

1 + 1 = . . . 50 Million!

It takes two arms to carry something securely for a long time without dropping it. This is a story of how two arms of IFC—investment and advisory services—successfully cooperated and helped each other to develop, nurture, and carry a client relationship that eventually led to an \$8 million investment deal and another \$42 million in the pipeline.

BACKGROUND

Since its independence in 1991, Ukraine has moved from a closed, planned economy to one of the fastest-growing, dynamic economies in Europe. Local businessmen have displayed entrepreneurial spirit and have comprised the backbone of the country's expanding economy. Although larger investment deals are often favored within IFC, it's frequently the smaller, local entrepreneurs who truly value and benefit the most from cooperation with IFC. When our assistance to them is a well-coordinated joint effort between investment and advisory services, they benefit even more. Asnova is a case in point.

Asnova Holding ("Asnova" or "the Company") was established in 1992 by four Ukrainian entrepreneurs with the opening of one small store in Kyiv selling basic goods such as shampoo and soap. The business grew, and in the late 1990s one of its companies became the exclusive distributor of Procter & Gamble's goods for Kyiv and Central Ukraine. Today, Asnova has evolved into a leader in the Ukrainian wholesale and retail market of fast-moving consumer goods, employing more than 4,600 people.

Asnova was first contacted by IFC back in 2002 on the recommendation of Procter & Gamble, which referred to Asnova as a reliable and trusted partner. In the years that followed, Asnova became not only a long-term investment partner of IFC but also a success story for its advisory services arm.

LESSONS LEARNED

1) Take a comprehensive approach to client management. Form a joint investment-advisory

services team at the early stages, and let advisory staff participate in initial meetings and take part in the appraisal process.

Although the company had demonstrated strong management skills and its ability to grow a successful business from scratch, during the appraisal IFC identified some areas in need of improvement. Asnova had no audited financials; the legal corporate structure was complicated, with more than 50 subsidiaries; and, while the company had taken an initial step by forming a closed joint-stock company, its corporate governance was in its infancy.

Coinciding with the appraisal process, the Ukraine Corporate Development Project, an advisory services project focused on improving corporate governance in the private sector, began actively rolling out its pilot company program, offering corporate governance assessments, followed by CG improvement plans and training and support in implementing recommended changes. The investment team thought that Asnova could benefit from this type of assistance.

The UCDP advisory staff was brought in early on to work closely with and complement the investment team—participating in numerous client meetings, conference calls, and internal investment team discussions. The advisory services team was asked to conduct a preliminary assessment of Asnova's corporate governance and inform the investment team of its findings. Advisory services also contributed by identifying potential risks for the investment project and offered mitigating solutions. Many of these findings were incorporated into the decision book of the investment project.

The investment team supported the advisory services team's findings by reinforcing the message to the Company that the need for CG improvements overall was much higher than what would be required as a precondition for a loan but that, in the end, it would help bring Asnova closer to international best practices. It was left up to Asnova's owners to decide whether or not (and when) to apply for the UCDP pilot program.

2) Advisory services and investment don't always happen simultaneously.

The advisory services team should be patient. You want the company to choose a time that's right for them and ensure that they are fully committed. Using investment as a motive (or stick) for improving things like corporate governance can lead to a "window dressing" exercise that, in the end, can increase the risk for the investment, not mitigate it.

Although the company's shareholders were interested in learning about CG best practices, they were at first somewhat skeptical about whether CG could really add value. At the time, Asnova was run like a small family business, with decisions made informally and issues usually discussed until everyone agreed. The advisory services team expressed concern that the company had inefficient decision-making procedures and that, due to a lack of formalized corporate governance structures, there was an increased risk of conflicts among the owners. This was communicated to Asnova's shareholders, but they believed that formalizing procedures and a clear division of powers could unsettle their friendly relationships.

As a result, the investment process continued while the advisory services team took a back seat. The investment team included some key requirements on corporate governance as a condition to financing the deal but didn't push on the rest. When IFC decided to invest, the advisory services team was somewhat disappointed, worrying that its leverage to encourage broader CG changes at the company was lost. However, having a strong working relationship with IFC and having sown the seeds of corporate governance at the outset

had its effect on the company. Having gone through a rigorous due-diligence process and evaluation of a range of strategic and management issues, the owners soon realized the weaknesses of their systems and the value that improved corporate governance could bring. After an eight-month break, Asnova's management re-engaged with IFC's UCDP team to become a corporate governance pilot company.

The advisory services team designed a CG improvement program with more than 30 different activities, including various workshops, special training for the company secretary, a revision of the board of directors' role, succession planning, and formalization of company procedures. From a CG-reluctant group of friends, the company owners became leaders and promoters of good corporate governance.

3) Investment and advisory staff need to work together as one IFC team. To make this happen, there must be frequent sharing of information between the investment and advisory arms. Both teams should know about the client's achievements and problems.

Throughout the process, the investment team and the advisory services team regularly informed one another of developments. The investment team often invited the advisory services staff to client meetings and internal discussions, and the advisory services team kept the investment staff up to date on any interactions with the company. Once the CG pilot program was under way, the advisory services staff summarized Asnova's achievements and also conveyed problematic areas in need of improvement, which were incorporated into a future action plan. At the same time, investment staff shared information on the company's performance and future ambitions. There were no formal procedures: each team member shared ideas and what he/she knew. Usually this happened either via e-mail or a simple chat between advisory services and investment staff.

This sharing of information helped the advisory services staff increase the quality of workshops by



Asnova CEO Urfan Guliev speaks at IPO Forum.

making them more relevant to the company's current situation and also by taking into account its medium- and long-term plans. This also enabled the investment team to keep abreast of what was happening in the company outside of the investment deal. Working together with Asnova's management and shareholders, IFC investment and advisory services staff were all part of a team that developed an attractive range of services to add value to the company's business.

4) Be a trusted partner of the client. Keep in touch with the client on a regular basis, including after the deal is signed and advisory services are completed, and broaden the relationship to involve the client in other activities.

Over the life of the relationship, IFC's investment and advisory services teams have built up a significant amount of trust with the company. The initial project, which was small by IFC standards, was the first step in building a strong relationship. It was used by both parties to get to know one another and has led to both sides wanting to deepen and expand the relationship.

It is important to keep in close touch with the client, even on an informal basis, and worthwhile to include the client in events that can benefit both parties—as a guest speaker at conferences and as a participant in training events organized by IFC. For example, Urfan Guliev, Asnova's chief executive officer, was

invited to speak about his company's experiences at an IPO Forum at which dozens of local companies were present. His presentation was cited as among the most interesting and informative. It put Asnova in the spotlight, and for IFC it provided a strong demonstration effect of how improving corporate governance and working with IFC on the financing side can lead to success. At the introduction of IFC, Guliev also recently made a presentation at a well-attended Ukrainian CFO conference at which he spoke highly about his relationship and experience in working with IFC.

Here our SmartLesson ends, but the relationship continues ...

In FY05, IFC provided a \$6 million A loan and a \$2 million C loan to Asnova for the expansion and modernization of its distribution, warehouse, and logistics business. IFC is currently working on a second financing for the company of up to \$42 million, including a syndication and possible equity investment, to further expand the company's operations. In spite of the UCDP's official closure, the company keeps in contact with IFC's advisory services consultants—seeking advice, sharing information, or simply discussing general CG trends in the country.

This is what good client relationship management is all about.

ABOUT THE AUTHORS

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