

PROPOSAL FOR FINANCING AND TECHNICAL COOPERATION FOR:

THE RUBEN REYNA PUPO SAVINGS AND LOAN COOPERATIVE OF THE NATIONAL UNION
OF SMALL AND MEDIUM ENTERPRISES, R.L. (CACPYMER) AND
THE FOUNDATION FOR SUSTAINABLE DEVELOPMENT (FUNDES)

EXECUTIVE SUMMARY

INTERMEDIARY
ORGANIZATIONS:

The proposed intermediary organizations (IOs) are the Ruben Reyna Pupo Savings and Loan Cooperative of the National Union of Small and Medium Enterprises, R.L. (CACPYMER) and the Foundation for Sustainable Development (FUNDES), both private, non-profit organizations created with the objective of promoting micro and small business development in Panama.

AMOUNT AND
SOURCE:

IDB:	<u>Financing:</u>	<u>Technical</u>	<u>Total:</u>
		<u>Cooperation:</u>	
<u>CACPYMER:</u>	US\$250,000	US\$130,000	US\$380,000
<u>FUNDES:</u>	US\$500,000	US\$100,000	US\$600,000
Total:	US\$750,000	US\$230,000	US\$980,000

Source of CACPYMER: Japan Special Fund
Funding: FUNDES: Social Progress Trust Fund

TERMS AND
CONDITIONS:

CACPYMER: Disbursement period: 3 years; to be extended on a non-reimbursable basis

FUNDES: Disbursement period: 3 years; Amortization period: 40 years; Grace period: 10 years; Fee: 1%

OBJECTIVES:

The objectives of the proposed program are to: (i) improve and expand the capacity of the participating IOs to grant credits and provide training and technical assistance services to microentrepreneurs and small business owners, in order to enhance their income and thereby improve the socioeconomic situation of their families; (ii) create and strengthen employment in both urban and rural areas of the country; (iii) contribute to the incorporation of environmental conservation practices; and (iv) strengthen the IOs institutionally in their lending activities so that they can achieve financial and operational self-sufficiency in the future.

DESCRIPTION:

The proposed program would consist of the following components: (i) Credit: resources would be used to expand the revolving credit funds of the IOs and would be used for on-lending to micro and small entrepreneurs to finance the cost of working capital and fixed assets to be used in light manufacturing, commerce, and service activities; and (ii) Non-

reimbursable technical cooperation: resources would be used to provide institutional strengthening to the IOs, and to assist the project beneficiaries through training and technical assistance activities.

**ENVIRONMENTAL
CLASSIFICATION:**

The Environmental Management Committee, at its meeting of February 8, 1995, classified these as Category II operations.

BENEFICIARIES:

The beneficiaries of the program would be micro and small entrepreneurs who currently lack access to conventional credit sources and have an annual per capita income below the level calculated by the Bank in defining low-income groups in Panama. CACPYMER's beneficiaries would be located in the Panama City and Colon area, while FUNDES would direct its attention to those clients primarily in the cities of David, Santiago, Las Tablas, Chitre, Penonome, and Aguadulce.

BENEFITS:

The primary benefits of the program are the following: (i) additional credit resources will allow each intermediary organization to expand its current lending operations, thereby assisting in achieving economies of scale in their operations; and (ii) the technical cooperation operations designed for each intermediary will enhance operational and financial efficiency in the execution of their programs, and will allow them to play a more proactive role in the future in formulating and implementing programs similar to the one proposed herein.

RISKS:

The main risks of the operation are: (i) the failure of the Panamanian Government to effectively implement its adjustment program which is aimed at opening the economy and improving the climate for private sector development; (ii) a possible reduction in the estimated demand for credit on the part of the entrepreneurs that will have to pay real interest rates on loans granted under the program; and (iii) the chance that institutional weaknesses of the IOs are not corrected as a result of the technical cooperation designed for this purpose.

**THE BANK'S
COUNTRY
STRATEGY:**

The Bank's Country Programming Paper (CPP) highlights the following priorities in Panama during the 1994-1996 period: (i) to support favorable macroeconomic, fiscal and sectoral reform; (ii) to improve the efficiency of public expenditures and support modernization of the state; (iii) to support sustainable development of the Interoceanic Region; (iv) to develop human resources and reduce poverty through social sector initiatives; and (v) to

rehabilitate and expand the basic infrastructure of the country.

**SPECIAL
CONDITIONS:**

As a special condition, it is recommended that an advance of funds up to 20% of both the financing and technical cooperation to each IO be disbursed at their request (see paragraph 3.11).

I. BACKGROUND

A. The requests

- 1.1 Discussions with the Ruben Reyna Pupo Savings and Loan Cooperative of the National Union of Small and Medium Enterprises, R.L. (CACPYMER) and the Foundation for Sustainable Development (FUNDES) began in 1992, and later that year the intermediary organizations (IOs) presented official proposals to the bank to expand their credit, technical assistance, and training programs under the Small Projects Program. Subsequently, consultants were hired by the Bank in October 1994 to complete the analysis of the projects.

B. Declaration of no objection

- 1.2 In June 1993, the Government of Panama, through the Ministry of Planning and Economic Policy, notified the Bank of its no objection regarding the proposed financing to CACPYMER. In August 1994, the Bank received similar notification for the financing to FUNDES.

C. The informal sector in Panama

1. Urban enterprises

- 1.3 The term microenterprise in Panama has generally been defined as one with fewer than 5 employees, fixed assets of less than US\$100,000, and annual sales of less than US\$100,000; small businesses have between 5 and 10 employees. The Government excludes those working alone from this definition. While no comprehensive studies of the informal sector in Panama have been undertaken, recent projections made by the International Labour Organization (ILO), estimates developed by Development Alternatives, Inc. in 1994 and household surveys indicate that there are approximately 6,100 to 12,000 microenterprises and around 4,800 small businesses operating in the country. In addition, there are as many as 87,000 individuals in the "self-employed" category, many of whom may be considered microenterprises if one expands the Government's definition of the term.
- 1.4 More than one-half (56%) of micro and small-scale enterprises are involved in commerce, while slightly more than one-quarter (27%) are involved in industry; the balance (17%) is involved in services. Approximately 56% of the microenterprises and 66% of the small-scale enterprises are located in the metropolitan Panama City area, where nearly 50% of the total population of the country is concentrated, and where 1 in every 5 persons is unemployed in the labor market.

2. Rural enterprises

- 1.5 The estimated number of microenterprises and small-scale enterprises located in rural areas has decreased in recent years

due to the flow of migration mainly away from rural areas such as Los Santos, Herrera, Veraguas, Cocle, and Chiriqui to the urban areas near Panama City. These rural enterprises are generally involved in activities related to agro-industry, agri-business, and commerce. While migration has simultaneously increased the country's level of unemployment and the number of workers who are independently employed, there is some evidence that this trend will reverse itself in the next few years as public sector workers who were part of the Government's voluntary retirement program return to their native provinces in search of lower costs of living and opportunities to establish small businesses. Since the education level of public sector workers in urban areas is generally higher than those in rural areas, the types of new businesses that will be established will likely not conflict with those that already exist or that have the potential for development.

3. Financial and non-financial bottlenecks for microentrepreneurs

- 1.6 The most important financial bottleneck for microentrepreneurs is the limited access to the formal financial system in Panama, which is oriented mainly to international trade. Among the types of financing available to the business community, one private bank (MultiCredit Bank) has developed a clientele among microenterprises and small-scale businesses, and a few finance companies and savings and loan cooperatives have provided limited financing. With the exception of CACPYMER and FUNDES, most non-governmental organizations (NGOs) are not involved in offering credit to small scale entrepreneurs.
- 1.7 Microentrepreneurs and small-scale business owners also face non-financial bottlenecks, the most important of which is the lack of training in basic business skills such as management, accounting, marketing, taxes, labor contracts, and the ability to negotiate with financial intermediary organizations to secure credit and non-financial services. And while microenterprises enjoy generous tax law exemptions, the red tape involved in legalizing a business and requirements for notary fees present significant administrative obstacles to their development.

D. The role of women in Panama

- 1.8 Nearly one-half of Panamanians involved in the urban workforce are women, one of the highest contributions in Latin America. In 1993, the overall unemployment rate in Panama was 12.5%, however, unemployment among women was about 20% of the total economically active population in the country, while that for young people of both sexes was about 30%. Poverty unequally affects Panamanian households; 47% of those headed by women are classified as living at the poverty level (defined as US\$265 for a family of five persons) while 33% of those headed by men are classified likewise.
- 1.9 Panama appears to have no particular regulations that limit women's access to financial services. Collateral requirements and

relatively high loan amounts are perhaps the major impediments to increased credit access to women. Despite such constraints, between 30 and 40 percent of the loans granted by Panama's primary microenterprise programs have been to women. Most of those loans made to women were related to the commerce sector, where loan amounts are generally smaller than in other sectors such as industry and services.

E. The strategy of the Government of Panama

- 1.10 The newly-elected Government has as its general objective the creation of an economic system that has the capacity to generate productive employment that will serve as the mechanism to alleviate the social problems caused by poverty. To achieve this goal, it will implement both private and public sector programs. The private sector program aims to stimulate competition under free market conditions, promote external trade, increase production, and develop goods and services that are economically competitive. The public sector program has as its goals the normalization of the country's external debt, the improvement in regulation and efficiency in private sector development, and increased investment and exports.
- 1.11 Several government agencies aimed at supporting microentrepreneurs will also be involved in the Government's plan to alleviate poverty and increase employment. These include the General Directorate of Small Enterprises of the Ministry of Commerce and Industry, which offers training programs at a low cost and technical assistance in the preparation of projects for no fees; the National Council for the Development of Micro and Small Enterprises, whose activities focus on strengthening the micro and small enterprise sector; and the Ministry of Planning and Economic Policy, which is charged with registering NGOs and identifying institutional strengthening and technical assistance requirements so that these institutions can better serve micro and small enterprises.

F. The strategy of the Bank in Panama

- 1.12 The Bank's Country Programming Paper (CPP) highlights the following priorities in Panama during the 1994-1996 period: (i) to support favorable macroeconomic, fiscal and sectoral reform; (ii) to improve the efficiency of public expenditures and support modernization of the state; (iii) to support sustainable development of the Interoceanic Region; (iv) to develop human resources and reduce poverty through social sector initiatives; and (v) to rehabilitate and expand the basic infrastructure of the country. Important actions that the Bank will take to achieve those priorities and impact directly on microenterprises and small-scale enterprises include institutional strengthening and decentralization, employment generation and poverty alleviation through human resource development, and an expansion of financial and non-financial services for Panama's poor. The operations proposed in this document are compatible with the Bank's strategy

in the sector, since their implementation would support the most disadvantaged groups by improving their income and generating new sources of employment.

II. INTERMEDIARY ORGANIZATIONS

A. Ruben Reyna Pupo Savings and Loan Cooperative of the National Union of Small and Medium Enterprises, R.L. (CACPYMER)

1. Origin and objectives

- 2.1 CACPYMER was founded on September 10, 1984 in Panama City as a private non-profit savings and loan institution by a group of Panamanian professionals belonging to the National Union of Small and Medium Enterprises (UNPYME). The primary objective of CACPYMER is to promote the independent ownership and management of businesses, while contributing to the economic and social development of the country by establishing and consolidating micro, small, and medium-size enterprises through programs of credit, technical assistance, general management, and technical and administrative training.

2. Organizational and operative structure

- 2.2 CACPYMER is structured at three distinct levels: the political level, comprised of the General Assembly; the supervisory level, made up of the Board of Directors, the Board of Supervisors, the Credit Committee, and the Education Committee; and the operational level, comprised of the General Manager and supporting units. The General Assembly is the supreme body of the cooperative and is composed of all registered members in good standing. At present, CACPYMER boasts a membership of 480 business owners.
- 2.3 At the supervisory level, the Board of Directors is responsible for administering and directing the Cooperative in implementing the plans adopted by the General Assembly, and is composed of five principal members (the President, Vice President, the Secretary, Treasurer and Vocal), three alternates, and one member of the cooperative. The Board of Directors meets at least monthly to propose modifications to the by-laws, secure funds for loans, maintain regular contact with Instituto Panameño Autónomo Cooperativo (IPACOO) and other national and international cooperatives, regulate all internal procedures of the cooperative, review the financial position of the cooperative, and appoint and supervise the General Manager.
- 2.4 The Supervisory Board, also elected by the General Assembly, is composed of three members. During its monthly meetings, the Board supervises the economic and accounting activities and ensures that the membership at large complies with the regulations, by-laws and decisions adopted by the General Assembly. It is also authorized

to oversee the loans and loan extensions approved by the Credit Committee and to ensure that those loans are secured.

- 2.5 The Credit Committee is composed of three members who are elected at the annual meeting of the General Assembly for a period of three years. The committee meets weekly to approve or reject loan applications in accordance with rules established by the Board of Directors, and to ensure that loans are used for their intended purposes.
- 2.6 The Education Committee, comprised of three or more members elected by the Board of Directors, meets annually to inform new members on the cooperative's activities, develop and promote educational and training programs, and prepare bulletins for the membership. Four ad-hoc committees (Admission Committee, Loan Default Committee, New Services Committee, and New Building Committee) are also presently operative and are comprised of between three and five persons who do not occupy directive posts in the cooperative.
- 2.7 At the operational level, the General Manager is responsible for the day-to-day operations of the cooperative, including the preparation of financial reports. To carry out his duties, the General Manager is supported by eight persons in the Collections Department, the Operations Department, and the Project Department. The Collections Department, comprised of three persons, is responsible for the analysis of the loan portfolio, legal proceedings initiated in the case of uncollectible loans, and loan follow-up. The Operations Department, comprised of three persons, is charged with members' deposits, accounting, and disbursements. Lastly, the duties of the Project Department, comprised of two persons, relate to analysis and evaluation of credit requests, administrative and financial assistance, and education and training.
- 2.8 CACPYMER's operational personnel totals 12 full-time employees, 4 of whom are at the supervisory level, 5 of whom are at the technical level, and 3 of whom are at the support level. In June 1993, 4 new positions were created at the supervisory level that expanded CACPYMER's organizational structure to include 3 new management offices, as follows: 2 in the area of credit payments, 1 in the area of projects, and 1 in the area of operations. Women occupy two-thirds of all posts and one-half of the managerial posts in the cooperative.

3. Activities

- 2.9 Since its creation, CACPYMER has been engaged in promoting credit and training services throughout the business community by sponsoring conferences and conducting promotional activities to earn funds and increase membership. Its credit activities were initiated in the heavily populated San Miguelito district of Panama City in 1987 with resources from a 25-month Small Project financing (SP/SF-87-03-PN) that consisted of a US\$250,000 loan and a

technical assistance program for US\$75,000. In 1988, CACPYMER decided to expand its services to other districts throughout the city, but later that year the national financial crisis caused the cooperative's funds and those of other Bank programs to be frozen, severely limiting the availability of credit to the program beneficiaries. One year later, several microenterprises that received funding through the small project were affected by acts of vandalism that occurred following the US military invasion of Panama, and subsequently were unable to repay their loans. This situation prompted the cooperative to reschedule and reprogram many of the credits granted with Bank resources, and after a careful review of the entire loan portfolio and the implementation of a series of corrective measures, by the end of 1992 the cooperative reduced its arrears rate from 21% to 4%.

- 2.10 With the original resources of the small project approved in 1987, CACPYMER extended 100 credits to microentrepreneurs engaged in industrial activities (76%) and service activities (24%), and created 180 new jobs which indirectly benefitted 443 persons. An additional 65 credits totaling US\$179,780 were extended with reflows from the original funds, and an additional 98 jobs were created. In all, over 1,800 people from 704 families benefitted from the project, including those who had received credit and those who were employed as a result of the expansion of the microenterprises.
- 2.11 Following the program financed by the Bank, CACPYMER secured US\$140,000 from the Inter-American Foundation (IAF) and US\$245,000 from the Ministry of Commerce and Industry (MICI) to expand its services to the province of Colon and the remaining part of the province of Panama. These resources have mainly benefitted small entrepreneurs, while loans made with IDB funds were specifically earmarked for lower income microentrepreneurs.
- 2.12 Nearly all loans made in both 1992 and 1993 were disbursed to beneficiaries located in urban areas, although the number of loans made in rural areas increased slightly between 1992 and 1993 from 2 to 5 groups. Likewise, nearly all loans were made to individuals having legally-established businesses, although as in the case of loans made in rural areas, those made to groups of clients increased slightly between 1992 and 1993. In terms of the total value of loans authorized in both 1992 and 1993, about 68% were destined to finance fixed assets; the balance financed working capital. In 1992-1993, 35% of CACPYMER's total loan portfolio was allocated to light manufacturing and construction, 36% was destined to wholesale and retail commerce, and 29% was allocated to services and other business activities. CACPYMER estimates that one-half of its clients return for new financing, which can be authorized when 75% of a loan made for working capital has been paid, and when 60% of a loan made for fixed assets has been paid.

- 2.13 The evaluation of a loan requires 5 hours of work with complete information; without complete information, the credit analyst must spend 3 extra hours visiting the potential client, thereby increasing the total time required to evaluate the loan to 8 hours. In 1993 each analyst dealt with an average of 125 clients. In addition to the loans already in process, the 2 credit analysts currently employed by CACPYMER dealt with between 70-80 new clients a year. In 1995, CACPYMER plans to hire an additional project analyst, one credit analyst and an administrative assistant to support the project manager. With the approval of the proposed program, CACPYMER expects to disburse 100 new loans valued at about US\$300,000, which will enable each credit analyst to handle about 100 clients, a number that the cooperative considers ideal.
- 2.14 CACPYMER's client profile reflects low-income entrepreneurs whose income typically does not exceed US\$1,000 a year, lack previous business experience and access to financial markets. Many have previously been employed by public enterprises in the past. Business owners are not required to become members of the cooperative to be eligible for a loan. They are, however, subject to an extensive screening process that includes the development of a business plan. The type of guarantees that CACPYMER requires before authorizing a loan depends on the amount, and usually includes an underwriter, mortgage or equipment guarantee. Loans made for US\$1,000 or less usually require an underwriter as a guarantee, while those for US\$5,000-US\$10,000 require property or equipment as a guarantee. CACPYMER does not require forced savings on the part of its clients, although it does require them to pay US\$10 a month that is considered as equity, or a form of capitalization of funds. Moreover, if a client has no previous business experience or knowledge of business operations, he is required to take training courses offered by the cooperative.
- 2.15 CACPYMER's training courses are offered in modules of 48 hours, broken down in terms of subjects and hours per subject as follows: (i) business administration, 9 hours; (ii) accounting, 12 hours; (iii) marketing and sales, 9 hours; (iv) labor topics, 9 hours; and (v) tax and social security topics, 9 hours. In 1993 a survey was administered to all members that revealed the need for technical assistance in the form of business training, and that this assistance be more participative and more dynamic than the traditional types of business training offered in the past. CACPYMER has plans to refocus on a different type of technical assistance and to establish a business education and training center that will house larger offices to promote the marketing of members' goods and services.
- 2.16 CACPYMER maintains a system to monitor daily inquiries from persons who solicit information about loans and training. In 1992, 536 persons solicited information, compared with 386 in 1994. Despite the decrease in number of persons approaching the cooperative for information, the total amount of funds requested between 1992 and 1994 remained about the same at US\$2,298,580 in 1992 and

US\$2,374,372 in 1994. Of the requests made to the cooperative for financing, 12% were approved in 1992, compared with 23% in 1993 and 11% in 1994.

4. Financial situation

- 2.17 An analysis of CACPYMER's financial position has been based on a review of its audited financial statements as of December 31, 1991, 1992, and 1993 (see Annex II-1).
- 2.18 Between 1991 and 1993 the total value of CACPYMER's assets increased from US\$844,583 to US\$1,167,922, due primarily to the expansion of its loan portfolio and increases in fixed assets and other assets such as pre-paid expenses. The total value of CACPYMER's assets are expected to increase considerably in 1995 with the construction of a new building on property that was purchased in 1993.
- 2.19 CACPYMER's liabilities increased from US\$775,039 to US\$1,043,756 during the period, which was attributed to a 29% increase in loans payable, and a doubling of accounts payable and savings deposits of the cooperative's members. Loans payable included: (i) US\$59,062 in short-term loans payable to MICI and to the Banco Confederado de América Latina (COLABANCO); (ii) US\$405,625 in long-term loans payable to the Bank and MICI; and (iii) US\$447,898 in donations. Donations are regulated under Law 38 that dictates many of the operations of Panamanian cooperatives, and are recorded by CACPYMER as a liability in a special reserve fund. They would become payable in the case of bankruptcy, first to the cooperative's creditors and second to IPACOOB. Owner's equity or members' shares increased 79% from US\$69,544 in 1991 to US\$124,166 in 1993.
- 2.20 The principal source of CACPYMER's total income in 1993 originated from lending operations, including interest, commissions and fees. Income from other sources such as investments and training fees declined in 1993, indicating the need for CACPYMER to review its current fee structure for courses provided to its members in order to cover related costs.
- 2.21 Total expenses rose by 61% from 1991 to 1993 and were mostly attributed to an increase in personnel and administrative expenses largely due to the hiring of new employees to support the expansion of CACPYMER's loan portfolio during the period.
- 2.22 CACPYMER reported a net loss of US\$5,679 in 1993, which was attributed to an adjustment of US\$17,590 that represented a clearing of books between CACPYMER and UNPYME of accounts payable and accounts receivable that were outstanding between the two organizations since 1984. Without this adjustment, CACPYMER would have recorded a net income of US\$11,911, representing an increase of 37% from its 1991 gain.

- 2.23 In summary, the cost-structure analysis of the cooperative's financial statements indicates that income represented 13% of performing assets in both 1993 and 1991, and that CACPYMER was able to cover all its costs with income derived from lending operations. Nevertheless, as the loan portfolio continues to increase, management will need to control its personnel and administrative expenses and generate additional revenues by considering increases in its training fees and interest rates to its clients in order to achieve financial self-sustainability in the future.

5. Institutional evaluation

- 2.24 The institutional image that CACPYMER projects throughout the local and international community is one of collaboration and seriousness. At the national level, CACPYMER maintains working relationships with other NGOs also involved in the field of credit, such as FUNDES and the Juan XXIII Cooperative. At an international level, CACPYMER collaborates with United States Agency for International Development (USAID), the United Nations Development Program (UNDP), the IAF, and the Bank.
- 2.25 The flow of information throughout CACPYMER's organization appears to be well structured, efficient and subject to strict internal controls. Computerized reports are generated using customized programs and standard software. The analysis carried out during project review revealed a need for CACPYMER to provide training in project management, evaluation, and monitoring for its employees to increase productivity. In addition, the creation and implementation of a computerized program to follow up on projects could impact positively on productivity. In order to address these institutional needs, part of the technical cooperation parallel to the credit program will be designated for training in the design and implementation of an internship program in project management, evaluation, and monitoring and of a computerized loan follow-up program.
- 2.26 As CACPYMER expands its operations in 1995 and relocates to a larger office in August, the cooperative plans to embark on an internal restructuring to improve the efficiency and productivity of its operations. The impact and results of this restructuring will be reviewed by a credit and financial systems consultant to be hired with funds from the proposed technical cooperation program. It is also recommended that the cooperative's 3-year strategic plan, which expires in 1996, be reviewed and revised accordingly at that time.
- 2.27 In summary, CACPYMER's strengths include its market niche in micro and small enterprise lending, which is evidenced by the large demand in credit from these types of businesses and the small supply of credit provided by similar institutions. The cooperative is challenged to meet this demand as it works to increase its personnel, improve its institutional weaknesses, and increase the flow of financial resources to meet the demands of its clients.

B. Foundation for Sustainable Development (FUNDES)

1. Origin and objectives

- 2.28 FUNDES-Panama was established in February 1984 and incorporated five months later under the name Foundation for Economic and Social Development, with the purpose of promoting micro and small enterprise development through direct credit, loan guarantee, and training programs. FUNDES-Panama is an affiliate of FUNDES in Switzerland, which has supported the development of a network of non-profit NGOs in 10 Latin American countries. In August 1992, FUNDES changed its name to Foundation for Sustainable Development to better reflect its present-day philosophy that focuses on long-term sustainable development. FUNDES-Panama is headquartered in Panama City with regional offices in the cities of David, Santiago, Las Tablas, Chitre, Penonome, Aguadulce, La Chorrera and Colon.

2. Organizational and operative structure

- 2.29 FUNDES is structured at the political, advisory, managerial, and technical and operating levels. The political level is organized by the Board of Trustees, the Board of Directors, and the Executive Committee. The Board of Trustees is composed of six persons who ensure that funding levels are adequate to maintain its activities, designate members of the Board of Directors and the External Auditor, approve financial statements, the annual budget, and the by-laws, and liquidate the foundation in the event necessary. The Board of Directors is currently composed of 18 members (President, Vice President, Secretary, Treasurer and 14 directors) who are elected annually to manage all assets of the foundation. Lastly, the Executive Committee of six persons is appointed by the Board of Directors, and is responsible for collaborating with the Board of Directors in the execution of its decisions.
- 2.30 The advisory level is made up of the External Auditor and six working committees (Promotion, Credit Guarantees, Direct Credit to Microenterprises, International Relations, Institutional Development, and Small Enterprises Support Services), which report directly to the Executive Committee.
- 2.31 The managerial level is comprised of the Executive and Deputy Directors, who are appointed by the Board of Directors with the approval of FUNDES-Switzerland. The directors report to the Executive Committee and are charged with supervising the daily operations of the foundation and participating in strategic planning exercises. A newly-created advisory level supports the Executive and Deputy Directors, and is comprised of the Human Resources and Inter-Institutional Relations offices.
- 2.32 The technical and operating level is organized into five areas: (i) the guarantee area, charged with guarantee analysis, bank transactions, follow-up, and portfolio management; (ii) the direct credit area, responsible for credit analysis, loan documentation

and disbursement, follow-up, payments, and portfolio control; (iii) the business support area, charged with training, advisory services, and environmental awareness; (iv) the internal service area, responsible for the coordination of regional offices, promotion, sales, maintenance, and computer support; and (v) the finance area, charged with activities relating to accounting, budget formulation, treasury, internal auditing, reports, and purchases.

- 2.33 At the present time, FUNDES employs approximately 70 persons, more than half of whom work at the technical and operating level. In 1993, the average number of total personnel assigned to the direct credit program was 37, including 10 credit analysts, 15 follow-up technicians and 12 administrative workers. FUNDES' indirect credit or guarantee program is staffed by 4 persons, 2 credit analysts, an administrative assistant and a follow-up technician.

3. Activities

- 2.34 FUNDES has concentrated its efforts on promoting the operations of low-income entrepreneurs engaged in light manufacturing and service activities located in the metropolitan and southwestern urban areas of the country by implementing direct credit programs, indirect credit programs through bank guarantees, and offering training services. Funds for the direct credit and institutional programs are funded by international donors and local contributors, while the credit guarantee schemes are funded equally by Swiss and local funding.
- 2.35 The foundation initiated its credit services in 1985 with a guarantee program offering financing between US\$6,000 and US\$50,000 to qualifying enterprises while guaranteeing 70-75% of the financing to its seven partner banks.
- 2.36 In 1986, FUNDES established its Microindustry Program with a small project financing of US\$500,000 (SP/SF-86-04-PN) that aimed to provide loans to qualifying start-up and existing businesses. In addition to the financing, FUNDES received a non-reimbursable technical cooperation for an amount of US\$100,000 for institutional strengthening, which resulted in the complete computerization of its accounting department, and the organization of its personnel, equipment, and procedures to carry out monitoring and follow-up programs for loans at both the technical and socio-economic levels. Program resources also financed 67 training courses for 1,207 program beneficiaries in the areas of credit and accounting, business administration, and marketing.
- 2.37 In 1989 FUNDES also launched its Program for the Restoration of Small Businesses with a donation of US\$5 million from USAID to rebuild 252 small businesses that were destroyed during civil unrest. The beneficiaries of this program received an average of \$20,000 to re-establish their businesses.

- 2.38 In the direct lending program, 866 loans totalling US\$3,515,000 were disbursed in 1993, an increase of 64% from the previous year. Eighty-six percent of the loans were destined to first-time borrowers. Loans made from Bank funds averaged US\$2,245 in 1993, had guarantees of tangible goods and personal finances, and maximum loan repayment terms of 36 months. At the end of 1993, FUNDES' arrears rate for direct loans was 6%. After a careful review of the portfolio, statistics revealed that loans in the transport sector did not perform well so they were discontinued. Loans to clients with established businesses are also being given priority, since newer businesses have had more defaults. FUNDES has also hired an ex-banker to act as regional credit manager to more closely monitor the status of the credit portfolio in the interior of the country. Finally, FUNDES has established an incentive program for its credit officers which rewards them with a commission for maintaining a portfolio in good standing; in the case of loans which remain in default, the credit officer does not receive the commission.
- 2.39 The interest rate and commission set by FUNDES for the direct credit program are calculated to allow full cost coverage. In 1993, the effective interest rate was 22.2% and the nominal interest rate was 13.5%. When taking into account the inflation rate, the real effective interest rate was 17.1% in 1993, which is adjusted periodically to reflect current market conditions.
- 2.40 In terms of productivity at the individual level in the direct credit program, in 1993 an average of 33 days were required per employee to process one loan, from the time of the first formal interview to disbursement of funds. Of the total number of new loans disbursed in 1993, each credit officer was responsible for 87 loans for a total of US\$351,500, compared with 84 loans for a total of US\$268,375 in 1992. The average number of loans made a month during 1992-1993 for credit officers was 7. In addition to managing the caseload of new loans, in 1993 credit officers handled an average of 13 outstanding loans a month.
- 2.41 Amounts granted for loans under the guarantee program have had a ceiling of US\$49,000 and averaged US\$24,573. In 1993, there were a total of 93 loans disbursed and 190 loans outstanding; each credit analyst was responsible for about 4 new loans and 8 outstanding loans a month. For applicants to the guarantee program, FUNDES requires a guarantee of between 70-75% of the requested loan amount, and clients must undertake an internal evaluation. FUNDES then recommends approval of the loan request to a commercial bank, which requires the potential client to undergo further analysis according to its own methodology. This program is costly to all parties involved, loan applications of the banks are not standardized, and productivity of the credit officers is much lower than in the direct credit program. In 1993, between 105 and 121 days were required to process a loan guarantee, which included the time from the initial interview until disbursement by a partner bank.

- 2.42 Of FUNDES' total loan portfolio in 1992-1993, 65% was allocated to the service industry, of which 35% was destined to wholesale and retail commerce and 30% was destined to other services; 35% of the total loan portfolio was allocated to light manufacturing activities during those two years. In 1992-1993 two-thirds of all loans were used to purchase fixed assets such as equipment; the balance was used to finance working capital. During 1992-1993 FUNDES made all its loans to promote businesses in the urban, rather than rural areas of the country, and provided credit only to individuals who established legal businesses and who were directly responsible for the operations of the business for which the loan is being made, as stated in the foundation's lending policy. FUNDES makes no group loans.
- 2.43 Given that the principal target group of FUNDES' financing is comprised of independent, low-income workers who lack formal training in business skills, FUNDES requires that its direct credit clients undergo a 45-hour training program as part of the financing and loan follow-up process. The objective of the training program is to enable an entrepreneur to identify and resolve administrative and marketing problems and to design and implement strategies to solve those problems. The course is offered in two parts at a cost of US\$50 per client, and is structured at the first level to build basic business skills and at the second level to involve clients in specialized seminars.
- 2.44 FUNDES estimates that the revenue earned from the training program covers more than 150% of its costs. However, much of this profit is used in the loan recuperation and follow-up phase of the loan process, where clients are trained outside the formal classroom to make prompt and accurate loan payments. FUNDES estimates that each client spends about 38 hours a year on the analysis, disbursement and follow-up for each loan in addition to the time spent in the training program. The cost to FUNDES of managing direct credit loans in amounts less than US\$500 is high, which in part is due to the high level of training required for the client requesting this amount of a loan, and in other part is due to long time it takes to feel the economic effect of making a loan of less than US\$500. FUNDES is therefore considering making group loans to individuals requesting loans in the amount of US\$500 or less.

4. Financial situation

- 2.45 An analysis of FUNDES' financial position has been based on a review of its audited financial statements as of December 31, 1991, 1992, and 1993 (see Annex II-2).
- 2.46 Between 1991 and 1993 the total value of FUNDES' assets increased 24%, rising from US\$6,808,636 to US\$8,458,696. This increase was primarily attributed to an expansion in the loan portfolio in 1993, which comprised 72% of total assets. The fixed assets account

increased significantly during the 1991-1993 period, due mainly to the purchase of the FUNDES building in Panama City in 1992 and to the expansion of the loan portfolio.

- 2.47 FUNDES' liabilities increased 3.5 times between 1991 and 1993, rising from \$620,136 to US\$2,162,452. This large increase was attributed mainly to a surge in accumulated expenses to be paid for employee benefits, worker lay-offs, and deferred income, as well as to an increase in the loans payable account which grew dramatically in 1993 as a result of the expansion in the loan portfolio. Owner's equity increased slightly during the period under review, reaching US\$6,188,500 in 1991 compared with US\$6,218,512 in 1993.
- 2.48 FUNDES' total revenues increased by 37% between 1991 and 1993, rising from US\$809,707 to US\$1,108,592. The expansion in revenues is attributed mainly to the large increase in the commissions charged on loans made under the guarantee program and fees charged to training program participants. Donations decreased steadily during the period 1991-1993, which reflects FUNDES' growing independence from external sources for revenue. In 1991 donations represented 4.3% of total income compared with 0.1% in 1993.
- 2.49 Total expenses rose by 19% from 1991 to 1993, and were mostly made up of personnel and administrative costs which increased by 62% between 1991 and 1993, due to the opening of the new offices outside of Panama City. Financial costs also increased 7.5 times between 1991 and 1993, due to the expansion of the loan portfolio. As a result of the effective management in income and expenses, FUNDES recorded a net profit of US\$77,732 in 1993 compared with US\$6,012 in 1992 and a loss of US\$54,506 in 1991.
- 2.50 An analysis of the operational cost structure of FUNDES indicates that the NGO is operating efficiently, as the foundation's total operational costs registered 15% of average performing assets in 1993. The evolution of the individual line items of personnel, administration and depreciation indicated an increase to 12% of total performing assets in 1993, which was attributable to the expansion in FUNDES' geographical coverage. In terms of the profile of the cost structure, total operating and administrative costs represented 96% of performing assets; the balance was attributed to financial costs, which increased during the period under review due to the increase in loans and other services provided to program beneficiaries.

5. Institutional evaluation

- 2.51 FUNDES' greatest strength since its inception is that it has been able to maintain an important influence and accompanying prestige in the small business community and among other NGOs in the same field. In part, FUNDES' reputation is attributed to its close links with the Catholic Church in Panama, a representative of which maintains a permanent post on the Board of Trustees, and in other

part, to its successful credit and training operations that have been undertaken throughout the country in the last several years.

- 2.52 The structural changes that have taken place during the foundation's 10 years of operation have occurred mainly at the advisory level, which was substantially expanded in 1991, and at the technical and operating level, which gradually developed over the years both in terms of number of personnel and responsibilities. These changes reflect the broad scope of FUNDES' activities that are carried out throughout the country, and the increase in number and type credit, guarantee, and training services.
- 2.53 The analysis carried out as part of the project review revealed several areas which need to be strengthened in order to assist FUNDES in becoming more financially self-sustainable. One area which needs to be addressed in the future relates to the difficulty in finding qualified technical staff with the necessary experience to manage credit operations. Therefore, there is a critical need to provide the necessary training to existing employees in order to increase their operational and technical expertise.
- 2.54 In addition to retraining personnel with appropriate skills, there is a need to redistribute the tasks involved in processing direct credit loans among the three categories of personnel involved in credit operations in order to achieve better efficiency in these functions. FUNDES is currently studying the possibility of creating a new unit whose function would be solely to handle the administrative tasks of loan follow-up to maximize the per capita monthly use of staff time in both the direct lending and guarantee credit programs.
- 2.55 With the expansion of FUNDES' operations and subsequent increase in personnel, the current centralization of information in the office of the Executive and Deputy Director at headquarters should be decentralized to the regional offices where the daily information is needed most. The Bank's non-reimbursable technical assistance will assist FUNDES in this area by providing funds for the purchase of a computer network system and for the training of personnel in its use in managing the loan portfolios. The other areas of staff productivity and training will also be reviewed in greater detail by consultants to be hired through the technical cooperation operation.

III. THE PROGRAMS

A. Objectives

- 3.1 The objectives of the proposed program are to: (i) improve and expand the capacity of the participating IOs to grant credits and provide training and technical assistance services to microentrepreneurs and small business owners, in order to enhance their income and thereby improve the socioeconomic situation of their families; (ii) create and strengthen employment in both urban and rural areas of the country; (iii) contribute to the incorporation of environmental conservation practices; and (iv) strengthen the IOs institutionally in their lending activities so that they can achieve financial and operational self-sufficiency in the future.

B. Description

1. Ruben Reyna Pupo Savings and Loan Cooperative of the National Union of Small and Medium Enterprises, R.L. (CACPYMER)

a. Credit program (US\$250,000)

- 3.2 The equivalent of US\$250,000 would be used to expand the revolving credit fund established with resources from the Bank's small project financing SP/SF-87-03-PN. Credit resources would be used for on-lending to individual microentrepreneurs at market interest rates to finance the cost of working capital and purchases of fixed assets such as machinery, equipment, and vehicles to be used in light manufacturing, commercial activities and services. It is estimated that approximately 60 loans would be disbursed with an average loan amount of US\$2,500. Special attention would be paid to urban beneficiaries in the cities of Panama and Colon, where credit services for small enterprises are limited. It is estimated that CACPYMER's historical level of total loans extended to women of 40% would be maintained.

b. Non-reimbursable technical cooperation (US\$130,000)

- 3.3 The non-reimbursable technical cooperation component of this project for an amount equivalent to US\$130,000 is aimed at strengthening the role of CACPYMER as an intermediary and providing training services to program participants. It is hoped that in the future CACPYMER will constitute a key element in the strategy of the social and economic promotion of Panama's low-income urban sectors by offering a combination of training, technical assistance and credit to program beneficiaries. The project beneficiaries would be provided training for a fee and would benefit from topics such as cost coverage, credit, environmental protection, and basic business principles such as organization, planning, inventory, controls, and marketing. This training would be provided by: (i) a local consultant with experience in credit and financial systems;

(ii) a local consultant with experience in training; and (iii) three credit advisors. Institutional strengthening would be provided by an international consultant hired by the Bank to carry out the required interim evaluation that will take place during the project execution.

2. Foundation for Sustainable Development (FUNDES)

a. Credit component (US\$500,000)

- 3.4 An amount equivalent to US\$500,000 would be extended to FUNDES to expand its on-lending to microentrepreneurs primarily located in the cities of David, Santiago, Las Tablas, Chitre, Penonome, and Aguadulce. Approximately 400 loans averaging amounts of US\$2,500 will be extended to program beneficiaries to finance working capital and/or fixed investments to support small enterprises involved in light manufacturing and agro-industry, handicrafts and other activities that will encourage the use of national raw materials, and services and commerce at both the wholesale and retail level. Approximately 50-60% percent of the loans will be channeled to women located in the interior of the country.

b. Non-reimbursable technical cooperation (US\$100,000)

- 3.5 The equivalent of US\$100,000 would be allocated to finance the non-reimbursable technical cooperation component of the program, including the institutional strengthening of FUNDES and provision of technical assistance to program beneficiaries. The resources would be used to finance: (i) an expert to design and install an updated credit management system; (ii) the acquisition and installation of a computer network system to connect the head office and regional offices and to improve efficiency in the management and follow-up of the credit portfolio; (iii) training of FUNDES' staff in the operation of the computer technology; (iv) preparation of a video to be used by FUNDES in its technical assistance program for final beneficiaries; and (v) hiring of an international consultant to undertake the required interim institutional evaluation.

C. Cost of the program

- 3.6 The total cost of the program would be the equivalent of US\$980,000 to be distributed as follows:

COMPONENT	CACPYMER	FUNDES	TOTAL
Credit	250,000	500,000	750,000
Technical Cooperation	130,000	100,000	230,000
TOTAL	380,000	600,000	980,000

The CACPYMER program would be financed in its entirety on a non-reimbursable basis with resources from the Japan Special Fund. Financing to FUNDES would be forthcoming from the Social Progress Trust Fund. The financing would be provided on a reimbursable basis and the technical cooperation on a non-reimbursable basis.

D. Execution of the program

1. Responsibility for program execution

- 3.7 Each IO would be required to sign a separate financing agreement with the Bank and would be responsible for executing the program in its territorial jurisdiction.

2. Credit regulations

- 3.8 The draft Credit Regulations governing execution of the program are presented as Annex III to this document. These regulations are consistent with the Bank's rules and policies for the Small Projects Financing Program, as well as with the legal provisions and banking and financial practices in effect in Panama.

3. Training and technical assistance to the beneficiaries

- 3.9 The training and technical assistance to be provided to the micro and small entrepreneurs when deemed necessary by the IOs, would be provided by the training officials and extension agents in each organization.

4. Procurement of goods and services

- 3.10 Responsibility for the procurement of goods and services covered by the proposed programs would be that of the respective IOs, to which end the Bank's relevant rules and policies would be followed.

5. Advance of funds

- 3.11 Both of the proposed operations will require sufficient funds to execute the programs in an efficient and timely manner. Therefore, as a special condition, it is recommended that an advance of funds up to 20% of both the financing and technical cooperation to each IO be disbursed at their request.

6. Technical cooperation

- 3.12 Responsibility for selecting and engaging the consulting services provided by this program would rest with each of the IOs, except for the hiring of the external evaluator which would be hired directly by the Bank.

7. Execution of the programs in stages

- 3.13 The programs of both IOs would be executed in two stages, the first of which would be considered terminated after the commitment of 50% of the funds. It is understood that the funds for a project are committed as soon as the beneficiary signs the corresponding loan contract with the respective IO. Before the implementation of the second stage, an evaluation would be undertaken of each of the programs, including an analysis of: (i) the application of interest rates charged by the IOs under their credit programs; (ii) the proportion of the loan portfolio in arrears; (iii) the profitability of the services rendered; (iv) any measures taken to protect the environment, including a list and description of the microenterprise activities handled by each IO, the amounts financed for each activity, and comments on their possible environmental impacts; and (v) any provisions geared toward women which facilitate their access to credit, training and technical assistance.

8. Disbursement period for program resources

- 3.14 It is proposed that the resources from the financing and parallel technical cooperation operations be disbursed within a period of 36 months starting from the date in which the respective agreements become effective.

9. Use of the interest rate spread and recoveries

- 3.15 The spread between the fee charged by the Bank and the average basic deposit rates set by the national banking system for deposits of up to one-year, to be used as a reference point in setting the interest to be charged to program beneficiaries, would be used to capitalize each IOs revolving credit fund.
- 3.16 While the financing agreements are in effect, repayments on loans granted from program resources may only be used by the IOs to grant new loans that substantially adhere to the same conditions as those set forth in the respective financing agreements and in the program's credit regulations, unless the Bank authorizes the IOs in writing to use them otherwise.

10. Use of the resources generated from the investments

- 3.17 Similarly, while the financing agreement is in effect, the resources generated from the investments will be used solely to cover operating costs, and the surplus, if any, will be added to the IO's revolving credit fund, unless the Bank authorizes it in writing to use it otherwise.

11. Portfolio in arrears

- 3.18 During the execution of the program, each IO will take appropriate steps to insure that arrears are kept below five percent of their

total loan portfolios. In the event that this is not adhered to, the Bank reserves the right to suspend disbursements, taking into account any circumstances that would justify a temporary increase in the delinquency rate. To this end, during program execution, each IO will submit information on the status of their loan portfolio to the Bank every six months as part of the required progress reports.

12. Environmental aspects

- 3.19 Among their training activities, both IOs carry out environmental education programs and support the execution of projects which foster the conservation and protection of natural resources and the environment. It is not believed that execution of this program would have a significant adverse impact on the environment; therefore, the Environmental Management Committee classified both operations in Category II at its meeting of February 8, 1995.

IV. THE BENEFICIARIES

A. Characteristics

- 4.1 The beneficiaries of the program would be micro and small entrepreneurs located in both urban and rural areas of the country who are involved in light manufacturing activities, wholesale and retail commerce, and service activities. These individuals currently lack access to conventional credit sources and have an annual per capita income at or below the level calculated by the Bank in defining low-income groups in Panama.

B. Estimated number of beneficiaries

- 4.2 It is estimated that a total of 460 loans would be granted under the credit programs of both IOs, 60 of which would be granted by CACPYMER and 400 of which would be granted by FUNDES. Beneficiaries of the CACPYMER program would be located in Panama City and Colon, while FUNDES' beneficiaries would reside primarily in the outlying cities of David, Santiago, Las Tablas, Chitre, Penonome, and Aguadulce. CACPYMER estimates that around 40% of the credit recipients would be women, and that its credit and technical assistance program would indirectly benefit around 300 persons. FUNDES estimates that approximately 1,000 persons would benefit indirectly from its proposed technical assistance and credit programs, and that around one-half of the loans would be disbursed to women.

V. VIABILITY, JUSTIFICATION AND RISKS OF THE PROGRAM

A. Socioeconomic viability

- 5.1 The proposed program's resources would directly impact on the living conditions and quality of life of more than 1,300

individuals who currently lack access to conventional sources of credit, and who currently have incomes below the level calculated by the Bank in defining low-income groups in Panama. Execution of the proposed program would enable micro and small entrepreneurs to receive technical assistance in addition to credit, thereby contributing to an increase in their productivity and income levels. The proposed program would also strengthen the level of employment in the rural sector. Other economic benefits would be derived from the execution of the proposed program, such as environmental impacts, and decreased migration from rural to urban areas.

B. Institutional viability

- 5.2 As previously mentioned, appraisal of the proposed operations revealed certain institutional weaknesses which should be remedied to assist the IOs in executing their programs more efficiently and to play a more proactive role in the future in formulating and implementing programs similar to the one proposed herein. To this end, the parallel non-reimbursable technical cooperation operations to each IO have been designed to provide institutional strengthening to enhance their capacity to provide loans, training and technical assistance to beneficiaries, and to improve their accounting and management information systems.

C. Financial viability

- 5.3 The program resources would be used to finance economic units whose financial viability would be verified by the IOs during their analysis of the loan applications, on the basis of eligibility criteria previously agreed with the Bank for both beneficiaries and projects.
- 5.4 The financial viability of the program lies in the application of variable interest rates which are positive in real terms and which, by providing for maintenance of value and capitalization of the IOs' loan portfolios, would also cover intermediation costs and the creation of a reserve against bad debts. Similarly, the services in the form of training programs to be provided by both IOs would generate additional revenue which would allow such activities to become self-financing in the future. In addition, the financial projections made during project appraisal demonstrated that, upon completion of this program, the IOs would be in a position to continue operations in a self-sufficient and profitable manner, for the benefit of the most disadvantaged persons in the country.
- 5.5 Moreover, the implementation of the parallel non-reimbursable technical cooperation would enable the IOs to achieve satisfactory levels of administrative and operational efficiency so that they can provide continuity in programs designed to benefit the country's micro and small entrepreneurs with limited economic means.

D. Justification

- 5.6 The two proposed financing and technical cooperation operations fall within the eligibility criteria of the Small Projects Financing Program (GP-75-7 and GN-1238-2) and are consistent with the Bank's Operating Policy on Women in Development (GP-114-3) and the guidelines established in the Bank's VIII Replenishment Document.
- 5.7 In addition, the proposed program and would directly benefit groups with limited economic means who at present lack access to conventional sources of credit, and would generate employment opportunities, foster the application of appropriate technologies, and result in actions which do not impact negatively on the environment. Most importantly, the implementation of the programs would strengthen the IOs both institutionally and financially so that they can play a more proactive role in the future in developing and carrying out projects targeted to the low-income and economically and socially vulnerable groups in both urban and rural areas of the country.

E. Risks of the program

- 5.8 The main risks of the operation are: (i) the failure of the Panamanian Government to effectively implement its adjustment program which is aimed at opening the economy and improving the climate for private sector development; (ii) a possible reduction in the estimated demand for credit on the part of the entrepreneurs that will have to pay real interest rates on loans granted under the program; and (iii) the chance that institutional weaknesses of the IOs are not corrected as a result of the technical cooperation designed for this purpose.
- 5.9 In spite of the risks identified, it is highly likely that the program beneficiaries will be prepared to pay the proposed interest rates in return for certainty and speed in the receipt of their credits, given the past number of loans disbursed under the revolving credit programs of the IOs. In addition, specific measures have been included in the parallel non-reimbursable technical cooperation operations to improve operational and financial systems which are expected to strengthen the IOs and contribute to the overall success of the projects.

VI. CONCLUSIONS AND RECOMMENDATIONS

- 6.1 The foregoing analysis supports the conclusion that the execution of the proposed program is viable. Therefore, the Management of the Bank recommends that the Board of the Executive Directors approve the corresponding financing and technical cooperation to CACPYMER and FUNDES.

**INTER-AMERICAN DEVELOPMENT BANK
COUNTRY DIVISION 4
SMALL PROJECTS FINANCING PROGRAM**

**RUBEN REYNA PUPO SAVINGS AND LOAN COOPERATIVE OF THE NATIONAL UNION
OF SMALL AND MEDIUM ENTERPRISES, R.L. (TC-92-04-36-4)
FOUNDATION FOR SUSTAINABLE DEVELOPMENT (TC-92-04-42-1)**

PLAN OF OPERATIONS

I. BACKGROUND

- 1.1 To complement the applications for financing submitted under the Small Projects Financing Program, the Ruben Reyna Pupo Savings and Loan Cooperative of the National Union of Small and Medium Enterprises, R.L. (CACPYMER) and the Foundation for Sustainable Development (FUNDES) have each requested from the Bank a non-reimbursable technical cooperation operation to fund their institutional strengthening and technical assistance programs.
- 1.2 The Government of Panama, through the Ministry of Planning and Economic Policy, notified the Bank that it has no objection to the Bank's granting the technical cooperations requested by the two institutions referred to in the preceding paragraph.

II. OBJECTIVES

- 2.1 The objective of this program is to contribute to the institutional strengthening of the intermediary organizations (IOs), and to provide training and technical assistance in business administration and related subjects to the credit program participants participating in the small projects financing programs to be carried out parallel to this operation. The technical cooperation would ensure that the subprogram is properly executed and that the IOs can in the future play a more proactive role in formulating and implementing similar programs aimed at assisting low-income groups.
- 2.2 The specific goals of this program are: (i) to improve and expand the capacity of the participating IOs to grant credits and provide training and technical assistance services to microentrepreneurs and small business owners, in order to enhance their income and thereby improve the socioeconomic situation of their families; (ii) to create and strengthen employment in both urban and rural areas of the country; (iii) contribute to the incorporation of environmental conservation practices; and (iv) to strengthen the IOs institutionally in their lending activities so that they can achieve financial and operational self-sufficiency in the future.

III. DESCRIPTION

- 3.1 To achieve the proposed objectives, the IOs would use the resources of this technical cooperation to finance the procurement of consulting services, the purchase computer equipment and software to implement loan evaluation monitoring programs, and acquisition of teaching materials to be used in their respective programs.

1. Contracting of experts

a. CACPYMER

- 3.2 CACPYMER will use part of the funds ear-marked for technical assistance to contract the following consultants according to the Terms of Reference presented in Annex I-1: (i) a consultant in credit and financial systems for a period of 12 months to prepare a financial plan, review the financial and accounting systems of the IO, and train the IOs personnel in its implementation and operation; (ii) three credit advisors for a period of 36 months each to identify potential clients and projects, advise borrowers, review and update the methodology for loan proposal evaluation, prepare periodic reports for the IOs, and advise IO personnel; and (iii) a training consultant for a period of 6 months to train program participants in basic concepts of business administration and related topics, management, and negotiation of financing.

b. FUNDES

- 3.3 Resources of the program would be used to hire the following individuals: (i) a consultant in the area of financial administration to design and install credit software to facilitate the monitoring, follow-up and evaluation of the credit portfolio; and (ii) a consultant in the area of credit systems to provide training to FUNDES' staff in the regional offices in the use of the computer network system.
- 3.4 In addition to the consultants to be hired directly by each IO, the Bank would be responsible for directly hiring an expert in institutional evaluations to carry out the required mid-term review required by the Bank for each IO. The evaluation would be carried out during a period of approximately 2 weeks, when approximately 50% of the parallel financing has been committed.

2. Procurement of supplies and equipment

a. CACPYMER

- 3.5 The procurement of supplies and equipment to be used by CACPYMER under the proposed operation will include: a vehicle for program supervision and technical assistance, a computer, and teaching materials for the training courses for the beneficiaries.

b. FUNDES

- 3.6 The procurement of supplies and equipment to be used by FUNDES in the execution of the program will include: (i) purchase and installation of a computer network system and related software to connect the 11 regional offices to FUNDES' headquarters in Panama City; and (ii) preparation of a video on microenterprise development to be used by FUNDES in technical assistance activities for the project beneficiaries.

IV. COST AND FINANCING

- 4.1 The total cost of the technical cooperation program would be an amount equivalent to US\$230,000, of which US\$130,000 would be allocated to CACPYMER and US\$100,000 to FUNDES. The break-down of the cost of each program would be as follows:

1. CACPYMER

<u>CATEGORY</u>	<u>AMOUNT IN US\$</u>
2.1 Fees <u>1/</u>	75,600
3.5 Teaching materials	5,000
5.1 International Travel <u>2/</u>	6,000
6.3 Equipment <u>3/</u>	23,000
8.2 Evaluation <u>4/</u>	15,000
98. Contingencies	<u>10,000</u>
TOTAL	\$130,000

- 1/ Fees for three types of consultants: (a) 1 expert in credit and finance at US\$1,200/month for 12 months; (b) 1 expert in training at US\$1,200/month for 6 months; and (c) 3 credit supervisors at US\$500/month for 36 months each.
- 2/ Fees for CACPYMER's personnel to attend conferences, seminars or visits to with other organizations specializing in cooperative lending activities for microentrepreneurs.
- 3/ Includes 1 vehicle and 1 computer with a printer.
- 4/ Fees for one consultant to undertake required institutional evaluation (1 visit of approximately 2 weeks).

2. FUNDES

<u>CATEGORY</u>	<u>AMOUNT IN US\$</u>
2.1 Fees <u>1/</u>	12,000
6.3 Equipment <u>3/</u>	68,000
8.2 Evaluation <u>4/</u>	10,000
98. Contingencies	<u>10,000</u>
TOTAL	\$100,000

- 1/ Includes expert in the design and installation of a credit system for approx. 200 hrs. @ US\$20/hr; and expert to provide training to FUNDES' staff in the financial information system (approx. US\$8,000)
- 2/ Includes purchase of computer hardware and software to set up a network connecting the 11 regional offices with the headquarters; and preparation of a video on microenterprise development.
- 3/ Fees for one consultant to undertake required institutional evaluation (1 visit of approximately 2 weeks).

V. EXECUTION

- 5.1 The proposed technical cooperation would be carried out parallel to the credit subprogram which would be approved at the same time as this operation. The consulting services described earlier would be engaged individually by each IO in accordance with the procedures for the selection and contracting of consulting firms and/or individual experts which have been agreed with the IOs. The Bank would be responsible for directly hiring the expert in institutional evaluations to carry out the required mid-term review required by the Bank for each IO.

VI. JUSTIFICATION

- 6.1 The proposed operation meets the requirements established by the Bank for granting non-reimbursable technical cooperation since it would be intended for the institutional strengthening of borrowing organizations that are involved in the process of economic and social development in Panama, and for program participants who would benefit directly from the operation.
- 6.2 Neither the IOs or program participants have the resources to finance the proposed technical cooperation operation, which will contribute significantly to an improvement in the operational and financial management of their credit operations. If the IOs are to carry out their activities efficiently and effectively, and assist the program beneficiaries to succeed in the development of their micro and small businesses, they will require the institutional strengthening and training for which this operation has been designed to provide.

VII. SOURCE OF FUNDING

- 7.1 Funding for CACPYMER's technical cooperation will be forthcoming from the Japan Special Fund; resources for FUNDES would be forthcoming from the Social Progress Trust Fund.

VIII. DISBURSEMENTS

- 8.1 The disbursement period for each technical cooperation would be 36 months, and would be implemented as of the date of the signing of the respective agreements. To provide sufficient time and resources to efficiently implement the programs and to acquire the necessary equipment and training materials, it is recommended that, at the request of each IO, up to 20% of the funds allocated to each program should be disbursed.

IX. REPORTS

- 9.1 All consultants and experts hired for periods greater than six months would be required to submit bi-annual progress reports to the respectively intermediary, with a copy to the Bank. Moreover, within 60 days of the end of their contracts, the consultants or experts would present a final report containing the results achieved and recommendations for future action.
- 9.2 The institutional evaluator would be required to present a report on the institutional evaluation of each intermediary based on the terms of reference to be mutually agreed upon.
- 9.3 Within 90 days following the date that the final report of each consultant or expert is presented, the IOs would be required to submit a report on the evaluation of that consultant or expert to the Bank.
- 9.4 Within 120 days of the end of the calendar year in which the last disbursement of the program is made, the IOs would be required to present to the Bank a financial report detailing the expenses charged to the non-reimbursable technical cooperation operation funded by the Bank, verified by independent auditors acceptable to the Bank.

X. SUPERVISION

- 10.1 Responsibility for supervising the execution of each of the two technical cooperation operations would rest with each individual IO. The Bank will also be responsible for supervision of the programs through its Country Office in Panama.

XI. EVALUATION CRITERIA

- 11.1 The technical cooperation of each intermediary would be evaluated approximately 24 months after the date of the last disbursement,

simultaneously with the financing programs, in order to verify the degree to which the IOs have complied with the project objectives. Consideration would also be given to the quality of the work undertaken and the content of the reports described in Section IX.

XII. UNIT RESPONSIBLE IN THE BANK

- 12.1 The Regional Operations Department 2, Country Division 4, will be responsible for these operations.

RUBEN REYNA PUPO SAVINGS AND LOAN COOPERATIVE OF THE NATIONAL UNION
OF SMALL AND MEDIUM ENTERPRISES, R.L. (TC-92-04-36-4)
FOUNDATION FOR SUSTAINABLE DEVELOPMENT (TC-92-04-42-1)

TERMS OF REFERENCE

I. RUBEN REYNA PUPO SAVINGS AND LOAN COOPERATIVE OF THE
NATIONAL UNION OF SMALL AND MEDIUM ENTERPRISES, R.L. (CACPYMER)

A. Credit and Financial Systems Consultant

- 1.1 CACPYMER will contract a consultant in credit and financial systems with a minimum of five years experience in the implementation and administration of credit programs and financial management. This consultant will work closely with cooperative employees for a period of 12 months and will be responsible for the following tasks:
- a. Prepare a financial plan that includes the analysis of the policies required to guarantee the self-sufficiency of the organization in the medium and long terms;
 - b. Review the financial and accounting systems of the organization and of the credit program to verify the financial position of the cooperative, and to formulate recommendations for improving this position;
 - c. Advise and train the cooperative's personnel so that the financial records of the project contain the following information: (i) disbursed amounts, authorized credit amounts, payments made and use of those payments; (ii) project investments that are recorded in accordance with Bank accounting standards; and (iii) sufficient detail in all accounts to identify acquired assets and services contracted, and their use;
 - d. Review the existing credit system, including the follow-up and evaluation components, and recommend modifications for its improvements, emphasizing beneficiary selection and the technical and financial viability of credit applications;
 - e. Review the administrative system of the loan portfolio and establish the required Bank methodology to analyze its classification; and
 - f. Prepare written guidelines for the process of decision-making for the Loan Committee.
 - g. Review both the impact and results of the internal structuring to be carried out within CACPYMER and the cooperative's 3-year strategic plan, and make recommendations for improvements.

B. Training Consultant

1.2 A consultant will be hired for a total of 6 months with a minimum of three years experience in training, and a degree or equivalent experience in business administration, economics, or finance. The consultant would be contracted to teach 3 modules of approximately 2 months each, and would be responsible for the following areas of training:

- a. basic concepts of business administration, including administration, marketing, production, personnel and finance and the operative inter-relationships of each of these areas;
- b. management, leadership, and organizational motivation;
- c. pricing policy and competitiveness analysis;
- d. basic finance concepts applicable to the administration of the cooperative, including cash flow analysis, loan amortization, investment decisions, and credit and cash sales policy; and
- e. basic concepts required to negotiate financing, such as the development of a project profile, objectives, financing requirements, and costs and capacity for repayment.

C. Credit Advisors

1.3 CACPYMER will contract three credit advisors with a minimum of five years experience in credit supervision and a formal education in the field of finance. The advisors would be contracted for a total period of 36 months each to undertake the following tasks:

- a. identify potential clients for the credit program through promotional activities;
- b. advise business owners on the preparation of the budget within Bank and CACPYMER guidelines, assist in the preparation of Bank and CACPYMER financing requirements, and follow up during both the implementation and operative phases of the project to identify and strengthen any weaknesses in the beneficiaries' operations, including training where required;
- c. review and update the methodology for the evaluation of loan proposals, the forms used in gathering data for the credit program, and the criteria used in project selection process;
- d. prepare periodic reports for CACPYMER and the Bank, including an analysis of the credit portfolio, evaluation of the execution of the program, obstacles identified, and activities undertaken; and
- e. train cooperative personnel to prepare reports on the loan portfolios for both the credit program and the cooperative,

including the analysis and evaluation of activities that will maximize the efficiency of the administration of the loan portfolio.

D. Specialist in Institutional Evaluations

- 1.4 The Country Office, in consultation with OD4, will contract an international or local expert or a firm specializing in microenterprise programs to conduct an institutional evaluation of CACPYMER after 50% of the funds allocated to this project have been committed. The expert or firm will be contracted with the specific view to measure the intermediary's progress in achieving operational and financial self-sufficiency in its programs.

II. FOUNDATION FOR SUSTAINABLE DEVELOPMENT (FUNDES)

A. Expert in Financial Information Systems

- 2.1 An expert with at least 3 years of working experience in the design and installation of financial information systems, preferable for organizations that work with microenterprise programs, would be hired for a period of approximately 200 hours to carry out the following tasks:
- a. Design and install a computerized financial information system to carry out the following functions: (a) accounting by funds, with financial and accounting ledgers; (b) control of the credit portfolio, separating costs for financial intermediation; (c) input of general data required for the administration of the credit program; and (d) follow-up and evaluation of the credit portfolio including: (i) up to date information on the status of the portfolio; (ii) incorporation of a data base on the beneficiaries of the program to measure the impact of the program; and (iii) control measures to gauge compliance with the objectives of the program.
 - b. Advise in the purchase and installation of the computer hardware and software to be installed in the headquarters and regional offices of FUNDES.
 - c. Prepare written guidelines for the use of the financial information system to be installed.

B. Specialist in Institutional Evaluations

- 2.2 The Country Office, in consultation with OD4, will contract an international or local expert or a firm specializing in microenterprise programs to conduct an institutional evaluation of CACPYMER after 50% of the funds allocated to this project have been committed. The expert or firm will be contracted with the specific view to measure the intermediary's progress in achieving operational and financial self-sufficiency in its programs.

RUBEN REYNA PUPO SAVINGS AND LOAN COOPERATIVE
BALANCE SHEET AS OF DECEMBER 31, 1993, 1992 & 1991
(US\$)

FINANCIAL STATEMENT	1993	1992	1991
<u>ASSETS</u>			
Cash	136,005	167,808	248,065
Investments	0	68,812	0
Accounts Receivable <u>a/</u>	65,351	55,720	40,714
Portfolio	911,457	715,878	540,488
(reserve)	(73,405)	(30,376)	(17,954)
Property	81,577	43,512	40,987
(depreciation)	(16,312)	(14,631)	(9,460)
Net Property	65,265	28,881	30,920
Other <u>b/</u>	63,249	9,035	1,743
Total Assets	1,167,922	1,015,758	844,583
<u>LIABILITIES</u>			
Loans	912,585	791,155	706,675
Deposits	42,119	26,819	20,341
Accounts Payable	71,295	80,423	35,528
Reserves <u>c/</u>	17,757	18,268	12,495
Total Liabilities	1,043,756	916,665	775,039
<u>EQUITY</u>	124,166	99,093	69,544
Total Liabilities and Equity	1,167,922	1,015,758	844,583

a/ Includes interest to be collected on loans.

b/ Includes pre-paid expenses, guarantees and deposits on guarantee, and miscellaneous assets.

c/ Includes a legal reserve fund, a cooperative education fund, and a social provision fund mandated by law.

RUBEN REYNA PUPO SAVINGS AND LOAN COOPERATIVE
INCOME STATEMENT AS OF DECEMBER 31, 1993, 1992 & 1991
(US\$)

FINANCIAL STATEMENT	1993	1992	1991
<u>INCOME</u>			
Credit Income	100,108	84,579	45,924
Other <u>a/</u>	16,912	3,305	28,056
TOTAL INCOME	117,020	87,884	73,980
<u>EXPENSES</u>			
Personnel	58,067	39,400	29,999
Administration	28,379	20,927	18,789
Provisions	9,029	12,216	9,143
Total Operational Costs	95,475	72,543	57,931
Financial Costs	9,634	9,950	7,359
TOTAL EXPENSES	105,109	82,493	65,290
<u>NET INCOME</u> <u>b/</u>	(5,679)	5,391	8,690

a/ Includes investment income, fees from training programs, and miscellaneous income.

b/ Includes and adjustment of US\$17,590 in 1993 that represents a clearing of books between CACPYMER and UNPYME of accounts payable and accounts receivable that were outstanding since 1984 between the two organizations.

FOUNDATION FOR SUSTAINABLE DEVELOPMENT
BALANCE SHEET AS OF DECEMBER 31, 1993, 1992 & 1991
(US\$)

FINANCIAL STATEMENT	1993	1992	1991
<u>ASSETS</u>			
Cash	503,223	198,650	728,971
Investments	850,000	1,050,000	1,635,569
Accounts Receivable <u>a/</u>	216,591	197,940	129,622
Portfolio	6,074,364	4,746,059	4,338,078
(reserve)	(214,070)	(204,805)	(213,958)
Property	924,189	832,882	131,137
(depreciation)	(93,888)	(60,323)	(21,972)
Net Property	830,301	772,559	109,165
Other <u>b/</u>	198,287	219,657	81,189
Total Assets	8,458,696	6,980,060	6,808,636
<u>LIABILITIES</u>			
Loans	1,805,000	625,000	500,000
Accounts Payable	15,708	18,588	17,749
Reserves <u>c/</u>	100,027	93,930	90,565
Other <u>d/</u>	241,717	24,030	11,822
Total Liabilities	2,162,452	761,548	620,136
<u>EQUITY</u>	6,296,244	6,218,512	6,188,500
Total Liabilities and Equity	8,458,696	6,980,060	6,808,636

a/ Includes interest to be collected on loans and deposits.

b/ Includes pre-paid expenses, guarantees and deposits on guarantee, and miscellaneous assets.

c/ Represents reserve fund for potential losses on guarantees.

d/ Includes payable marketable securities, accumulated fees and deferred income.

FOUNDATION FOR SUSTAINABLE DEVELOPMENT
INCOME STATEMENT AS OF DECEMBER 31, 1993, 1992 & 1991
(US\$)

FINANCIAL STATEMENT	1993	1992	1991
<u>INCOME</u>			
Credit Income	586,797	506,338	545,721
Investments	107,725	114,625	120,859
Donations	600	7,084	34,740
Other <u>a/</u>	413,470	209,465	108,387
TOTAL INCOME	1,108,592	837,512	809,707
<u>EXPENSES</u>			
Personnel	580,287	447,599	357,475
Administration	329,775	279,371	185,662
Provisions			
Unrecoverable Loans	67,750	80,000	229,650
Authorized Guarantees	5,500	17,222	85,078
Total Operational Costs	983,312	824,192	857,865
Financial Costs	47,548	7,308	6,348
TOTAL EXPENSES	1,030,860	831,500	864,213
<u>NET INCOME</u>	77,732	6,012	(54,506)

a/ Includes fees charged to program participants.

**MODEL CREDIT REGULATIONS
FOR
THE RUBEN REYNA PUPO SAVINGS AND LOAN COOPERATIVE AND
THE FOUNDATION FOR SUSTAINABLE DEVELOPMENT**

SUMMARY OF PRINCIPAL CONDITIONS

I. BENEFICIARIES

- 1.1 The beneficiaries of the program would be those low-income micro and small entrepreneurs, defined in accordance with the guidelines of these Regulations, who are capable of executing and operating the project(s) covered by the financing and who do not have access to conventional sources of credit.

II. ELIGIBLE PROJECTS

- 2.1 To be eligible for financing, a project must satisfy the following requirements: (a) represent aspects of economic and social improvement in the quality of life of its beneficiaries; (b) contribute to the conservation of nature; and (c) demonstrate the capacity of the beneficiaries to work independently in the future. The types of projects that can qualify include those involved in: light manufacturing, wholesale and retail commerce, and services.

III. USE OF THE RESOURCES

- 3.1 The proceeds of the credit program would be used to finance the fixed assets and working capital needed to develop those productive, trade and service activities of the entrepreneurs that are technically and financially viable.

IV. TERMS AND CONDITIONS OF THE LOANS

- 4.1 The following terms and conditions will be applied to the loans approved in the credit programs of this project:
- a. Denomination of loans and repayment: Loans made from program resources and repayments by their beneficiaries will be denominated in current US dollars, since that is the currency of business operations in Panama.
 - b. Terms: Repayment and grace periods would be established by the intermediary organization in accordance with the type of activity that would be financed, the return on capital invested, and the capacity of the beneficiary to repay the loan. In general, loans for working capital would not exceed 12 months, with grace periods of 6 months, and loans for fixed capital would not exceed 36 months, with grace periods of up to 12 months.

- c. Loan amounts: The maximum loan amount for both CACPYMER's and FUNDES' clients would be US\$4,000.
- d. Interest rate: The interest rates charged by the intermediaries on loans made to the program beneficiaries would be variable and positive in real terms, and would be set by the intermediaries taking into consideration the average lending rates applied by the national banking system, plus the spread needed to cover the cost of intermediation and to create a reserve for bad debts. The intermediary, in consultation with the Bank, will periodically revise the interest rates charged on the loans and, if necessary, take appropriate measures consistent with the country's economic policies to harmonize such rates with the Bank's policy in this area.
- e. Repayments: The Intermediary will provide beneficiaries with repayment schedules showing the amounts and dates for payments to principal and interest, the amount of the loan and the rate of interest.
- f. Guarantees: The principal guarantee for the execution of the projects financed with resources from the Bank will be the character and the administrative aptitude of the program's beneficiaries, their technical competence, the ability to produce and market the product, and the economic capability of the project in general. The loans may also be guaranteed by:
(a) land having titles or other proprietary rights; (b) buildings or equipment; (c) guarantors; (d) products that are expected to be obtained; or (e) other goods.

PROPOSED RESOLUTION

PANAMA. FINANCING TO THE COOPERATIVA DE AHORRO Y CREDITO DE LA UNION
NACIONAL DE PEQUEÑAS Y MEDIANAS EMPRESAS RUBEN REYNA PUPO, R.L.
WITHIN THE PROGRAM FOR FINANCING SMALL PROJECTS

The Board of Executive Directors

RESOLVES:

1. That the President of the Bank, or such representative as he shall designate, is authorized, in the name and on behalf of the Bank, as Administrator of the Special Fund of Japan, to enter into such agreement or agreements as may be necessary with the Cooperativa de Ahorro y Crédito de la Unión Nacional de Pequeñas y Medianas Empresas Rubén Reyna Pupo, R.L., of the República de Panamá, to grant it, within the Program for Financing Small Projects, approved by Resolutions DE-85/78 and DE-147/79: (a) nonreimbursable financing for the execution of the program referred to in Document PR- ; and (b) nonreimbursable technical cooperation for the execution of the program, in accordance with Annex I of said document.

2. That up to the sum of US\$250,000, is authorized for the purposes indicated in paragraph 1(a), and up to the sum of US\$130,000, for the purposes indicated in paragraph 1(b), both chargeable to the resources of the Special Fund of Japan.

PROPOSED RESOLUTION

PANAMA. FINANCING TO THE FUNDACION PARA EL DESARROLLO SOSTENIBLE
WITHIN THE PROGRAM FOR FINANCING SMALL PROJECTS

The Board of Executive Directors

RESOLVES:

1. That the President of the Bank, or such representative as he shall designate, is authorized, in the name and on behalf of the Bank, as Administrator of the Social Progress Trust Fund, to enter into such agreement or agreements as may be necessary with the Fundación para el Desarrollo Sostenible, of the República de Panamá, to grant it, within the Program for Financing Small Projects, approved by Resolutions DE-85/78 and DE-147/79: (a) reimbursable financing for the execution of the program referred to in Document PR- ; and (b) nonreimbursable technical cooperation for the execution of the program, in accordance with Annex I of said document.

2. That up to the equivalent of US\$500,000, is authorized for the purposes indicated in paragraph 1(a), and up to the equivalent of US\$100,000, for the purposes indicated in paragraph 1(b), both chargeable to the resources of the Social Progress Trust Fund.