants as a means of building local capacity and the interest of staff to develop their own viable businesses.
- Develop policies with respect to the ownership of the SEED “brand” and other tangible and intangible assets owned by IFC/SEED.
- Help staff build capabilities based on functional expertise (such as financial analysis, market research, or information systems) and/or domain expertise based on in-depth knowledge of particular subjects (such as industries, technologies or policy areas).
- Help staff develop business plans for proposed commercial ventures based on sound market research. In this regard, it will be important to determine how well potential customers will receive these businesses once ties to the World Bank are severed and companies are forced to sell services at prices that cover the full cost of operations (including foreign consultants, if required).
- Help staff gain experience managing a commercial enterprise. Individuals within SEED who have an entrepreneurial bent will need to gain additional capabilities over the next two years to be able to manage a commercial firm and market services to a broad range of customers, including international organizations.

248. With regard to the latter, SEED should consider shifting responsibility for specific practices in different countries to particular individuals and let them run them as small business units (SBU) within SEED. This would entail giving individuals profit and loss (P&L) responsibility for their unit with the task of managing product development, marketing, human resources, and financial matters. SBU managers should move from managing against a fixed budget to managing with specific business objectives in mind (e.g., sales growth, profitability, etc.)

SEED should focus its efforts on a narrower set of activities and provide more intensive services to clients.

249. SEED has evolved a great deal since its inception in light of actual experience and continues to refine its role within the mandate given to it by IFC and other donors. The organization recognizes that there is a need to focus efforts and has already taken steps to reduce the scope of its activities. SEED is now in the process of refining its strategy based on experience gained over the past few years. Given the results of the evaluation, as part of this process, SEED should consider undertaking the following in order to yield more immediate and significant impacts:

- SEED should place an even greater emphasis on the provision of management consulting services to SMEs to enable them to use existing assets more productively, rather than attempting to help companies to secure financing. Given this focus, SEED should consider

¹⁷⁵ In June 2000, SEED staff made a related presentation to SEED donors.

how best to provide more intensive follow-up services to help companies implement recommendations and address issues that constrain growth and profitability.

- SEED should focus on developing SME training programs that address critical issues within companies based on a thorough analysis of IEP projects. SEED should take steps to ensure that IS clients are kept informed of training programs and are encouraged to attend.
- Given limited market demand, SEED should reduce the level of expenditures allocated to broad-based efforts to develop local private consultants, and shift resources to using local consultants on SEED client projects in order to provide greater opportunities for on-the-job training as part of more intensive interactions. Moreover, the new approach that SEED has adopted to build the capacity of local providers should be evaluated early-on to gauge whether it is likely to be successful.
- SEED should continue intensive work with selected business associations that offer significant promise, concentrating on efforts to ensure that they expand membership, institute needed members services, and establish a sound financial footing.
- SEED should focus on specific government reforms that have a direct bearing on the performance of SMEs, and in areas where SEED (or IFC) has developed certain expertise such as leasing. In this regard, the organization should work to ensure that reforms are well-conceived, adopted by legislative and regulatory bodies, implemented within relevant institutions, and carried out in a way that meets the needs of SMEs. This will likely entail more intensive, longer-term efforts that require careful coordination with other international donors.
- SEED should consider what role, if any, the organization can play in reducing capital constraints faced by SMEs given high collateral requirements. This issue is likely to require actions on multiple fronts, including the establishment of credit guarantees and pledge registries as well as reform of bankruptcy and other laws.

SEED should consider reorganizing its operations based on countries and practices.

250. SEED should consider adopting a matrix management structure built around countries and practices. The latter could be defined by type of client (e.g., private business, government, or international donor) or product (e.g., strategic planning, market research, or information system).
251. Matrix management would help promote cross-practice interactions within countries based on country-specific objectives, while also enabling staff to be part of peer groups with shared responsibility for accomplishing objectives related to particular practices. Staff would be responsible to their respective country manager; however, staff would also report to designated practice leaders.
252. Country managers would have responsibility for supervising staff in their office and achieving specific goals and objectives for the country. Practice leaders would oversee efforts to develop new products, train staff, and market services in each of the four countries. To be effective, it will be imperative for all staff to have a clear understanding of the goals, objectives, and performance metrics for which they will be held accountable with respect to both countries and practices.

SEED should reconsider its pricing policy, beginning with a clear articulation of objectives.

253. SEED is similar to a private company in that it competes on the basis of quality and price. However, unlike a for-profit firm, the organization also has explicit development objectives. Before setting prices, SEED should specify the objectives of its pricing policy. These objectives could include one or more of the following:

- Maximizing the use of the service among customers in the *target population*;
- Recovering the costs of providing the service;
- Exerting downward pressure on prevailing market prices for the service; or
- Maximizing profits (or surplus).

254. With objectives defined, SEED should then take steps to determine the specific prices for particular services. As part of this process, it needs to consider how customers are likely to respond to different prices, prices charged by other organizations for similar services, and its own cost structure.

255. As part of this process, the organization should tighten up the policy with respect to what it charges particular companies for services. The extent of the subsidy extended to specific companies should be based on explicit guidelines rather than left to ad hoc decisions to ensure fairness and transparency. The magnitude of the subsidy extended to particular firms should be made transparent so that companies will understand the true cost of service delivery.

SEED should continue efforts to strengthen information systems.

256. While SEED has taken significant steps to develop its own information systems to supplementing those provided by the SME Department. These efforts should continue. Cost accounting should be a fundamental part of financial management, complementing traditional financial accounting systems. Managers should know how much it costs to provide specific services as well as how much revenue it earns from these services in order to make sound business decisions and ensure adequate accountability to all stakeholders. In this regard, SEED should define, measure and assign direct *and* indirect costs to specific outputs (e.g., IEP, IP, training courses, etc.) on a systematic basis.