

Access to Finance for Small and Medium Enterprises (SMEs)

Since its creation in 2000, IFC's Capacity Building Facility (CBF) has sought, as one of its key goals, to increase the access of small and medium enterprises to finance. To that end it has pursued three strategies: direct support to financial service providers; capacity-building assistance to network support organizations that assist financial service providers and investment funds; and knowledge products designed to help create more effective programs. An evaluation of the facility's 39 access-to-finance projects shows that IFC's private-sector focus puts it in a unique position to support the development of sustainable, local financial systems that can support small and medium enterprise. Further, the evaluation shows that IFC's access-to-finance projects are most effective when coordinated with the IFC investment and advisory services offered by IFC's regional facilities.

This note synthesizes an evaluation of 39 Access-to-Finance projects that as of May 2005 had received \$8.5 million from the CBF, a trust fund established in 2000 to promote the development of small and medium-size enterprises (SMEs) through grants for innovative and pilot projects. The projects were assessed according to five sets of indicators: The projects were scored on five issues: outcome effectiveness, design, project management, cost effectiveness, and the innovation value to IFC. The importance of these indicators varied from project to project. For example, IFC undertakes some projects in order to explore the potential of new institutional forms or implementing partners. Such projects can generate innovation value regardless of outcome effectiveness, as long as they are designed and managed appropriately. At the same time, the evaluation demonstrated consistent correlations between certain management practices and project design features and results related to outcome effectiveness, cost effectiveness and innovation value.

FINANCIAL SERVICE PROVIDER PROGRAMS

The Access-to-Finance program has provided direct funding to 23 financial service providers. Four were evaluated in depth:

- Sacombank (Viet Nam). The project funded portions of a broad restructuring initiative aimed at improving the bank's core management capacity and developing

systems for an SME lending program. The bank achieved over 80 percent growth in two years in a US \$378 million portfolio, over 50 percent of which is invested in SME loans.

Findings on Project Effectiveness

- Projects are most viable and scalable when developed within commercially-structured institutions.
- Projects that support for-profit commercial models leverage IFC's unique strengths, and contribute significantly to innovation in the financial-services industry.
- Many projects involving non-profit financial service providers or network support organizations (NSOs) pose significant challenges. In some cases, the non-profit structure preempts an investment role for IFC and undermines IFC's capacity to support commercialization.
- Most projects measure the growth in services (for instance, number of clients, growth in portfolio or savings, or number of trainees) as an indicator of client impact. This is probably valid, but IFC may need some measures of the real impact on final borrowers to develop a more nuanced appreciation for the relative value of different types of financial services and institutions.

- Bank South Pacific (BSP). The project focused on developing the bank's SME lending systems. Quarterly reports indicate a ten-fold increase in monthly SME loans (2,475 approvals per month, averaging US\$1,265 each in February 2005), geographic expansion and robust performance of the credit scoring system.
- IPC/Novobanco. The project funded a strategic partner that performed preparatory work associated with a launching a start-up bank.
- ACCION/Genesis. The project supported a network support organization that provided technical advice to Genesis, a Guatemalan non-profit microfinance institution (MFI). Genesis made significant operational improvements, but failed to transform into a commercially structured financial institution.
- Women's World Banking (WWB), a non-profit organization that maintains a network of relationships to microfinance institutions in developing countries (IFC project supported WWB's Affiliate Capitalization Facility, a vehicle for capitalizing WWB's non-profit affiliates).
- The Foundation for International Assistance International, Inc. (FINCA), a nonprofit organization that provides financial services tailored to the needs of the working poor in countries around the world. The IFC project supported efforts by FINCA to transform its non-profit affiliates into commercially viable financial service providers.

The Sacombank and Novobanco projects supported concurrent IFC investment programs. In Sacombank, IFC is directly involved with bank management regarding the restructuring program, as well as negotiations with large strategic investors, and it managed the performance of the Novobanco initiative from its position as one of the investors financing start-up costs. Although IFC has no parallel investment in the BSP project, the project was administered directly by the Pacific Enterprise Development Facility (PEDF) under contract with the BSP.

In contrast, the Genesis project demonstrates the added risk of access-to-finance projects where IFC lacks a direct stake. In it, a merger attempt failed in part because of management reticence and inability of the Genesis board of directors to keep the process on track. If IFC or ACCION had entered into the initiative as potential investors, they would have been better positioned to detect and influence these issues at an earlier stage.

While performance metrics are generally inadequate to measure overall institutional performance in financial service providers, projects with parallel IFC investments benefit from complementary performance monitoring. Still, IFC's capacity to assess and monitor financial service providers would be enhanced significantly with more robust performance indicators for the institutions' financial performance, service delivery and operational efficiency.

NETWORK SUPPORT ORGANIZATIONS (NSO)

The CBF has supported seven access-to-finance projects that support international networks of financial service providers or investment funds. The four Network Support Organizations reviewed as part of this evaluation include:

- SEAF, an investment fund management company with a portfolio of funds specializing in SME investments in developing countries.
- Shorecap Exchange (SCE), a subsidiary of an investment fund management firm that provides technical assistance to the financial service providers in which the fund invests.

Findings on Project Design

- IFC brings funding, experience, and prestige to an emerging commercial initiative. When it engages in an investment or advisory relationship with the implementing partner, it can use an access-to-finance initiative to make lasting improvements in the operational capacity of the implementing partner.
- Projects in which IFC has an investment at stake generate more robust and timely information, develop better management, and have clearer deliverables and objectives related to viability and scalability.
- Projects that provide funding to organizations without IFC investment or direct participation are indistinguishable from the grant programs of many other donor agencies. In such projects, IFC's project design and management is less rigorous than that of other donor agencies who dedicate significant resources to managing grant programs.

PERFORMANCE OF NSO PROJECTS HAS BEEN MIXED

All four NSOs are nonprofit organizations that aspire to create, support, or manage commercially viable financial institutions or investment funds. They had some important successes. The SEAF project was highly effective in creating information technology capacity that significantly improved the organization's financial management and efficiency. SCE was launched with a capitalization plan that projected \$8.5 million in grants. The WWB's Affiliate Capitalization Facility sets high standards for affiliate financial performance and commitment to the microenterprise sector; most of its recipients have achieved impressive rates of growth, commercial funding, and profitability since receiving project funds. And the subsequent evolution of the affiliates suggests that FINCA is in fact developing commitment and capacity to support commercially viable and scalable institutions.

However, the long-term success of the NSOs in their respective roles depends on their ability to perform at commercial standards of technical capacity and financial viability. While access-to-finance project objectives generally are clear about the deliverables expected of the NSOs, all of the

Findings on Project Management

Management of access-to finance projects has suffered from lack of staff continuity, sporadic coordination with IFC investment operations, and low allocation of resources and staff incentives for the task managers. Lack of management attention to stand-alone advisory projects appears to be the principal factor, since IFC performs these same functions well in investment operations, often with the same implementing partner.

projects fail to address some significant gap in the organizations' capacity to play their respective roles by commercial standards. This lack of precision regarding the institutional model of the NSOs is likely due to the experimental nature of the access-to-finance projects, which were conducted in part to explore the potential of the non-profit organizations.

Findings on Cost Effectiveness

- Access-to-finance projects are generally well leveraged; most finance less than 20% of total project costs.
- It is possible to be over-leveraged, in which case competing objectives or requirements of other donors may dilute project objectives and IFC's technical contribution.
- The transaction costs associated with technical assistance and investment operations with individual financial service providers are high relative to the scale of these operations. This is why IFC has attempted to convert network support organizations into holding companies, so they can serve as future collective investment vehicles.

KNOWLEDGE PRODUCT PROJECTS

The CBF has funded nine initiatives that produced feasibility studies and standardized financial and non-financial products for replication. Three were chosen for in-depth analysis:

- The Technical Assistance Facility for Financial Intermediaries (TAFFI), which sought to build general training capacity within existing training facilities.
- The International Finance and Banking Academy (IFBA), which was designed to produce feasibility studies and business plans for sustainable bank training facilities in West Africa. The feasibility studies identified unmanageable challenges to the initiatives and further activity was suspended.
- The Leasing Manual project, which documented IFC's institutional experience in developing the operational, accounting and regulatory aspects of leasing industries in developing countries.

All three projects were designed to produce an intermediate

input for future initiatives. The TAFFI project supported efforts by GTZ to deliver general bank training courses. While it focused on developing training methodologies and training facility trainers, it ignored issues related to the sustainability and scalability of the training institutes themselves.

IFBA illustrates how a project can have value even if it does not seem to be effective: it answered a well defined question about the commercial feasibility of bank training services in West Africa. The Leasing Manual project documented a clearly defined model for future IFC support to leasing initiatives; the coordination of contributions from IFC technical staff not only produced an excellent product but also built a community of specialists that can be mobilized for future projects.

The Leasing Manual Project succeeded in documenting IFC's institutional experience and creating mechanisms for knowledge sharing and cooperation between leasing specialists within IFC. It serves as a guide for regional office to provide comprehensive support to a leasing development program on a country level. The achievements of the project will likely enhance IFC's profile as a leading agency in developing leasing institutions and markets, and strengthen IFC's role as a technical advisor to banking authorities in developing markets. Expansion of services to SMEs will be a downstream outcome if the manual is successfully employed.

Findings on Innovation Value

- Some access-to-finance projects have significant value because they are innovative, even though their results may not seem impressive.
- Exploratory projects that were not structured to monitor a well defined experiment produce little observable value for IFC or the implementing organization.
- Information exchange between facility task managers and investment project portfolio officers tends to be robust when a project supports activities key to the success of the investment operation; without this link, knowledge management tends to be less organized.

CONCLUSIONS

Access-to-finance projects perform best when they are coordinated with direct IFC investment. Investment operations generate synergies in program design and management that compensate for the inherent difficulty of funding technical assistance to external organizations. They help IFC to identify institutional weaknesses and to focus its technical assistance accordingly, and they engage IFC in management decisions that shape the overall development of the partner organization. An investment relationship also creates a long term obligation in the partner organization to IFC.

The main strength of IFC's access-to-finance program lies in its capacity to support the development of commercially

viable service providers. Access-to-finance projects are most robust when developed within commercially-structured institutions—in the case of financial service providers (FSPs), licensed and regulated financial institutions. IFC's expertise in promoting commercial viability is particularly valuable in emerging markets where innovative non-profit institutions are seeking to become sustainable financial-service institutions.

IFC is unique among development agencies, donors, and investors for its ability to leverage supports to financial institutions and markets. Unlike most bilateral and multilateral organizations, which have to channel resources through the public sector, IFC can invest directly in private companies. IFC also can make investments at earlier stages of institutional development—in greenfield operations, for instance. At the same time, as a member of the World Bank Group, it can engage policy makers on financial sector matters.

RECOMMENDATIONS

Program Strategy

IFC should focus its access-to-finance advisory services on initiatives that leverage its investment capacity. Such a strategy would use access-to-finance projects to extend the traditional frontiers of IFC investment operations and advisory services.

IFC should develop a deliberate strategy for helping capable, motivated non-profit organizations to transform their access-to-finance initiatives into commercially viable institutions. IFC has experience with corporate governance, institutional models, and funding mechanisms, so it is well positioned to help leading edge non-profit financial service providers and network support organizations transform their access-to-finance initiatives into commercially-oriented institutions.

IFC should strategically select retail microfinance institutions for direct IFC investment and advisory services. The high price tag for individual investments in emerging microfinance institutions will be cost effective in the long run if IFC can build capacity in network support organizations and investment funds that will replicate access-to-finance initiatives. IFC will have to partner initially with the network support organizations in individual retail institutions in order to define its long term market niche and to build durable capacity within these organizations.

Project Management

IFC should professionalize technical assistance management and improve coordination with investment.. The quality of project design, management and effectiveness of technical assistance projects will match that of other IFC business lines when they receive the same level of manage-

ment attention and recognition. The best access-to-finance projects have been created by innovative IFC staff who sought to enhance investments or extend IFC advisory capacity. Given mandate and incentive, IFC staff would do more of the same.

IFC should identify aspects of the institutional model that are critical to the commercial success of the venture. Access-to-finance projects should spell out and monitor expected outcomes related to the corporate governance, financial performance, service delivery and regulation of network support organizations and financial service providers. This is particularly important in projects that support non-profit organizations that are engaged in commercial ventures.

IFC should establish metrics to measure the performance of implementing organizations according to commercial industry standards. Industry-specific indicators are needed to assess the performance of financial service providers and network support organizations. For financial service providers, standard indicators of financial performance should be supplemented with performance indicators for portfolio performance, operational efficiency and service delivery. Performance standards for network support organizations should reflect the business model of their funding initiatives (e.g., equity fund manager, strategic partner, bank holding company, etc.). Since most NSOs engage in multiple lines of activity, IFC will have to develop an appraisal format that also measures the capacity of NSOs as related to the specific funding role that are of interest. IFC should refer to its own due diligence standards for investment operations in similar initiatives as a model for financial performance metrics.

IFC should publish performance indicators for financial service providers and network service organizations. Systematic disclosure of performance indicators would benefit future operations of IFC as well as the development finance industry in general.

IFC should develop mechanisms that facilitate knowledge management. Information about project performance plays a critical role in at least three phases of project administration. Guidelines and lessons from previous projects should inform project design and selection; performance information should be organized and available during project execution; and project performance should be organized and cataloged for future analysis and project design. Standardization of performance metrics would facilitate knowledge management.

IFC should calculate benchmarks for the investment required to build prototype financial institutions that specialize in lending to small and medium scale enterprises. An objective assessment of historical costs associated with the creation of model SME financing programs, greenfield commercial banks, and transformation of non-profit organizations into commercial banks would help define standards for cost-effectiveness.