Final Evaluation of the EC-funded Private Sector Support Programme titled "Support to the Risk Capital Facility 2" – SA/21.031700-05-01

SOUTH AFRICA

Final report

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FINAL REPORT	
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List of Acronyms

AFD	Agence Française de Développement
ASGISA	Accelerated and Shared Growth Initiative of South Africa
ATIRR	After Tax Internal rate of Return
B-BBEE	Broad-Based Black Economic Empowerment
BBSDP	Black Business Supplier Development Programme
BEE	Black Economic Empowerment
BP	Business Partners
BSS	Business Support Services
BSP	Business Support Programme
CBO	Community-Based Organisation
Cosatu	Congress of South African Trade Unions
CPPP	Community Public Private Sector Partnership
CSP	Country Strategy Paper
DBSA	Development Bank of Southern Africa
DFD	Development Funds Department
DFI	Development Finance Institutions
EC	European Commission
EDD	Economic Development Department
EDSA	Entrepreneurial Development Southern Africa
EIB	European Investment bank
EU	European Union
FA	Financial Agreement
GDP	Gross Domestic Product
GWME	Government Wide Monitoring and Evaluation
HDIs	Historically Disadvantaged Individuals
HDPs	Historically Disadvantaged Persons
HEDC	Highveld Entrepreneurial Development Centre
ICT	Information and Communication Technology
IDC	Industrial Development Corporation
IDT	Independent Development Trust
IDZ	Industrial Development Zone
IRR	Internal Rate of Return
KfW	Kreditanstalt für Wiederaufbau
KPI	Key Performance Indicator
MFI	Micro-Finance Institution
MFRC	Micro-Finance Regulatory Council
MOA	Memorandum of Agreement
MTR	Mid Term Review
NAO	National Authorising Officer
NEDLAC	National Economic Development and Labour Council
NEF	National Empowerment Fund
NFC	Niche Fund channel
NGOs	Non-governmental organisations
NYDA	National Youth Development Agency
ODA	Official Development Assistance
PICSA	Public Investment Corporation, South Africa
PII	Partnership in Industrial Innovation
PIMD	Post Investment Monitoring Department
PPFA	Preferential Procurement Framework Act
PPP	Public Private Partnerships
PSC	Project Steering Committee
RATIRR	Real After Tax Interest rate of Return
RCF	Risk Capital Facility
ROM	Result Oriented Monitoring
SADC	Southern African Development Community
SAMAF	South African Micro-finance APEX Fund
SARS	South African Revenue Service
SAVCA	South Africa Venture Capital and Private Equity Association
SBSP	Sector Budget Support Programme
SBU	Sector Business Unit
SEDA	Small Enterprise Development Agency
SEFA	Small Enterprise Finance Agency
SME	Small and Medium Enterprise
SMEDP	Small and Medium Enterprise Development Programme
SMME	Small, Micro and Medium Enterprise
SRI	Social responsibility Investment
SOE	State-Owned Enterprise
SPV	Special Purpose Vehicle
SR	Social Responsibility
Stats SA	Statistics South Africa
TDCA	Trade and Development Cooperation Agreement
the dti	The Department of Trade and Industry
TIDP	Trade and Industrial Development Programme

VC	Venture Capital	ZAR	South African Rand
WR SBU	Work out and Restructuring Strategic Business Unit		

EXECUTIVE SUMMARY

➢ Methodology and report presentation

This evaluation was conducted over a period of six weeks in September and October 2013 in South Africa by two independent experts with financial and private sector development backgrounds.

The mission was based on project document review, extensive meetings with the RCF team, visit and assessment of a sample of "investees" as well as meetings with the main stakeholders. A visit to the European Investment Bank was also organised in Luxemburg.

The mission's findings, conclusions and recommendations are presented in this report, structured in four main chapters as follows: (context and structure of the Programme are detailed in Annexes 7.1 and 7.2:

- Presentation of the Programme results, in Chapter 2;

- Main findings classified as per the usual OECD-DAC criteria: Relevance, Effectiveness, Efficiency, Impact and Sustainability, in Chapter 3;

- Main conclusions and lessons learnt, in Chapter 5;

- Recommendations for the future of RCF and for potential future activities to improve access to finance for Small, Micro, and Medium Size Enterprises (SMMEs), in Chapter 6.

➢ Context and objectives

South Africa is still confronted with inequalities inherited from the apartheid era, twenty years after, despite the Government Broad-Based Black Economic Empowerment (B-BBEE) policy.

The economic power of the black people remains limited in the business arena, while unemployment mostly consisting of Historically Disadvantaged Persons (HDPs) is about 30% of the population, despite the efforts of the last twenty years, with an even higher percentage in the poorer regions.

In this context, the Risk Capital Facility (RCF) objectives were/are to support the development of HDP controlled small and medium size enterprises (SMEs) with a significant HDP job creation impact, including female employment.

The objectives are particularly challenging, since SMEs to be supported should be controlled by HDPs who usually do not have much financial means, limited business experience especially in the poorer regions where the needs are significant, in a competitive market.

The Black Economic Empowerment (BEE) target of RCF, as defined in the investment guidelines is the result of an economic and political decision, based on the very special post-apartheid situation of the country, whereby the costs of the programme in term of concessionary interest and high risk financial support is warranted by the social and economic benefits to BEE empowerment. The Programme is fully relevant and in line with the B-BBEE Government policy to support HDPs as well as with the EU Private Sector support focus.

- Programme structure

The programme was structured as a Sector Budget Support Programme (SBSP) contracted by the European Union (EU) with the South African National Treasury, in line with the Country Strategy at the time. However, RCF follows a number of the features attached to more traditional Programme support, especially since the RCF 2 was a follow up of a previous programme referred to as RCF 1.

The Risk Capital Facility 2 amounted to Euro 50 million, of which, Euro 47,23 million was to be utilised through equity or quasi equity facilities to support high risk HDP controlled SME development projects, non-bankable with traditional lenders. The balance was to be used to fund the operational costs of the programme plus the fees due to the European Investment Bank (EIB) which acted as the advisor and supervisor to the Programme during the investment phase.

A special allocation for Euro 5 million equivalent has been provided by the South African Government to support the “investees” Business Support needs, as a new programme feature, compared to RCF 1, based on the result of lessons learnt.

Oversight of the Programme rested with the Department of Trade and Industry (dti) through a large Project Steering Committee (PSC) harnessing a wide array of competence. The implementation of the Programme was entrusted to the Industrial Development Corporation (IDC). The various responsibilities of the partners in the programme were defined through Memorandums of Understanding/Agreement (MOU/MOA) between the EIB and the EU, the EIB and IDC and the dti and IDC.

The main feature of the programme was its catalytic role in promoting access to finance for BEE through the financial support of high risk HDP controlled (defined as more than 25% of equity controlled by HDP) SME development. This support was to be delivered through three different channels, the Direct channel whereby IDC would identify the prospective clients (about 50 % of the investees), the Niche Fund channel whereby RCF would co-invest in Funds with socio-economic and financial targets in line with its covenants (targeting about 20 % of the investees) and the Third Party channel whereby RCF would co-invest with commercial financial institutions. The objectives of the last two channels were to increase the leverage and outreach of the programme through the involvement of partners.

The SME target was described in the Financing Agreement and more precisely defined in the investment guidelines, to ensure that the investees supported meet the challenging objectives of the Programme.

- Results

Seven categories of results were expected, in terms of enterprises supported, in terms of jobs created, with at least 30 % female employment, with a regional bias towards the poorer regions, a sector wide dispersion, at an interest rate of return (IRR), which allowed for the maintenance of the nominal value of the Facility over the duration of the programme. Another expected result was increased HDP empowerment through shareholding and opportunities for HDPs to hold managerial positions. Other expected result was access to and use of BSS as well as increased South African investments in other African countries and strengthening of HIV/AIDs prevention and protection of the environment by the investee businesses.

Globally, the results have been attained despite the challenges (Cf. Table 1 hereafter).

Main difficulties in achieving the expected results and wider impact were the following:

- The delivery of the Programme was delayed at the start by one year due to the slow setting-up of the various Memorandum of Understanding/Agreement, while the investment phase which was due to be spread over four years had to be extended by another two years, due to the limited number of acceptable prospects.

- RCF was not able to activate the Third Party channel, thereby not increasing its leverage and outreach as much as planned through the involvement of the commercial financial institutions.

- The Business Service Support grants took time to become operational. Its effectiveness and real impact is yet to be assessed in view of its recent deployment.

Table 1: RCF results per the seven categories

Expected results	Results obtained	Comments
Result 1: SMEs access to development funding increased, resulting in 70 enterprises having been funded	Since its inception, RCF2 has supported a total of 78 Investees. The breakdown is as follows Active: Direct Channe-53 Active Niche Fund Channel_10 Exits-2, Write Offs_13 (NB the total number of investees does not include cancellations which were 7)	The most common investment instruments among the 63 active RCF 2 investees are the subordinated loans constituting 81% of the deals followed by 16% preference shares and 3% shareholder loans or equity. The funds were leveraged at an average of 286% over the course of the 7 years.
Result 2: Increased numbers of new jobs created for HDPs in particular for women, resulting in some six thousand new jobs.	It is estimated that RCF has facilitated the creation of 6369 jobs in the SMEs that have been supported. It is estimated that 30% of newly created jobs are held by women.	IDC is not systematically tracking their investees annually and it is possible that the figures might have changed since the last comprehensive survey conducted in 2010/11.
Result 3: A revolving self-sustainable RCF 2 has been established, which is on target to achieve the financial goals established by the dti and to meet the agreed expectations of other investors.	It is still too early to say whether the fund will revolve and remain sustainable as there have only been 3 exits and reflows to the value of ZAR 30, 295, 705	The set IRR is competitive in the market given the high risk nature of the fund.
Result 4: Increased HDP empowerment through shareholding and possibilities for HDPs to hold managerial positions.	The approved investees either had a 25.1% shareholding or were on course to fulfil it within the stipulated one year. There were 7 applications with a Worker's Trust component intended to improve the BEE shareholding. However, some investees struggled to achieve the requirements within the	The IDC has not been able to provide the updated HDP empowerment statistics in all the investees due to limited visits. It is important for RCF to follow up the HDP empowerment annually to see whether or not there are any changes.

	stipulated 12 months[1]	
Result 5: Access to and use of BSS has been improved through effective assistance to SMEs. As a result the Investees have received adequate BSS in the form of relevant training, technical assistance and monitoring over the project lifetime.	27 out of the 63 active investees received BSS at a cost of ZAR 20, 247, 155. Of this figure, only ZAR 4, 384, 210 has been disbursed.	Access to and use of BSS has improved immensely from the time of the MTR. Through RCF, IDC now undertakes ex-ante a BSS needs survey on all its project applications. BSS is now a major feature in the organisation. The amount set aside for BSS is ZAR45 000,000[2]. The approved amount at the point of the final evaluation is less than half of the budget allocation and the disbursed amount is slightly less than 10%. One of the Niche Funds has made a request that IDC considers providing the BSS as a loan for their investees.
Result 6: Increased South African SME investments in other African countries, targeting 500 jobs, either for HDPs in South Africa or residents in those countries.	This target was relaxed as the project's main geographic result is expected in South Africa and besides that the present IDC infrastructure is not yet ready to tackle SME's abroad.	RCF2 made an investment in Angola but the inability to collect receivables from main debtor (Angolan Government) resulted in increased uncertainty to repay facilities.
Result 7: Environmental enhancement activities will be actively encouraged. The health and environmental aspects of investee businesses have been strengthened. As a result every investee business has HIV/AIDS and environmental protection plans. The progress against plans will be monitored and measured yearly.	Some of the investees do not have formal HIV/Work policies but they have activities, which promote environmental/HIV awareness.	The log frame states that progress against plans would be measured yearly, however, this has not been done despite the fact that the Feb 2012 PSC meeting took a decision that PIMD should develop a template to address the key issues noted by the EIB-IDC on the monitoring of HIV plans.

[1] Cleardata and Massive TV have struggled to reach this target
[2] Euro5 million converted using an exchange rate of Euro1=ZAR9 according to the 2nd amendment to the RCF2 IDC EIB Memorandum of Agreement dated 19 December 2011

- Findings

The main point to bear in mind is the great challenge that the project addresses, i.e. economic development through access to finance support towards SMEs controlled by Historically Disadvantaged Persons with a view to supporting Black Economic Empowerment, promote economic development and HDP job creation, with a strong bias towards the poorer regions of the country in a very competitive environment.

In such context, the fact that the Programme has managed to achieve almost all the expected results is a great accomplishment and the Programme can be deemed a success.

It is regretted however that the Programme did not assess through a systematic annual review the social and financial performance of the investees over time, so as to measure the effective social impact as well as the overall value of the portfolio, especially bearing in mind the risks associated with the clients whose subordinated loan interest and principal repayments have been postponed to the end of the loan duration due to insufficient cash flow.

- Key issues

This being said, a number of improvements could be undertaken to ensure an even better performance and a number of lessons can be drawn for the future.

- IDC as the implementing agency

The choice of IDC as the implementing agency had, at the time, the obvious advantage of entrusting the Programme to a reliable, professional and financially strong institution, compared to Khula (now merged into the Small Enterprise Finance Agency (SEFA) or the National Empowerment Fund (NEF), with the disadvantage of not being SME focused. This last weakness has been mitigated over time; IDC now has full responsibility over the financial support of this smaller segment of the market through its new subsidiary: SEFA.

It is unfortunate that in accordance with EU procedures, the management of RCF2 as Budget Support Programme could not be entrusted to a private entity. With hindsight, it seems that a private party could also have managed such a facility efficiently; however, this would not have resulted in the indirect impact capacity building at IDC level described thereafter.

- EIB support

The EIB’s advisory and supervisory role was globally effective in helping to structure the RCF Programme and ensuring its rigorous implementation, building up IDC’s capacity in the process. It is regretted that it was not able despite its efforts i) to help improve the

Third Party channel process[3], to make it acceptable to commercial financial institutions through involvement with IDC higher management and ii) that it could not ensure, that a global portfolio review be conducted yearly to monitor more clearly and accurately the financial and socio economic results of the Facility.

- Deal flow

The Programme had to be extended by three years overall, due to the slow setting up of a number of agreements between the parties involved at the beginning of the Programme, as well as due to the slow deal flow.

The limited numbers of investees (however within target) supported is mostly due to cancellations and the unsuccessful Third Party channel process which did not meet the private financial sector's requirements for an effective cooperation, mostly linked to the burdensome investees' assessment process, IDC perception as a competitor, as well as some lack of interest on the part of the large banks for the limited amount of the Facility (this last argument would not apply to the smaller financial institutions which could have been approached further to the mid-term review recommendations). It is important to note that the issue of cancellations was to some extent outside the control of RCF. An analysis carried out by the EIB in February 2012[4] shows that before cancelations, performance of the fund channel by channel was on track.

The limited deal flow is also due to the competition from a number of other Funds developed by IDC over the last few years on a model similar to RCF, as far as the Direct channel is concerned.

Because of this slow deal flow, the Facility amount is still not fully committed (78%[5] committed as of end of June 2013) and the reflows have not been reinvested; neither RCF 1 nor RCF 2 are yet revolving.

- Leverage

The funds have been leveraged up to an excess of 300% from the initial expectation of 100%. In that respect, RCF was effectively catalytic towards the financial support granted

[3] During Q1/Q2 of 2008 the RCF SBU was actively involved in negotiating framework contracts with potential Third Party Channel (TPC) intermediaries. The EIB regularly provided its review, assessment and recommendations on the status of the discussions. The Bank has in the past promoted a deal-by-deal approach and has particularly encouraged a potential transaction with Business Partners, which unfortunately did not come to fruition. In line with the provisions of the Investment Guidelines, the EIB has then continued to provide its input in the advancement of the TPC, in particular in light of the expected restructuring of the TPC following MTR recommendations, when RCF engage negotiations with Khula regarding a potential co-operation.

[4] EIB presentation to Feb 2012 PSC

[5] 78% is based on the increased Fund size as compared to the 93% when considering the original Fund size estimate of R423 million. This was due in some cases to exchange rate fluctuations.

by IDCs to the investees as well as towards the niche funds developments through an increased visibility to raise other parties’ investments.

However, this leverage has been achieved mostly through other public funds, from IDC for Direct channel clients or from International Development Financial Institutions (IDFIs) co-investments as far as the Niche Funds are concerned. Once again, the absence of private financial leverage is the result of the failure of the Third Party channel (refer to our recommendations thereafter in this regard).

- Number of investees supported

The targeted number of clients effectively financed, as per the initial target may appear limited at 70. The evaluators, however, consider that the challenge was such that it was difficult to find capable HDP businessmen with minimum financial, management and technical capacity willing to engage in business development in the poorer areas of the country.

Most of the other IDC managed Funds similar to RCF but with different targets do not face such stringent conditionalities in respect of the potential beneficiaries[6].

- Business Support (BS)

An important component of the Programme was the associated Business Support grants to back up the investees. While this is considered as fully relevant and a significant feature of the Programme, it is regretted that this support was late to be organised and delivered, the investees’ BS needs being systematically assessed ex ante only from 2011, further to the mid-term evaluation recommendations. Progress remains to be achieved to ensure the effectiveness of the BS delivery and impact measurement. However, a survey conducted in 2013 concluded that BSS was achieving reasonably favourable results.

- Reliance on IDC support

RCF has been structured as an administrative team, which manages the RCF Programme ring fenced within IDC while its implementation as far as the Direct channel is concerned is in the hands of IDC various Sector Business Units (SBUs) and Departments. This does not allow the RCF team to have a front seat approach in dealing with the investees. However, this also allows the Programme to benefit from IDC expertise and capacity with regard to marketing, risk assessment, post investment monitoring or restructuring. The fact that RCF clients belong to the smaller segment of enterprises does not always attract the full attention of IDC departments. For example, IDC Post Investment Monitoring Department

[6] Not all other funds managed by IDC have BEE components, or minimum job creation or equity or quasi equity instruments while their cost is often lower: **https://www.thedti.gov.za/parliament/IDC-Incentives.pdf**

does not conduct a systematic annual review of all RCF clients; therefore there is no updated appreciation of the risks and value of the RCF “investments” as mentioned above.

The Niche Fund channel however is managed directly by the RCF team which relies on IDC expertise as far as participation to the Advisory Committees, Board or Credit Committees is concerned.

Overall the RCF organisational set up is deemed as satisfactory, providing the required expertise at a limited cost and allowing indirect benefits for IDC.

<u>- Financial instruments used and pricing</u>

While the project favoured equity or quasi equity financial instruments, the effective financial instruments used were mostly subordinated loans whose interest and principal repayments were linked to the availability of sufficient cash flow, both repayments being pushed back to the end of the loan duration should they not be able to be serviced. This in practice granted quasi equity support to the enterprise in as such that the repayment was in many cases pushed back to the end of the loan, pushing to the future the equity support issue i.e. the injection of sufficient capital to support the business expansion. This delays the need for real equity support to the end of the loan period, when one should have a better visibility of the “investees” future prospects.

Supporting the “investees” through real equity from the start could not be achieved since the shareholders’ ability was usually limited and RCF real equity support would have “crowded out” the promoter’s shareholding in the enterprise without bringing sufficient funding.

The initial pricing targeting an After Tax Internal Rate of Return (ATIRR) of 10%, calculated to achieve a nominal return of the facility amount was reduced, to the evaluators’ satisfaction, to a Gross IRR of 10%, made up of 50% upside usually based on a percentage of the turnover. The initial targeted return made it very difficult to finance a business with low equity over time.

<u>- Significant deal structure</u>

Two types of financing schemes are worth mentioning for contrasting purposes:

a) Workers’ Trust share financing, often for significant amount of equity, through long term loans to be repaid from “investees” dividend. The few cases assessed by the evaluators showed that the financing resulted in an excessive leverage, without any “real” BEE results, since the workers would not realise <u>in the best of cases</u> any income for the following ten or fifteen years. The real justification of the scheme was to create an excessive financial leverage without any HDP management effective commitments, devised by the promoters of the project to obtain unsustainable financial support.

The argument that the Workers would thereby be a party to the project is misleading, unconfirmed in practice; it would be better to provide the Workers' Trust with a share of the profits yearly, if any, as a simpler motivation instrument.

b) "Project finance" support on the other hand proved rather successful, whereby the financial and BS support was granted to new or small businesses on the strength of a significant contract gained from a large reputable client. This financing allowed the SME to gear up to service the contract, usually over a number of years, giving it time to build up its business model and develop other clients over time. This type of financing also benefited from the main contract assignment and implicit guarantee, limiting RCF risks to the investees' technical capacity to deliver.

It is recommended to review the effectiveness of Workers' Trust share financing schemes and build on the apparent favourable "project finance" processes (see our recommendations thereafter).

- Impact

- Direct impact

The evaluators confirm their good appreciation of the investment guidelines and of the various covenants defining the RCF SME targets. Most of the SMEs funded did effectively meet the Programme objectives and covenants, except for seven investees supported through the Agri-Vie Niche Fund (these investees are not counted in the RCF statistics, as they do not meet the BEE criteria). The Facility did play its catalytic role for most of the investees supported as well as for the Niche Funds capacity to raise investments, especially Utho Capital Infrastructure Fund, a 100% BEE managed fund (which might eventually need BSS support).

The direct impact is therefore achieved, subject to the above mentioned remark regretting that a more precise yearly assessment of the social and financial results is not systematically organised for the whole portfolio, which should also help to draw lessons.

- Indirect impact

The indirect impact linked to the Sector Budget Support Programme is real at the Government level, especially at the dti level through its involvement with the Programme as Chair of the Project Steering Committee.

The indirect impact is even more significant at the IDC level, whereby from a single RCF development facility ten years ago, the IDC now manages thirteen different Funds structured on the RCF model, managing ZAR 17 billion provided by IDC and other partners (as against about ZAR 500 million just for RCF2).

Furthermore, the IDC has taken the Business Service Support concept forward to assist all its clients, establishing its own fully fledged Business Support Department.

Finally, the support provided by EIB contributed to the set-up of RCF structure and operational process, building up the capacity of IDC in this respect. Their involvement all along the risk assessment process helped to improve the rigorous analysis of the operations.

- Lessons learnt

The main issue for this programme is the limited number (however within target) of enterprises effectively supported (78) over the Programme seven years mostly due to the failure of the Third Party channel having not allowed harnessing the financial power of the commercial financial institutions.

It is therefore recommended that IDC should address this major issue through the setting up of an ad hoc working group with the private financial institutions to devise ways to improve cooperation with its Development Funds Department, and in the future to include the private sector stakeholders early on in the design of similar Programmes.

A number of other lessons learnt have been identified. They are listed in the following table linked to the related issues.

Table 2: Lessons learnt

Key issues	Lessons learnt
Budget support versus Programme structure	- More time should be devoted to engage the National Treasury to increase their ownership of the Programme and draw lessons learnt - Positive role of the EIB as an advisor/supervisor which could eventually be provided by a number of other institutions to be selected through tender
Equity and quasi equity versus subordinated loans	- Development finance targeting small and medium size enterprises with high risk, a number of them at the start-up phase, cannot be effectively supported by equity or quasi equity instruments, unless having high growth potential
Leveraging private sector financing	- The private sector must be included during the design phase of the Programmes to ensure that they meet their requirements if their financial leverage is to be secured
Cooperating with other programmes	- Cooperation with other Programmes supporting SMEs should be formalised during the Programme preparation to ensure common interest and targets
Maintaining nominal value of	- Yearly in depth assessment of the investees should be undertaken to

the revolving Facility	ensure proper monitoring of the Programme, especially regarding the financial "balloon" made up of "late" principal and interest repayment
Effective socio economic impact	- Programme should ensure that real socio and economic performance is assessed, deriving the real impact of the Programme so as to draw effective lessons learnt
Delivery and impact of the Business Support Services	- Same comment as above to assess effective impact of the BSS and draw lessons learnt
Delays in the disbursement of the funds	- Coordination among stakeholders take always more time than foreseen, especially for a new venture; such memorandum of Agreement should be secured before the start of Programmes
Flexibility in the investment guidelines	- Guidelines should continue to include some area of flexibility especially for the non-core covenants defining the size of the beneficiaries/projects and expected results
Costs per job created	- Costs per job created should be computed to measure the results achieved and allow comparison with other Programmes with similar purposes
Third Party channel	- Third Party channel implied the cooperation of the private financial sector; that should have been involved from the design of the programme to ensure their expected participation
Characteristics of projects funded, Workers' Trust support and project finance	- Workers' Trust support in lieu of BEE shareholding seemed negatively linked to the projects' performance - Absence of real BEE shareholder cum management responsibility also appears detrimental to the performance of the investees - Importance of a partner with a sound knowledge of the processes in case of new developments - Effective financial support in the form of a project type financing linked to a significant contract from a reputable party appears promising
Exit strategies	- Exit strategies should be addressed at the credit application level, not only from the cash flow of the enterprises, but also from other exit options, should the cash flow not match the expected returns, so as to prepare the parties on other possible options
Catalytic impact	- RCF had a catalytic impact at two levels, i) at the end beneficiary level through allowing the IDC funding of the "investees" thanks to its "high risk" support, also comforting the three Niche Funds vis a vis other investors and ii) indirectly through the exceptional growth of specific IDC Facilities created along the RCF process model

- <u>Key recommendations</u>

Recommendations to the stakeholders
<u>European Commission</u> - Devote more time to ensure ownership of the Programme by the National Treasury and the Economic Development Department somehow disowned due to the perceived close involvement of the EU in the programme; - Enlist the cooperation of the dti and IDC to ensure some visibility of the RCF support towards the general public as well as would be black entrepreneurs. - In the future, institutionalise the role of outside advisor/supervisor for Programmes with high technical processes, especially in the financial sector, through competitive selection processes. - Ensure that key stakeholders especially from the private sector are involved in the design of any Programme targeting SME development.
<u>Government stakeholders</u> - The National Treasury and the dti should ensure that the real costs per job created for RCF and other Programmes with similar objectives are computed, monitored and compared to promote their effectiveness in the future; - In the future, ensure that all stakeholders are involved in the preparation of a Programme; in RCF case, commercial financial institutions should have been involved beforehand in the design of the Third Party channel process; - Due to the importance of harnessing the private sector in the BEE development effort, IDC, supported by the dti should form a working group to increase the outreach of the Facilities under its management through private financial institutions' involvement; - Consider inviting from time to time a private financial institution to participate in the Project Steering Committee meetings to try and garner synergy, trying to understand their requirements and getting them to know about the RCF; - Consider the inclusion of EDD as a member of the PSC due to the role that this Department now plays in SME policy development and since they are now IDC's parent ministry.

European Investment Bank - Because the EIB, Kreditanstalt für Wiederaufbau (KfW), Agence Française de Développement (AFD) and other Development Finance Institutions (DFIs) are providing a number of wholesale credit lines to refinance SMEs, they should try to link such credit facilities to the support of SME development (BEE SMEs in the RCF case) as planned through the Mutual Reliance Initiative signed recently between the EU and the EIB, the KfW and the AFD; - It is recommended that in future Programme support initiatives, EIB insists like for RCF on a more rigorous monitoring of the investees, regular analysis of the portfolio and the assessment of the Programme impacts to ensure that lessons are drawn and mistakes avoided.
Industrial Development Corporation - Create a working group with the main private commercial financial institutions to enlist their support for development finance; - In the future, commercial lenders should be associated with the design of the development facilities ex ante, especially with the identification of prospective targets (investment guidelines), decision process and co-financing implementation; - BSS should be made available not only to the beneficiaries but also to their main suppliers and out growers with the joint financial support from the IDC/DFD/RCF clients; it should also be made available to the Niche Funds themselves; - Subject to further study, a dedicated Management Support Department could be created within IDC, providing hands on management support to the impaired clients with a chance of redress and not to always rely on outside short term consultants; - Ensure that the IDC filing system allows consultation of the documents produced by the various IDC departments and SBUs by the RCF/DFD officers, easily; - Ensure that PIMD has the necessary manpower to review annually all IDC clients' performance, especially the RCF "investees" re the social and financial performance so that RCF has the information to conduct a global portfolio review based on these individual yearly assessments.
Development Funds Department/DFD/RCF team - A paradigm shift is required from investment management to portfolio management. - Formally nominate a head of the RCF facility itself with related task description to ensure

that somebody is officially in charge and responsible for the RCF activities and monitoring under the head of the Development Funds Department;

- Ensure the preparation of yearly work plans for RCF so as to have objectives against which to measure performance, assess deviation from the plan and suggest remedial actions. In such plans, SMEs could be categorised in line with the classification provided by the National Small Business Amendment Act of 2003 and 2004 (See Annex 7.1) thereby providing a further benchmark regarding the intended characteristics of the investees;

- Ensure that at least once a year, the global performance of the programme is assessed, completing a portfolio and global performance review and computing the real impact of the fund by assessing the socio economic results and potential value of the portfolio, having in mind especially 1- the important "balloon" represented by principal and interest repayments pushed back to the end of the facilities granted and 2- the concentration of jobs to be created and number of shareholders on a handful of "investees" and Workers' Trusts.

- Consider creating a special category within the on-track investees by differentiating those up-to-date as far as principal and interest payments are concerned and those which have delayed their repayment obligations until the end of the facilities;

- Consider providing RCF beneficiaries with some visibility signs and award documents which could help their visibility vis-á-vis their clients and bankers, promoting the EU support visibility at the same time as well as through mentioning the EU support in the Programme marketing and information documents;

- Ensure that lessons learnt are regrouped in RCF quarterly or annual reports, the more so that "lessons learnt" is a standard clause on the clients' write off reports. To regroup them in the reports would give them more pre-eminence;

- Consider supporting the adoption of BSS by the Niche Fund investees by providing interest free loans to finance the beneficiaries' 50% own contribution;

- Prepare exit scenarios well in advance, together with IDC Work out and Restructuring Department (WRD), for the clients showing an important financial burden due at the maturity of the RCF commitment, so as to prepare as much as possible for a solution that would allow the clients' survival;

- Organise a yearly conference with beneficiaries to draw lessons learnt, show off success stories and give visibility to the programme and its EU funding source towards would be beneficiaries, making increased use of the media;

- Ensure that the electronic filing system is improved to give easy access to the clients' basic documents that are the beneficiaries business plans and the Post Investment Monitoring Department (PIMD) or Work out and Restructuring Department (WRD) business reviews;

- Measure the total investment per job created as a complementary indicator of the capital intensity of the projects undertaken;

- Also compute the real costs (in term of concessionary interest rate and higher risk taken) per job created to allow comparison with other job creation focused programmes, eventually establishing a maximum limit in this regard, based on lessons learnt;

- Include catalytic role assessment of RCF proposed commitments in each credit application, to justify its mobilisation by IDC;

- Review the effectiveness of supporting Workers' Trusts for high percentage shareholding, without real BEE shareholders and BEE management in the projects funded;

- Liaise more regularly with other programmes supporting job creation and SME support, especially the programmes managed by Small Enterprise Development Agency (SEDA);

- With the support of IDC which might be interested for its other clients, liaise with large public corporations, to support BEE controlled enterprises which could benefit from suppliers' contract with the financial support of RCF/DFD/IDC (project finance support); this specific co-operation by state owned enterprises like Eskom or Transnet or others as well as private sector entities could be formalised into MOAs with IDC, possibly in cooperation with the SEDA Supplier Development Programme which has the same non-financial objectives.

- <u>RCF 2 Sustainability</u>

Within this South African context, and having in mind the challenging investment guidelines, the mission recommends that the RCF programme be continued as long as BEE special support is required, using the reflows to support the continuation of the facility.

Possibly, in view of the identified successes through “project” finance type of support, RCF may prioritise such an approach in its support to the BEE SMEs, developing its focus along lines similar to the proposed Value Chain approach detailed in Paragraph 6.2.2

- Possible future Small, Micro and Medium Enterprise (SMME) access to finance support in South Africa

During the course of the evaluation, the mission has identified some areas where support to SMME access to finance might be welcome, naturally subject to further in depth assessment and analysis, with the effective participation of all stakeholders in the identification, preparation and design of the support, especially the commercial financial institutions.

Based on a segmentation of the SMME market into i) high growth potential SMMEs, probably less than 1% of the market, but with significant impact in term of social, economic and financial development, ii) "lifestyle" SMMEs, the majority of the formal market segment, with low development prospects but high impact due to their large numbers and iii) the informal sector mostly made up of micro entrepreneurs.

- The high growth potential SMMEs segment

It is not recommended to support the high growth potential SMMEs through a specific Programme, since they are already supported by a lively Venture Capital industry and existing incubator programmes.

- The "lifestyle" SMEs segment

a) SME Credit Rating Scheme

Main drawback for such SMEs' access to finance rests with their lack of transparency, detrimental to the financial institutions ability to assess risk and therefore dispense with excessive collateral request. To improve such transparency, it is recommended to consider helping to provide a performance and credit rating service based on privately sourced due diligence review of SMEs which would outline the enterprises' strong and weak points, providing useful information not only to the enterprises' owner but mostly to the enterprises' bankers and other partners in the value chains. Similar scheme has been successfully developed in India by the National Small Industries Corporation[7] with the support of a number of private service providers in cooperation with the banks, having contracted more than 26,000 enterprises so far. As recommended above, such a scheme already under consideration by the dti must be assessed in full cooperation with the financial sector and credit rating providers.

Such financial, promotional and analytical support by the Development Partners could be coupled to Technical Assistance linked to the identified SMEs' weak points, including possible hands on monitoring/reporting by audit companies during the financial institution financing support.

[7] Cf. http://www.nsic.co.in/creditrating.asp

b) “Project finance” scheme

Based on the good success of “Project finance” type of support for SMEs benefiting from a significant contract from large and reputable clients as noticed from this RCF 2 final evaluation, it is suggested to study the provision of technical and financial support to new potential suppliers of large groups, duly identified in cooperation with these larger public and private enterprises.

The Small Enterprise Development Agency does manage such a scheme targeting quality, management and know how support for such potential large corporations’ new suppliers, however without the financial arm to support the investments usually required.

A Programme providing identification of potential SMEs in collaboration with the large enterprises, needs assessment, technical assistance support and financial provision could be devised with the strong involvement of the financial institutions and the large groups willing to participate in the Programme, the main support needed from the Development Partners being the grant support element to conduct the needs assessment as well as advisory on how to structure the project finance scheme on a wide scale involving both private and public institutions.

<u>- Micro entrepreneurs segment and Micro Financing Institutions (MFIs)</u>

a) MFI support

Developmental Micro Financial Institutions (MFIs) in South Africa are comparatively much weaker and less effective than in the rest of Africa. Even the International Finance Corporation (IFC) has been struggling to identify one such institution to be supported through an IFC equity investment. In view of the large number of unemployed in South Africa who most probably do have some sort of informal business activities, it is recommended to try and understand the reasons for such MFI weakness and address the issue.

b) Micro Entrepreneur formalisation

This last proposal concerns the segment of the informal market, generally considered as large but fully outside the structured framework and therefore not able to grow through the benefits from the official financial channels or others.

It is recommended, subject to the full backing from the Government at the highest level, in view of its dependence/reliance on several different governmental institutions, and to further studies, to design a very simple specific registration category for micro enterprises, with a maximum turnover (to limit undue competition with existing formal businesses), maximum three to five employees (on very simple employment contracts), and very limited and simple tax contribution, so that micro enterprises would be drawn into the formal sector, with the related benefits of being able to contract officially, to employ, to have bank accounts, to be eligible for social benefits etc. and therefore have a chance to grow.

Such a scheme would obviously not bring any significant increased fiscal income to the Government in the short term, but it will provide a way to encourage more formality and improve official employment.

Brazil has been developing such a scheme since 2009 with apparent success[8], with the registration of about 850,000 Individual Entrepreneurs by the end of 2010, according to the Ministry of Development, Industry and Foreign Trade, which is the Government agency responsible for implementation of the initiative.

[8] Cf. http://infosurhoy.com/en_GB/articles/saii/features/economy/2011/01/04/feature-03

1 INTRODUCTION

1.1 FINAL EVALUATION OBJECTIVES AND EXPECTED OUTPUTS

The overall objective of the final evaluation of the RCF 2 Programme is to provide decision-makers in the South African Government and the EC with a detailed assessment of the performance of the programme to date in terms of its relevance, efficiency and effectiveness, and with special attention to its impacts and prospects for sustainability.

The expected results and indicators defined in the Financing Agreement (and its Riders 1 and 2) should form the basis of measurement. However, important developments that have taken place during implementation will need to be taken into account. This will include the findings and recommendations of the mid-term review.

The specific objectives of the final evaluation are:

- Based on the design and evolution of the programme, to assess the relevance, efficiency, effectiveness and impact of programme implementation;
- To assess the sustainability of the programme;
- Provide clear key recommendations on potential future activities in the Private Sector in South Africa, especially in terms of improving access to finance for small, micro and medium enterprises (SMMEs), where there are market constraints and for which development funding could add value.

1.2 METHODOLOGY

The consultancy was made up of a team of two experts, a team leader with a finance background and a private sector development expert, with a strong knowledge of the country.

The final evaluation was based on a thorough understanding of the socio-economic context in South Africa and the legacy from the apartheid years. It takes into consideration the Government policy in this regard as far as SME support and employment is concerned as well as the EU response strategy at the time.

The mission has been divided in successive steps as follows:

- Inception phase

This in country phase which started on 16th September. It concentrated on the review of the relevant documents, initial meetings with the main Government stakeholders and understanding of the RCF organisation, management and governance within IDC, so as to reach a common approach within the evaluation team as well as with the EU and the authorities.

This Inception phase translated into an Inception report which outlined the mission’s proposed methodology and organisation.

- Field phase

The field phase was then divided into three main parts, from 23rd September until 25th October:

- The first part dealt with meeting the various parties to the programme, such as the RCF programme officers, the various IDC Units involved with the programme, a sample of investees including the three Niche Funds, as well as a review of the rejected applications (about 20 investees/applicants or 30 % of the portfolio) to understand RCF constraints in supporting some risky applications. The selection of investees/rejected applicants assessed took into consideration a spread of the sectors, regions, size of the investments as well as performance.
- The second part focused on the main external stakeholders supporting the programme such as the Project Steering Committee (PSC) members, the EIB and the other Government departments dealing with private sector support. The meetings with these entities not only focused on their role relative to RCF but also aimed at understanding their views regarding possible future avenues to support SME access to finance, and therefore employment in the years to come, within the Government strategy in this regard.
- The third part was more general, to allow the mission a good understanding of the SME finance environment in South Africa, with meetings with public and private finance institutions, as well as SME associations. Also, meetings were organised with other programmes supporting SME access to finance and job creation and the main Development Partners involved with private sector support to understand their respective approach to the issues and avoid overlap in the future.

- The EIB phase on 28th and 29th October:

By the end of October, two working days were spent with the EIB in Luxemburg to fully appreciate the EIB’s contribution to RCF, seen from their perspective.

These meetings focused on the EIB’s views of potential private sector financial support for the future, with or without their involvement.

- Final phase, from 4th November until 22nd November

Based on the above, and upon the return of the mission from Luxemburg, this draft report has been presented to the PSC members and other stakeholders in the form of a power point presentation.

The final report shall be prepared henceforth to integrate comments received from various parties.

- Limitations

In undertaking the evaluation, the team experienced some challenges mainly related to the availability of up to date information of the investees. The last comprehensive survey on the investees was done in 2010/11 and since then, IDC through the Post Investment Monitoring Department has not been able to visit all the investees. Therefore the data on development indicators does not reflect the current status but rather looks at the information collected during the 2010/11 survey and what was then supplied in the investment applications after this survey. Given the time allocated for this evaluation it was not possible to collect up to date statistics that would provide a good understanding of the progress made from the time when the investments were made. It is our view that information provided through the 2010/11 survey provides a good insight in overall progress made and has been used for the analysis in this report.

1.3 PROJECT BACKGROUND

1.3.1 The political, economic and social background

(For a detailed analysis of the political, social and economic situation in South Africa, please refer to Annex 7.1)

South Africa is a politically stable country of 51.8 million inhabitants with a non-racial democratic system. The country enjoys a multiparty political system, active opposition, a solid constitution and an independent judiciary.

Government integration through inter-ministerial committees results in different clusters which include the economic and employment cluster. This cluster deals with issues of Government's economic strategy, including issues relating to the second economy (the informal economy). The cluster's key objectives are:

- Sustainable economic growth;
- Job creation;
- Redistribution of income;

- Human Resource development and skills development;
- Competitiveness of the economy;
- Research and development;
- Spatial development;
- Stable financial system; and
- Economic Governance

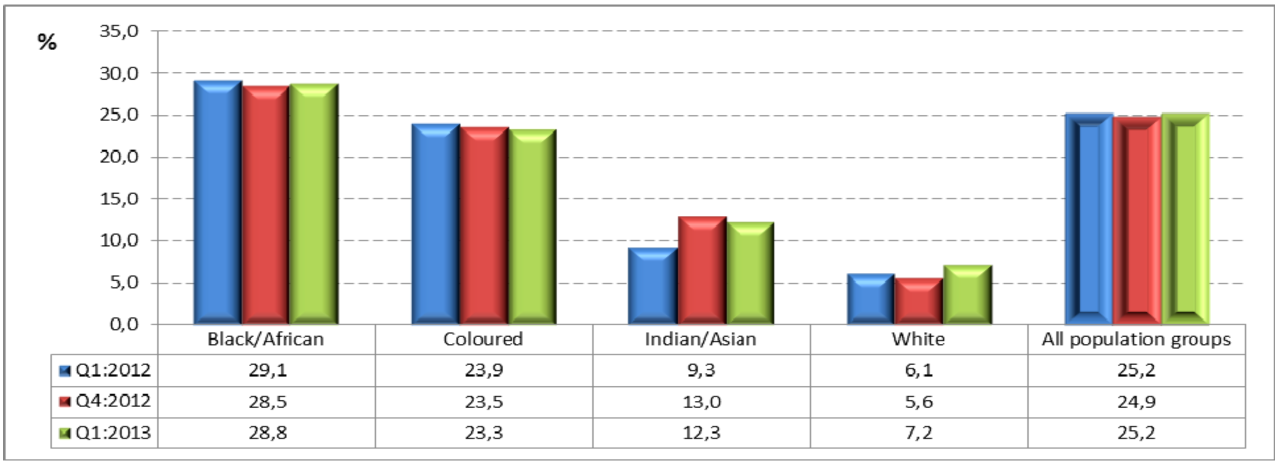
According to Stats SA[9], black Africans are in the majority at 79 % and females are slightly more than males by 4 %. The country has the largest and most diverse economy in the continent and until the global recession, South Africa has enjoyed positive economic growth for more than a decade.

Despite the apparent successes the Government still faces a plethora of challenges. South Africa remains a racially unequal and dual society with respect to wealth and income distribution. South Africa's Gini coefficient of 0.58, points to a significant social and economic divide between the first and second economy. The second economy contains millions of the very poorest — mostly black people, marginalised and unskilled, who take up informal activities simply to survive.

Further, unemployment rates in South Africa still remain unacceptably high. According to Stats SA Labour Force Survey; [10] the number of unemployed South Africans for the periods Q1: 2008 to Q1: 2013 averaged 4.3 million. Unemployment is highest among the black population at nearly 30 %. The unemployment rate for women remained higher than the national average between Q1: 2008 and Q2: 2013. Figure 1: Unemployment Rates in South Africa according to Race for the period 2012 to 2013.

[9] www.statsa.gov.za/publications/populationstats.asp
[10] Stats SA labour Force Survey

Figure 1: Unemployment Rates in South Africa according to Race



	Black/African	Coloured	Indian/Asian	White	All population groups
Q1:2012	29,1	23,9	9,3	6,1	25,2
Q4:2012	28,5	23,5	13,0	5,6	24,9
Q1:2013	28,8	23,3	12,3	7,2	25,2

Source: Stats SA website

1.3.2 The Broad-Based Black Empowerment Policy

After the country’s first democratic elections in 1994, the Government devised various policies which aimed at reducing the effects of apartheid, especially in terms of economic empowerment for HDPs.

Central to this, was the development of what is called the Preferential Procurement framework which facilitated the access by the HDP to Government tenders. Suppliers would be allotted points regarding the degree of compliance that they met and would thus be awarded Government contracts on this scale.

Further on, it was realised that this was not sufficient to redress the legacy of the apartheid years and a wider Broad-Based Black Economic Empowerment (B-BBEE) Act was devised to support the development of HDP controlled enterprises.

The B-BBEE act has evolved in order to include seven core elements which were aimed at broadening empowerment. These elements were:

- B-BBEE: Ownership: This is to the extent that the company has black shareholders.
- B-BBEE act: Management control: this was how much black people would have strategic and operation control in the company.
- B-BBEE: Employment equity: this is how many black people are employed in the company.
- B-BBEE: Preferential procurement: how the business will procure services and goods from black suppliers.
- B-BBEE act: Skills development: how the company is investing in skills training for black employees.

- B-BBEE: Enterprise development: how the company is assisting black business development in the country.
- B-BBEE act: Corporate investment: how the company is assisting black beneficiaries.

The focus of the B-BBEE is to favour companies with a high B-BBEE score through the Preferential Procurement Act. These companies themselves request their suppliers to be empowered to improve their own rating. Thus Broad-Based Empowerment is driven down the supply chain. Various other legislations support the BEE effort, including the Skills Development Act and Employment Equity Act.

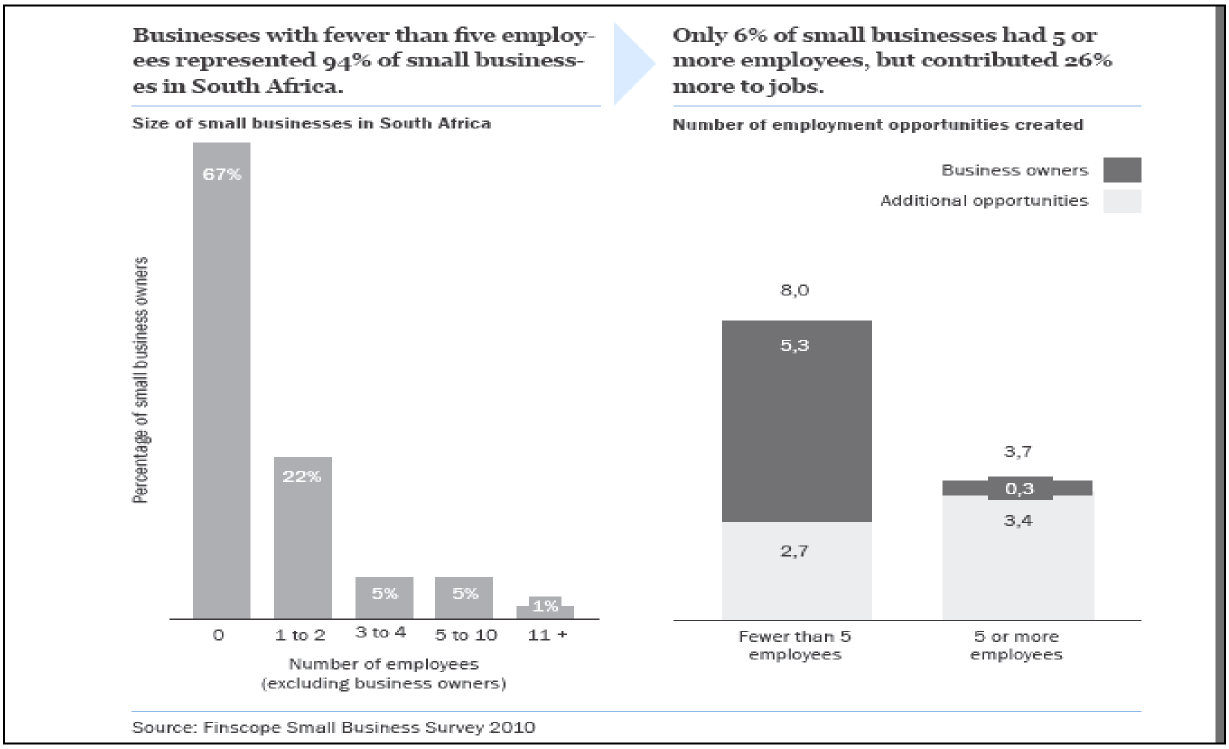
1.3.3 The SMME landscape in South Africa

The promotion of SMMEs is provided for under the White Paper on the Promotion of Small Business (1995) which sets out the Government’s policy on the development and promotion of small business in South Africa. This was followed by the National Small Business Enabling Act in 1996 which defined SMMEs and provides for the establishment of support institutions for SMMEs, the act was amended in 2003. The new Integrated Strategy on the promotion of Entrepreneurship and Small Enterprises is also a key strategic document which gives “renewed impetus”[11] to the small business sector and seeks to bring into life the Government’s policy of promoting small businesses.

The New Growth Path released in December 2010 by Ebrahim Patel, the Economic Development Minister, set job creation as a priority, with a target of creating five million additional jobs in the next ten years. It aims to reduce unemployment from 25 % to 15 %, largely through the development of small businesses. Further, in his 2011 State of the Nation address, President Zuma stated that “*the small business sector is a critical component of the job creation drive*”. Figure 2: SMMEs and Employment Creation, below shows the contribution of SMEs to employment figures in South Africa:

[11] dti: (2011) Rethinking Small Business Support in South Africa: Report on the Review of Government Support for Small Business

Figure 2: SMMEs and Employment Creation



However, according to the report on Evaluation of Budget Support in South Africa (2013) [12] there is no significant increase in the number of enterprises paying corporate income tax over this period, i.e. South Africa is not creating large numbers of micro, small and medium firms. For manufacturing the picture is similar – across all size segments there were fewer firms in 2010 than in 2007.

SMME financing faces a plethora of challenges, mainly related to policy, leadership and inadequate resources to name just a few. Box 1: SMME Challenges, below gives a brief description of these challenges:

Box 1: SMME Challenges

Challenge	Description
Lack of overall small business policy leadership	• Small business lacks a clear champion at the highest level of Government resulting in Government supported SMME agencies not being allocated sufficient resources to execute mandates.
Approach to policy Formulation	• The relationship between national and provincial Government is not as strong as it should be; • Perception that the national small business policy is really a Dti policy rather than a policy for the country as a whole; • Development of the 2005 Integrated Strategy was not as inclusive

[12] Evaluation of Budget Support in South Africa Draft Final Report 2013

	as the development of the 1995 white paper; and • South Africa has no clear goals for SMME development which sets measurable targets and milestones to be achieved
Role of provincial and local Government	• National SMME strategy does not give enough guidance to provinces and the roles are not clearly stated in the Act and in the 2005 SMME strategy
Unclear mandate of SMME institutions	• Scope of institutions such as SEDA need to be reviewed as it is felt that they are under on-going political pressure to extend their operations beyond what their resources and operational capacity can accommodate
Inadequate Resources	• Support institutions such as SEDA feel that their budgets are not commensurate with the mandates they are expected to fulfil for example its budget of ZAR 400 million since the institutions’ merger
Weak Coordination and integration of small business support	• Within small business development circles, the institutions are not very well coordinated
Weak monitoring and evaluation of small business support	• South Africa lacks an overarching framework for monitoring and evaluating the operations and impact of small business support institutions and programmes
Overlapping Institutional roles	• Having several institutions targeting the same market with largely similar offerings creates confusion .e.g. there is a role overlap between the small business activities of the National Empowerment Fund (NEF) and SEDA
Operations	• For example there are complaints that SEDA’s Board takes too long to make decisions that enable the organisation’s incubation programme to respond to open new incubators
Lack of SMME business data	• There are huge discrepancies in data statistics. For example the dti and Fins cope’s figures on small businesses vary significantly
Limited Use of Innovative SMME models	• Financial institutions can use alternative such as project financing, leasing and factoring
Underdevelopment of Microfinance Sector	• South Africa has an underdeveloped and undercapitalised microfinance industry which has failed to scale up to meet the needs of the SMME sector

Source: Rethinking Small Business Support in South Africa: Report on the Review of Government Support for Small Business (2011)

1.3.4 The Government’s Private sector support strategy

Core components of the Government's strategy include;

- To establish a one-stop shop and single funding agency for small and micro-business through the consolidation of Khula, South African Micro-Finance Apex Fund (SAMAF) and IDC funding, amongst others;
- To improve access and reduce the overhead costs of government in order to make more resources available to end-users;

- To fully implement Government's long-standing commitment to pay small business suppliers within 30 days, with clear consequences (fiscal penalties) for non-compliance by public entities;
- To integrate small and micro-enterprise support systematically into all sector strategies; this is critical to ensure a space for smaller enterprises in the value chains of major industries and to support the development of clusters and sectoral regulations and market institutions that meet the needs of smaller producers;
- To initiate a red-tape elimination campaign to simplify regulated procedures and forms and remove any bias against smaller producers, for instance in zoning requirements, with results reported to Cabinet on a quarterly basis;
- To strengthen access to micro-finance for small enterprises in order to bring more citizens into economic activities and thus widen the enterprise pool in the country as one key step to promote the growth of new enterprises; and
- To address smaller businesses' concerns about access to and the cost of space in shopping malls.

In order to achieve this, the Government has put into place several institutions that are meant to improve access to financing for SMMEs. Box 2: Funding Programmes for SMMEs shows some of the organisations that fund SMMEs in South Africa.

Box 2: Funding Programmes for SMMESs

Institution	**Target Area**	**Loan Facility**	**Services Offered**
National Empowerment Fund (NEF)	Broad Based Black Economic Empowerment	The NEF consists of four funding channels Imbewu Fund: ZAR 250 000-10 million Entrepreneurship Finance: Maximum ZAR 5 million Procurement Finance: ZAR 10 million Franchise Finance: ZAR 5 million	NEF is a driver and thought leader in promoting and facilitating black economic participation by providing financial and non-financial support to black empowered businesses and by promoting culture of savings and investment among black people
National Youth Development Agency	Youth Development Programmes	ZAR 1000-10million	Promotes youth development through guidance and support to initiatives across sectors of society and spheres of Government The NYDA's primary target group is young people aged between 14 and 35 years. The majority of beneficiaries should be from low-income households. Emphasis will also be placed on young persons with disabilities. NYDA Enterprise Finance aims to promote

			entrepreneurship among young people, so it
Small Enterprise Finance Agency (SEFA)	Lower end of SMMEs	The facilities range from a minimum of ZAR 50 000 to a maximum of ZAR 5 million	SEFA was established on 1st April 2012 as a result of the merger of the South African Micro Apex Fund, Khula Enterprises and the small business activities of IDC Delivering wholesale and direct lending; Providing credit guarantees to Small, Medium and Micro businesses; Supporting the institutional strengthening of Financial Intermediaries so that they can be effective in assisting SMMEs; Creating strategic partnerships with a range of institutions for sustainable SMMEs development and support; Monitoring the effectiveness and impact of financing, credit guarantee and capacity development activities; Developing (through partnerships) innovative finance products, tools and channels to catalyse increased market participation in the provision of affordable finance

1.3.5 SME financial support in South Africa

The South African Financial sector is characterised by a sound regulatory and legal framework. It boasts of both domestic and foreign banks/institutions. These banks/institutions provide a full range of services that are commercial, retail, merchant banking, mortgage lending plus insurance and investment. The banking system remains the main source of capital to start and grow businesses. The Finscope South Africa Small Business Survey[13] estimates that 47% of business owners are formally banked. In South Africa, large banks contribute 95 % of all lending to SMMEs[14] and according to the dti report entitled "Rethinking Small Business Support in South Africa; Report on the Review of Government Support for Small Business December 2011" commercial banks are less likely to finance informal micro and small enterprises and start-ups preferring instead to

[13] Finscope South Africa Small Business Survey (2010)
[14] World Bank: Bank Financing of SMMESs in five Sub-Saharan African countries; The Role of Competition, Innovation and the Government Policy Research Working Paper 6563

focus on formal SMMEs and established businesses. Suffice to say, Finscope estimates that 47 % of business owners are formally banked through commercial banks[15].

A comparative analysis of South Africa with other countries[16] will reveal that South Africa is lagging behind other countries with regards to SMME lending. Comparatively the study found out that banks in Kenya, Rwanda and even Tanzania seem to be more involved with SMMEs than banks in South Africa and Nigeria. An in-depth study of these best practices might benefit the SMMEs sector in South Africa. Further, the World Bank Africa Region Survey report mentioned above also points out that; the share of SMMEs lending in the overall loan portfolios of banks varies between 5 and 20 %. Table 3: SMME Lending Patterns in selected African countries below shows these trends.

Table 3: SMME Lending Patterns in selected African countries

Banks Involvement	**Kenya**	**Nigeria**	**Rwanda**	**South Africa**	**Tanzania**
SMMES's share of total bank lending	17.4%	5.0%	17.0%	8.0%	14.0%
Contribution of SMMEs to banks net income	20.5%	11.0%	20.0%	15.0%	16.0%
% of Revenues derived from					
Credit	68.0%	22.4%	71.0%	27.0%	73.0%
Deposit and Account Management	12.7%	53.2%	11.4%	50.0%	12.0%
Other transactions and fee based services	19.3%	24.4%	17.6%	23.0%	15.0%

Source: World Bank: Bank Financing of SMMESs in five Sub-Saharan African countries; The Role of Competition, Innovation and the Government Policy Research Working Paper 6563

1.3.6 The EC strategy in South Africa

South Africa and the European Commission (EC) consider themselves 'true strategic partners"[17]. Relationships between South Africa and the EC have grown since 1994 and were cemented through the signing of the Trade and Development Cooperation Agreement (TDCA) in 2004[18] The South Africa-European Union Strategic Partnership Joint Action Plan document notes that "A key element of the Strategic partnership is the common commitment to promoting an agenda of liberty, peace security and stability in the

[15] Quoted above
[16] World Bank: Bank Financing of SMMESs in five Sub-Saharan African countries; The Role of Competition, Innovation and the Government Policy Research Working Paper 656

[17] The South Africa-European Union Strategic Partnership Joint Action Plan
[18] The agreement was signed in 1998 but only entered into full force in 2004

world and in Africa in particular." Box 3: EC/SA Areas of Cooperation shows key areas of cooperation between the EU and South Africa that are outlined in the TDCA agreement.

Box 3: EC/SA Areas of Cooperation

Area of Cooperation	Key Elements
Development Cooperation	The real value added by ODA is not only finance itself but what comes from it, namely best practice, innovation, risk taking, pilot programmes, systems development, capacity building and skills knowledge; The Strategic Partnership will add value to the existing cooperation including the Joint Country Strategy, with a view to developing a stronger and sustainable cooperation; and The development of the second economy.
Trade and Investment	Both SA and EU are firmly committed to the development objectives of the Economic Partnership Agreements and the regional integration will foster sustainable development in the whole region
Science and Technology	The EU and SA agree to strengthen the existing Science and Technology policy dialogue between South Africa and the EU; Both parties are firmly committed to supporting African Science and Technology initiative including in areas of capacity building infrastructure development within the context of the African Union/NEPAD science and technology programmes, as well as those of the Africa, Caribbean Pacific Group of States.

The Joint Country Strategy Paper (CSP) covers cooperation between South Africa and the EU in the years from 2007 to 2013. It should be noted that the CSP was drawn up by South Africa, the European Commission and EU Member States and it fully takes into consideration the Trade, Development Cooperation Agreement (TDCA) between the EU and South Africa mentioned above. The CSP lays out some of the EU's cooperation agenda and South Africa's policy agenda. These are listed below:

- The political objective is to support and develop South Africa's political role as a stabilising factor in the region, continent and beyond;
- The economic and trade objective is to help South Africa play a crucial role in the integration of the region and be a trading partner in the globalised world economy, while expanding and liberalising mutual trade in goods, services and capital;
- The development objective is to reduce poverty and inequality in accordance with the Millennium Development Goals, promoting internal social stability as well as

environmental stability. This will focus on three main areas, each corresponding to one specific cooperation objective:

- Promote pro-poor, sustainable economic growth including the second economy i.e. economic growth that focuses on generating employment, reducing inequality, developing skills and tackling social exclusion.
- Improve the capacity and provision of basic services for the poor at provincial and municipal level and promote equitable access to social services. These services mainly relate to health, HIV/AIDS, education, housing, and the infrastructure to provide basics such as water, sanitation, access to sustainable energy services, waste management and communication; and
- Promote good governance. In the public domain the focus will be on fighting crime, including corruption and promoting safety, security and the rule of law. In the non-public domain the focus will be on strengthening civil society — especially NGOs, including social partners, and community-based organisations (CBOs).

1.3.7 The RCF1 lessons learnt

Experience from the RCF 1 programme has shown that:

- o *“Returns - As intervention in higher-risk situations is its purpose, its return requirements should reflect that risk. The returns targeted should not be lower than those targeted by co- investors bearing the same level of risk. It would also seem prudent that the RCF, as the equity investor, benefits from an appropriate level of up-side in its investments to compensate for the risk that it is taking”.*

This lesson learnt translated into a rather high After Tax Internal Rate of Return (ATIRR) objective for the fund at 10 %, which with hindsight had to be lowered down to a Gross IRR of 10 % made up of a 50% upside usually based on a percentage of turnover. This will be discussed further in Paragraph 3.2.7 thereafter.

- o *“Business Support - For many investees, professional assistance and a degree of training and mentoring remains essential to the profitability and sustainability of their enterprises. Provision of business support to the investee businesses could, where appropriate, be outsourced to specialists with a commercial and business operational background. The funding of such business support will be provided through low or interest-free loans with flexible repayment terms. The use of business support is to ensure the sustainability of the RCF investment whilst the use of a low or interest-free loan as its funding mechanism is to mitigate the financial stress on investees required to take up such business support”.*

This lesson learnt was duly integrated into RCF 2 through the provision by the Government of a Euro 5 million grant scheme to support BSS delivery. However, as shall be seen thereafter, its implementation was slow to start (Cf. Paragraph 3.2.5).

- *"Deal flow - In order to broaden its geographical and sectoral reach and further improve its deal flow, the Fund will benefit from co-investing with other (mostly smaller) Investment Funds active in different segments of the market. In addition, possibilities exist to look into cross-border activities, promoting South African investments in the small enterprise sector in neighbouring countries. Co-investments with other funds or financial institutions will be regulated by a process acceptable to all parties as set out in the Financing Agreement. In its investment guidelines specific detailed developmental targets will be set, including sectoral, environmental and geographical spread as well as gender-specific targets (in terms of jobs created, supervisory and managerial positions fulfilled etc.)".*

This lesson learnt was duly taken into consideration in the RCF 2 framework through required minimum investments in the rest of Africa or through the Niche Fund and Third Party channels. Results were not always in line with expectations as will be described hereafter.

- *"Performance Drivers - agreement on detailed performance drivers prior to launch of the programme will help the RCF-SBU to build the desired portfolio. These will be developed between dti, EIB and IDC on the basis of work done in the first phase and will take account of, inter alia, desired portfolio characteristics, investment to be made in partnership with non-IDC partners and funds to be raised externally".*

Investment guidelines, including specific requirements for each of the three channels did answer this lesson learnt. It did work, except for the Third Party channel.

1.4 RCF 2 PROJECT PRESENTATION AND DESCRIPTION

The Risk Capital Facility is a complex project structured as a Sector Budget Support Programme, however with most of the characteristics of a project.

It is to be implemented by the Industrial Investment Corporation (IDC) through a Project Monitoring Unit, the RCF 2.RCF 2 objectives and strategy

"The overall objective of the Programme is to contribute to the economic growth of South Africa and to promote the participation of Historically Disadvantaged People (HDP) in its economy.

More specifically, its programme purpose aims at job creation, through the provision of financial assistance in the form of equity and quasi-equity to small and medium *enterprises. It supports its investments by supplying low or interest-free loans to enable SMEs to acquire technical assistance and training"*[19].

The activities of the programme described in the Technical and Administrative Provisions annexed to the Financial Agreement are summarized as follows:

"The facility provides 'gap' finance to small enterprises that is not currently available to businesses with inherently high risk profiles. The high risk inherent to its clients will be managed through active monitoring by the implementing organisation and the provision of business support services as well as enhanced co-operation with other funding channels and use of their support networks".

RCF 2 is structured as a Sector Budget Programme based on a number of agreements among various parties described hereafter in Paragraph Project structure.

The main agreement is the Financing Agreement (FA) between the EC and the Republic of South Africa which defines:

- The nature and purpose of the operation;
- The EC contribution;
- The Beneficiary contribution and the administrative/financing conditions; and
- The operation modalities: expected results, main activities, indicators, lessons learnt, linkage with other operations, results of economic and cross-sectoral appraisals.

The agreement is foreseeing the project implementation:

- Central management will be used to allocate € 47 Million as sector budget support to the Government of South Africa in three tranches;
- The contracting authority is the National Authorising Officer (NAO);
- The PSC chaired by the dti, including members of key institutions, will provide for guidance to the project management;
- IDC will manage the RCF 2 on behalf of the Government and EIB will act as monitor and quality control organisation for the dti and EC;
- The programme, after rider 1 and 2 shall extend up to the end of 2018, the investment period covering the years from 2006 up to 2011, when the service contract with the EIB lapses. In fact, the investment period has been extended by a PSC recommendation

[19] Quoted from the RCF 2 Financial Agreement

up to the end of 2014, while the termination date was set at the end of 2018. In practice, the dti has the ability to modify the programme, being a Sector Budget Support Programme while the PSC is only an oversight and advisory committee.

1.4.2 Project structure

The RCF project is a complex project due to the number of parties involved in the delivery of the activities but also due to the number of different IDC departments concerned by the achievements of the results Cf**.** Annex 7.2, as well as due to the delivery of the Programme through three different channels.

Comprehensives guidelines defined the SME target to be supported, while a Business Support component was attached to the Programme.

For a detailed description of the Project structure, please refer to Annex 7.2.

1.4.3 The medium term review and ROM recommendations

The Medium term review (MTR) and the second monitoring mission (ROM) made a number of recommendations; some of them were implemented while others were discarded. This paragraph points out the outcome of the main recommendations from the MTR and ROM. The full review of the implementation of the recommendations can be found at Annex 7.5

- Main recommendations implemented:
  - The Programme has been further extended by two years;
  - With regards to BSS, it is now a requirement that independent mentors be appointed for each client where business support is provided. The mentors provide regular (monthly reporting) on the progress achieved by the clients. In addition, the Business Support Systems and procedures require that IDC Business Support professionals conduct BS due diligence (diagnosis) to develop Action Plans and implementation of the BS intervention to achieve the objectives as set out in the TORs.
  - The "rest of Africa" investments were not considered as feasible anymore;
  - Discussions were organised with Khula and thereafter with SEFA as well as with NEF and Business Partners (BP) to try and find some cooperation/financing arrangement under the Third Party channel; unfortunately the significant reorganisation which happened in the sector hampered progress to reach some agreement as far as Khula was concerned; cooperation with NEF was strong and numerous "investees" were both funded with RCF, IDC and NEF acting together; however, cooperation with Business Partners could not be organised due to the delays in approving a credit application on the part of RCF, this was unacceptable to BP.

- Niche funds are made aware of the importance of supporting investees with significant socio economic impact, however, a number of the investees, especially by Agri-Vie do not meet some of the BEE requirements[20];
- Documentation of lessons learnt are said to be organised in cooperation with the new IDC Knowledge Management Department through some interviews with RCF staff, however this is still work on progress. Lessons learnt are made available by this new Department through the IDC web portal.
- It is regretted that lessons learnt are not regrouped in RCF quarterly or annual reports, the more so that lessons learnt is a standard clause in the write off reports. To regroup them in the reports would give them more pre-eminence.

o Main recommendations not implemented:
  - Use RCF 1 and 2 reflows to ensure that the Funds are revolving; the fact that part of the RCF 1 reflows were assigned to another IDC managed fund (funded by dti) points to a relatively lower priority for BEE SMEs and HDP employment support, relative to the aims of the other funds managed by DFD as well as to the difficulties in identifying worthwhile BEE businesses, especially in the poorer regions of the country;
  - Empowerment of RCF account officers was not organised, especially with regard the Direct channel; preference was given to keep IDC sector units’ account officers in the front seat with regard to the relationship with the clients;
  - Preparing yearly work plans against which the activities of RCF could be benchmarked;
  - Monitoring the socio economic results and the financial results on a portfolio basis to draw lessons in this respect, including more detailed analysis of HIV/AIDS and environment plan existence, satisfaction of investees with RCF process, quality of jobs created directly and indirectly and impact of “investments” per size of SMEs;
  - Assessing rejected applications on a global basis to understand main issues in this respect. Although EIB encouraged such a review in the context of the 2nd amendment to the IDC-EIB Agreement in 2011.

2 RCF 2 RESULTS AND OUTPUTS

2.1 BUDGET SUPPORT CONDITIONALITIES FOR THE RELEASE OF THE THREE TRANCHES

Annex 7.4 outlines the general and special conditions for the release of the three fixed tranches, eventually modified by the two riders.

These conditions are a mixture of Budget Support conditionalities and project related covenants.

[20] Seven of these investees not meeting the Social economic results are not counted as part of the RCF investees in RCF reporting

Overall, the conditions were met for the release of the three tranches, taking into consideration the two riders extending the duration of the investment phase of RCF 2 by three years.

2.2 Performance indicators

- ➢ Key Performance Indicators as per the log frame

Key performance indicators (KPI) are detailed in the log frame document attached as Annex 7.8.

These KPIs have been slightly amended further to the two riders to the Financial Agreement, to define more precisely some of the covenants, without real changes in the requirements, such as insisting on HIV/AIDS prevention plans in each investee, or reflows achieving 100 % of the nominal amount after deduction of IDC management fees and actual or expected delinquencies.

Similarly, better defined expectations for training and associated financing were introduced, without changing the overall HDP development support philosophy.

The main modifications brought in by the Riders were:

- the adaptation of the investment target per annum as well as the expected HDP job creation per annum, to reflect the extended/revised investment period;
- increased flexibility in setting up the pricing of the facilities;
- a compulsory BSS needs assessment prior to any investment, such assessment being part of the application process.

- ➢ Key Performance Indicators relevance

As per the Financing Agreement, RCF 2 was designed to support through equity and quasi equity minority investment the empowerment of 1- Historically Disadvantaged Persons (HDP’s) through 2- BEE controlled (minimum 25 %) 3- SME support.

This translated into seven anticipated results and their related indicators:

- Approximately 70 SME’s should be funded from the € 47 million grant through investments as equity or quasi-equity. Simultaneously the investees would benefit from a business service programme funded by a € 5 million grant from IDC;

- The RCF Programme should create 6000 new employment of which 30 % are to be held by women. These jobs should be created for HDPs;

- RCF 2 should be revolving and sustainable;

- The investee should increase HDP empowerment through shareholding and possible access to management positions but also will have to achieve a 25 % HDP ownership within one year from investment;

- Access and use of BSS should be implemented to improve effective assistance to SME’s whatever the nature of support is needed as training, technical assistance and monitoring;

- Environment and anti HIV activities will be actively encouraged. Investees shall set up an environment and HIV/AIDS protection plan;

- Fifteen investments shall involve SMEs active in the rest of Africa, to provide a minimum of 500 HDP jobs.

These KPI appear reasonable and well adapted to measure the results from the programme, except for the last one which could not be met as seen thereafter. The main issue would concern the methodology to collect and monitor these results, not only relying on investees or Niche Funds own reporting. In practice, the collection of the results is supervised by the Post Investment Monitoring Department, which unfortunately does not provide systematic yearly reporting for each investee.

A secondary remark concerns the measuring of the investment per job created which should have also measured the total project investment per job created and not only refer to the RCF commitments; in the same token, the measurement of the real cost of the concessionary funding provided should have been measured per job created so as to allow comparison with other programmes in terms of cost per job created.

➢ Other covenants introduced through the Annex A Investment Guidelines of the EIB Agreement with IDC

The Investment Guidelines include the indicators listed in the FA as well as complementary indicators to define the “economic environment”: what is an SME, what is the Black Economic Empowerment (BEE), what is the Broad Based Black Economic Empowerment (B-BBEE) framework and what is the investment strategy and target of the Facility such as the participation of females in SMEs, what shall be the maximum/minimum investments (modified as per Rider 2), cost per job created, regional spread per sector and per region.

Additionally, the following guidance forms part of the covenants mentioned in the EIB Agreement with IDC:

o All funds will be made available to Black Economic Empowerment SMEs;

- o Investment channels: Direct Investment Channel should not exceed 60 % of the portfolio by value; a combination of the Niche Fund Channel and the Third Party Channel should together constitute a minimum of 40% of the portfolio by value; and
- o Average ZAR investment required per HDP job created at maximum ZAR 60,000 in terms of local RCF invested amount as measured on a portfolio basis, while the cost per HDP job per SME investee shall not exceed ZAR 300 000,000 in terms of local RCF invested amount.

These covenants are complementary to the seven original indicators mentioned in the FA and are defining how the EC objectives have to be reached. These shall not be considered as performance indicators, but rather as providing a clear definition of some of the terms in the Financial Agreement.

The EIB and RCF are checking systematically that 100 % of the FA indicators as well as the indicators defined in the guidelines are met for each proposed investment.

2.3 RCF 2 results with regard project objectives (results 1 – 7) and its outputs (including rider 1 & 2 modifications)

It is difficult to draw significant lessons from RCF 1 at present since a number of the clients have drifted away from IDC and their fate cannot easily be reviewed; Annex 7.4 gives a brief outline of RCF 1 portfolio at present with some lessons to be learnt, such as a thorough pre-investment due diligence on the investees' management capacity and their access to markets, duly supported by BSS and close post investment monitoring.

The results presented are based on reports and data provided by the IDC. It should be pointed out that the last comprehensive client survey was the 2010/2011 RCF Client Assessments concluded in May 2011 and since then, the IDC does not have an up to date status report on the developmental indicators for all the clients.

2.3.1 Result 1: Number of SMEs supported

Under this Result Area, RCF 2 intended to support a total of 70 SMEs through its three investment channels. Since its inception, RCF has supported a total of 78 investees[21]. This total figure excludes the 3 active niche funds as well as the one that was exited.

RCF 2 currently has a total of 63 active SMEs in its portfolio which are supported through the Direct Investment Channel and the Niche Fund Channel (clients that are RCF compliant) as at the end of June 2013.

[21] Source: RCF 2 Portfolio Data – The 78 investees includes, currently 53 active investees in the Direct Channel, the 10 RCF compliant investees in the Niche Funds, 13 write offs as well as 2 exits

Under the Direct Investment Channel, RCF 2 has supported 53 active SMEs to the total value of ZAR261, 700, 737. Ten investments that are fully compliant with the RCF criteria, to the total value of ZAR21, 774, 738 (RCF funded portion), have been made by the Niche Funds[22]. Table 4: shows that the majority of instruments used were subordinated loans.

Table 4: Number of SMEs financed net of cancellations and the amounts invested per annum up to June 2013 (Niche Funds and Direct Channel)

Year	Number of Approvals	Value (ZAR)	Investment Instruments used
2007-2009	39	248 341 475	Subordinated Loans, Preference Shares and Ordinary Share and Shareholders Loan and Shareholders Loan and Equity.
2010	3	43 186 499	Subordinated Loans, Preference Shares.
2011	13	16 328 763	Subordinated Loans and Preference Shares.
2012	17	95 183 000	Subordinated Loans and 2 Preference Shares.
2013 (up to June)	3	(7 989 000)	Subordinated loans
Total	75[23]	393 000 737	Combined Direct Channel and Niche Fund Channel

Source: IDC Annual Implementation Reports, IDC Quarterly Reports

Table 5 below, shows the number of Niche Fund Channel approvals.

Table 5: Number of Approvals and amounts in the Niche Fund Channel per year as at end of June 2013

Year	Number of Approvals	Niche Fund	Value ZAR	End investment approvals	Value ZAR
2007	-				
2008	2	Agri-vie	45 000 000	6	13 859 003
		Phoenix Recovery Fund*	20 000 000	N/A	N/A
2009	1	Evolution One	30 000 000	7	15 127 056
2010	1	Utho Infrastructure	30 000 000	4	9 965 682
TOTAL			**125 000 000**		**38 9510 741**

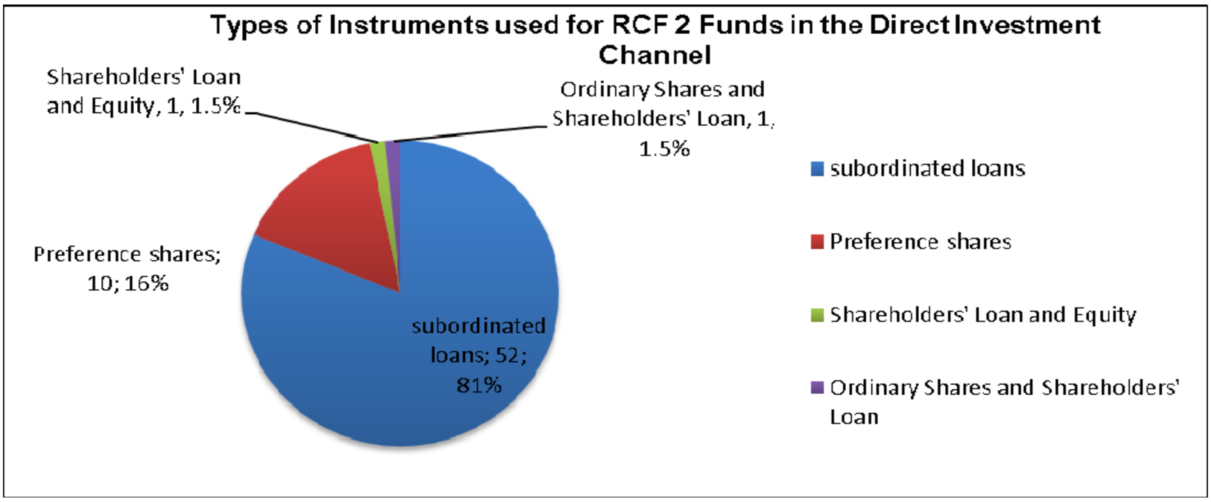
* has since been cancelled

[22] August 2013, IDC Quarterly Report 2013
[23] This figure is different from the data in the RCF 2 Portfolio data. Evaluators were not able to obtain clarity on the reason for the difference

Source: IDC Annual Implementation Reports, IDC Quarterly Reports

Under the Direct Channel, subordinated loans constituted 81 % of the deals concluded followed by preference shares at 16 % and 3 % as shareholder loan or equity. Figure 3: shows the different types of instruments that were used in the Direct Investment Channel.

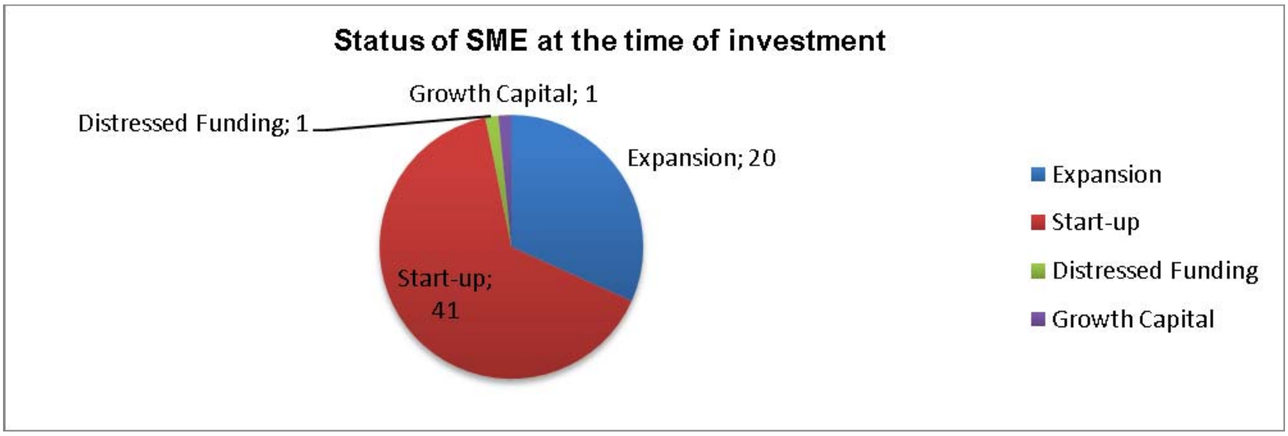
Figure 3: The type of instruments used for RCF 2 in the Direct Channel



Source: IDC Annual Implementation Reports, IDC Quarterly Reports

It emerged from the Desktop Review that businesses seek funding from Development Financial Institutions (DFIs) such as IDC, SEFA and NEF at the start-up phase due to the fact that South African commercial banks consider SMEs as high risk investments. As a result, out of the 63 active RCF 2 investees, 41 were start-ups, Figure 4: highlights this scenario.

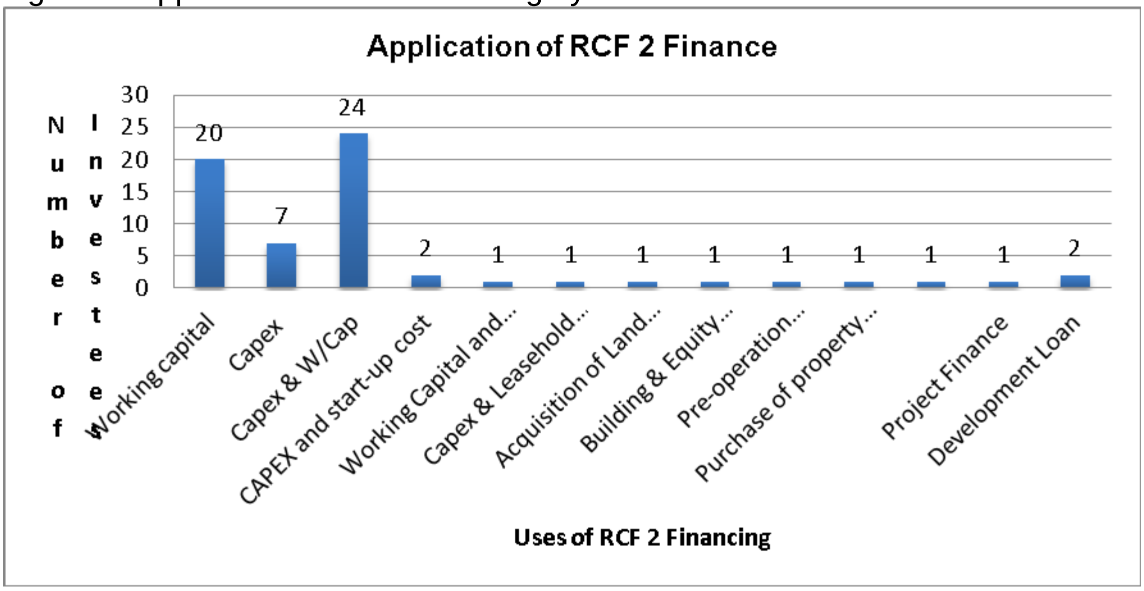
Figure 4: Status at the time of investment



Source: RCF 2 Portfolio data

The high number of start-ups have contributed to the extensive use of RCF 2 funding by clients for either working capital, capital expenditure or a combination of the two because businesses at this stage require this type of assistance while they establish themselves. Figure 5: shows that the highest numbers of applications were for Capex and or Working Capital. Applications for infrastructural development such as acquisition of land, building and equity, purchase of property did not seem to feature much.

Figure 5: Application of RCF 2 funding by clients



Source: RCF 2 Portfolio Data

At the time of the MTR, it was noted that no investment had been realised under the Third Party Channel, this situation has not changed. The Risk Facility was marketed to 16 institutions but this did not succeed as they were reluctant to engage with the IDC[24]. Some

[24] 2007 IDC Annual Implementation Report

institutions (ABSA, Nedbank, Standard Bank, NEF and Ithala) initially showed interest but not much progress was made as they saw the IDC as a competitor and the Programme as an administratively slow and cumbersome process for a small complementary funding. Another major issue was the reluctance of the institutions to have an audit conducted on them by the IDC.

Table 6: Number of active SMEs supported per sector, and amount committed as at end of June 2013, shows that the agribusiness sector attracted a significant share of the RCF 2 funds. This concentration was in line with the objectives of the Fund as agriculture is one of the priority sectors. The sector had 21% of the approvals in number, their value accounted for 39% of the RCF 2 funds. It is important to note that this figure dropped from 50% in August 2009 at the time of the MTR. Despite this concentration, the sectors covered in the portfolio are fairly diversified.

Table 6: Number of active SMEs supported per sector, and amount committed as at end of June 2013

Sectors	Number	Amount Committed (ZAR)	Average amount per investee (ZAR)	Percentage
2010 & Construction	5	18 580 682	3 716 136	7%
Agro Industries	13	110 672 974	8 513 306	39%
Chemicals	13	42 349 758	3 257 674	15%
Franchising	4	5 100 000	1 275 000	2%
Forestry and Wood Products	3	9 300 000	3 100 000	3%
Green Industries	6	19 369 056	3 228 176	7%
ICT	1	1 237 005	1 237 005	1%
Media	2	25 880 000	12 940 000	9%
Metals	11	37 785 000	3 435 000	13%
Textiles	3	6 701 000	2 233 667	2%
Transport	2	6 500 000	3 250 000	2%
TOTAL	**63**	**283 475 475**		**100%**

Source: RCF 2 Portfolio Data

However, it is worth noting that there have been no investments in Tourism, Mining and Mineral Beneficiation as well as Healthcare sectors. RCF continues to market the fund to these SBUs[25].

The programme had a geographical spread target of 65% investees (either in value or in nominal terms) outside the Gauteng and Western Cape Provinces. In the Direct and Niche

[25] August 2013, IDC Quarterly Report 2013

Fund Channels, this figure stands at 42% and 40% respectively in nominal terms. In terms of value, the respective geographical spread for the Direct Channel and the Niche Funds are 39% and 27% which is far off the mark.

Currently, the overall geographical spread figure is 58.7% in nominal terms and 45% in value terms. The fund had investments in all the nine provinces of the country as shown in Table 7: Number of active SMEs supported and amounts per Province as at end of June 2013.

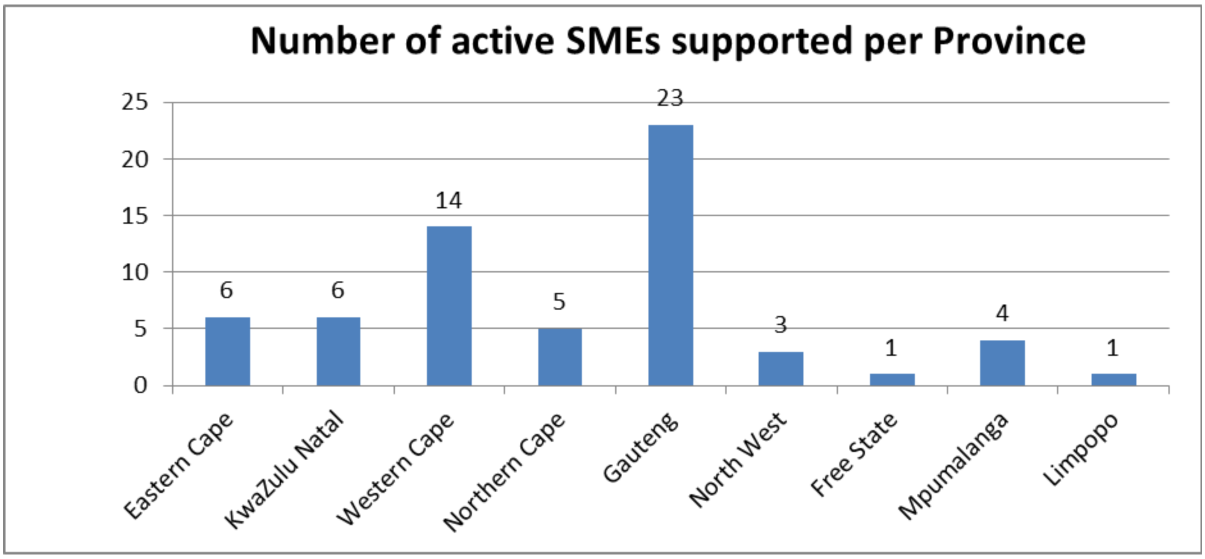
Table 7: Number of active SMEs supported and amounts per Province as at end of June 2013

Provinces	Number	Amount (ZAR)
Eastern Cape	6	40 227 074
KwaZulu Natal	6	14 918 000
Western Cape	14	46 265 244
Northern Cape	5	45 089 302
Gauteng	23	110 552 423
North West	3	5 981 092
Free State	1	8 642 340
Mpumalanga	4	9 800 000
Limpopo	1	2 000 000
TOTAL	**63**	**283 475 475**

Source: RCF 2 Portfolio Data

Figure 6: Number of active SMEs supported per province as end of June 2013 shows investee spread across the provinces. The investment in poorer provinces was mainly driven by corporates or well established business entities such as franchisees like Pick'n Pay as opposed to individual entrepreneurs, which is indicative of the brain drain to more economically active provinces.

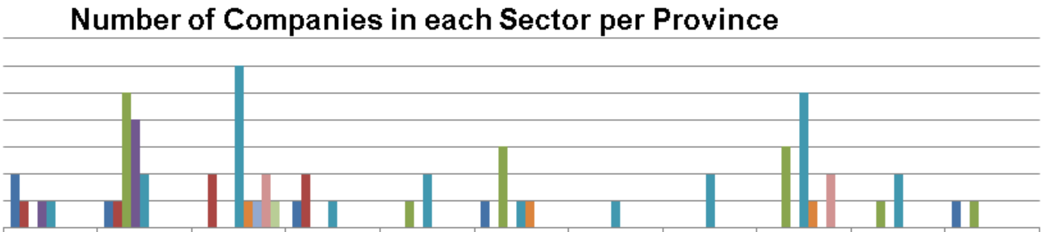
Figure 6: Number of active SMEs supported per province as end of June 2013



Source: RCF 2 Portfolio Data

The sectoral analysis of clients funded per province reveals that the chemicals sector is the most dominant as there are investees in 6 of the 9 provinces except Eastern, Western and the Northern Cape. Figure 6: Number of SMEs supported in each sector per province as end of June 2013 also indicates the Agro industries sector to be the next best represented as it appears in 5 out of 9 provinces.

Figure 6: Number of SMEs supported in each sector per province as end of June 2013



	2010 & Construction	Agro Industries	Chemicals	Franchising	Forestry and Wood Products	Green Industries	ICT	Media	Metals	Textiles	Transport
Eastern Cape	2	1		1		1					1
KwaZulu Natal	1	1	2	2							
Western Cape		5			1	3			3	1	1
Northern Cape	1	4									
Gauteng	1	2	6	1	2	1	1	2	5	2	
North West			1			1			1		
Free State			1								
Mpumalanga			2						2		
Limpopo			1								

Source: RCF 2 Portfolio Data

In order to understand the performance of RCF 2, there is a need to consider the statistics on rejections, cancellations, write offs and success stories.

➢ Rejections

There have been twenty six (26) rejections in total and a majority of these were due to the following reasons:

- RCF pricing impeded the viability of the transaction – 27%;
- Failure to submit information needed – 30%; and
- Failure to align to the objectives of RCF – 30%.

➢ Cancellations

There have been fifteen (15) cancellations, (7 full cancellations, 6 partial, 1 Niche Fund and 1 Niche Fund end investment). The reasons behind the full cancellations is that potential investees were subsequently offered better rates from commercial banks especially on the debt side[26] or in some instances they failed to meet the conditions precedent. Partial cancellations arose from the fact that initially applicants sought funding

[26] Discussions with the RCF Unit at the IDC

for more than one project and ended up dropping some of the projects due to changes in the market conditions.

- Write offs

There was a total of thirteen (13) write offs, out of which nine (9) were in the franchise sector. The reason for the write offs was given as poor market performance in the 2010 Annual Monitoring Report[27]. This also is the case with write offs that occurred after 2010. Thirteen write offs appears high as a percentage of the total approvals (20 %), however, the value of the write offs which is ZAR 22, 300, 000 is low (6 %) when compared to the total fund size. One single investment, Ellen Arthur SA (Pty) Ltd accounted for ZAR 11, 000, 000 meaning the other 12 write offs were on average ZAR 941, 667 each.

- Investments on track

Thirty seven (37) out of the sixty three (63) active clients are on track. This represents 59% of the investees. It is important to note that all ten (10) investments in the Niche Funds are on track.

2.3.2 Result 2: Number of new jobs created

The fundamental objective of the RCF Programme was to support the creation of 6,000 jobs for HDPs. The fund also required that jobs created through the Direct Investment Channel be at a RCF “investment” per job not exceeding ZAR 100,000 on a deal by deal basis and ZAR 60,000 on a portfolio basis.

RCF2 is estimated to have facilitated the creation of 6369 jobs in total. For the Direct Channel the Fund has created 5840 jobs which translates to an RCF “investment” of R49, 315 per job created. This is clearly within the targeted RCF “investment” per job of R60, 000[28]. These figures are based on forecasts from the IDC and the actual number could be more or less. Table 8: RCF 2 number of jobs created in the Direct Channel as at end of June 2013 shows that the highest number of jobs were created in 2007.Out of the total number of jobs created, 71% are accounted for by 21 investees, while 53% are from 12 investees and of these 3 are reported to be experiencing challenges or are not on “track”, 31% of the jobs created are from 4 investees that are in the agro industry. These statistics highlight the concentration risk of the portfolio and this means that if any of the major contributors to job creation were to go down, this would have a major impact on the achievement of the development indicator targets.

[27] 2010/2011 RCF Client Assessments
[28] August 2013 Quarterly Report

Table 8: RCF 2 number of jobs created in Direct Channel as at end of June 2013

Year	Number of jobs created net cancellations	Percentage held by women	RCF "investment" per Job (ZAR)
2007	1797	35%	31, 315
2008	931	45%	33, 415
2009	932	78%	51, 444
2010	472	37%	45, 523
2011	863	33%	45, 765
2012	1190	45%	72, 714
2013 (up to June)	-345	77%	64, 144
TOTAL	5840	43%	49, 315

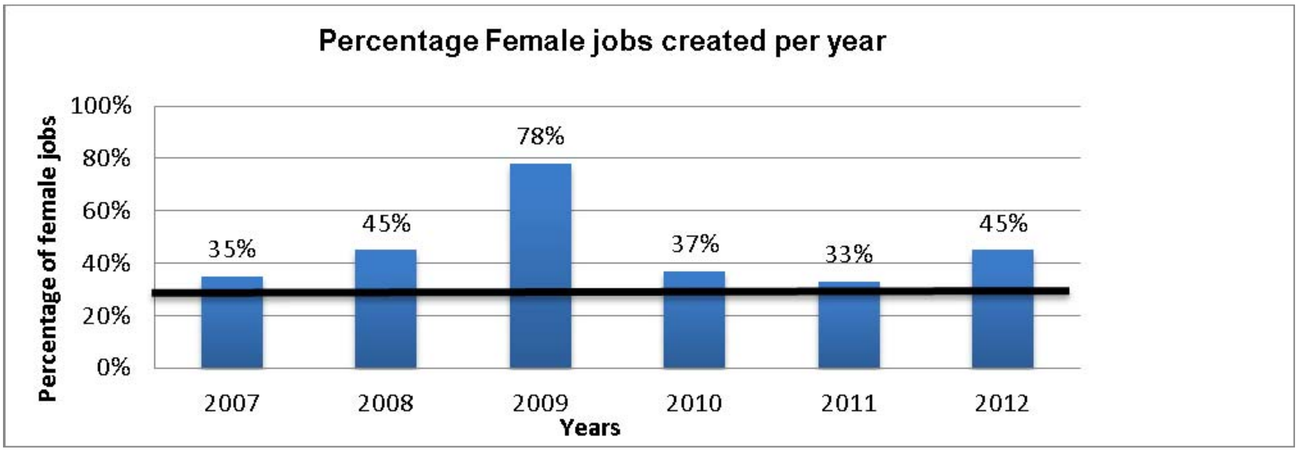
Source: RCF 2 Portfolio Data and IDC Annual implementation Reports 2007-2012

The figures achieved between 2007 and 2011 indicate that RCF was creating a sufficient number of jobs compared to the targets. The high RCF "investment" per job figure in 2012 is influenced by the high amount invested during that year.

The quarter ending in June 2013 had some corrections from investments made by the Niche Funds which led to adjustments in the number of new jobs created. The net figure taking into account the cancellations and the adjustments was -345.

From the total number of jobs created, RCF 2 required that at least 30% should be females. Figure 7: Performance of RCF 2 with regards Female HDP empowerment per year clearly indicates that RCF 2 achieved this target every year from 2007 to 2012, it is estimated that HDP women employment is at about 43% of the entire portfolio, which is a significant achievement.

Figure 7: Performance of RCF 2 with regards Female HDP empowerment per year



Source: RCF 2 Portfolio Data

2.3.3 Result 3: A revolving self-sustainable Fund is established

Under this result area, the objective was to ensure that a revolving self-sustainable fund is established.

Table 9: RCF 2 Portfolio as end of August 2013: RCF2 Portfolio as end of August 2013 below, shows the overall picture of RCF 2's portfolio and shows its revolving and self-sustainability capacity. However, up to now, the reflows have not been reinvested by RCF 1 or 2 since the full available amount has not yet been fully committed.

Table 9: RCF 2 Portfolio as end of August 2013

DIRECT CHANNEL	PORTFOLIO
N° of transactions approved (net of cancellation)	68
Value of approval (net of cancellation)	ZAR 288 000 737
Cost per job	ZAR 49 315
Average deal size	ZAR 4 235 304
Total value of investment facilitated	ZAR 1 406 173 434
Cancellations	7
NICHE FUND CHANNEL	
N° of approvals (net of cancellations)	3
Value of approvals (net of cancellations)	ZAR 105 000 000
TOTAL COMMITTED	**ZAR 413 000 737**
Disbursements	ZAR 308 142 238
Reflows	ZAR 30 295 705
Impairments	ZAR 40 904 609
Expected return	5.4%

Source: RCF 2 Portfolio data

RCF 2 had an objective to maintain its nominal value over time, i.e. a nominal Internal Rate of Return (IRR) of zero % post bad debts and fund management fees. The nominal IRR calculated on the current portfolio indicates a return of ca. 5.4% excluding upside, according to RCF. This IRR is only based on historical investments and excludes uncommitted funds[29]. The 5.4% expected return includes bullet repayments from investees which the IDC may or may not receive meaning the real value of the amounts to be received could be lower[30]. The reflows amount to R30, 295,705.

Table 10: Status of active RCF 2 clients Status of active RCF 2 clients shows that a majority of these (62%) of these are on track with their commitments. Only 8% of the clients are under legal action and one client has ceased operations. All the Niche Fund

[29] August 2013 Quarterly Report
[30] Further comments on this issue in next Chapter

clients are on-track and they are included in the total of thirty nine (39) investees. IDC defines investments to be on track when there are no defaults on payments, however, it is important to be more specific on this definition and refine it further to describe the different status of the investments that are on track (principal and interest paid regularly or pushed back to the facility maturity).

Table 10: Status of active RCF 2 clients

Status of clients	Number of clients	Investment Instruments
Under supervision	16	Subordinated Loans
Legal action	5	Subordinated Loans
On-track	39	**21** Subordinated Loans, **6** Preference Shares, **1** Redeemable Preference Share, **1** Shares and SHL, **6** Equity and SHL, **1** Loan/Profit Share, **1** Quasi Equity Loan, **1** Equity and **1** Shareholder’s Loan + Equity
Ceased operations	1	Redeemable Preference Shares
Liquidation	2	Subordinated Loans

Source: RCF 2 Portfolio Data

Despite, the difficulties experienced by some clients, RCF 2 appears well placed to be a self-sustainable fund barring any further cancellations, write offs or impairments. The reflows are expected to increase going forward and this should allow the objective of RCF 2 becoming a revolving fund, subject to some further analysis of the “balloon”[31] repayment (Cf. Paragraph 3.5.2).

2.3.4 Result 4: Increased HDP empowerment

The target for RCF 2 in this result area was for increased HDP empowerment to reach 25 %+ 1 in terms of SME ownership. Alternatively, an acceptable plan was to be put in place to achieve the required shareholding within one year post the approval of the investment. Fifty nine of the approved investments satisfied this requirement. The remaining four investees are expected to reach 25% or 25.1% in due course.

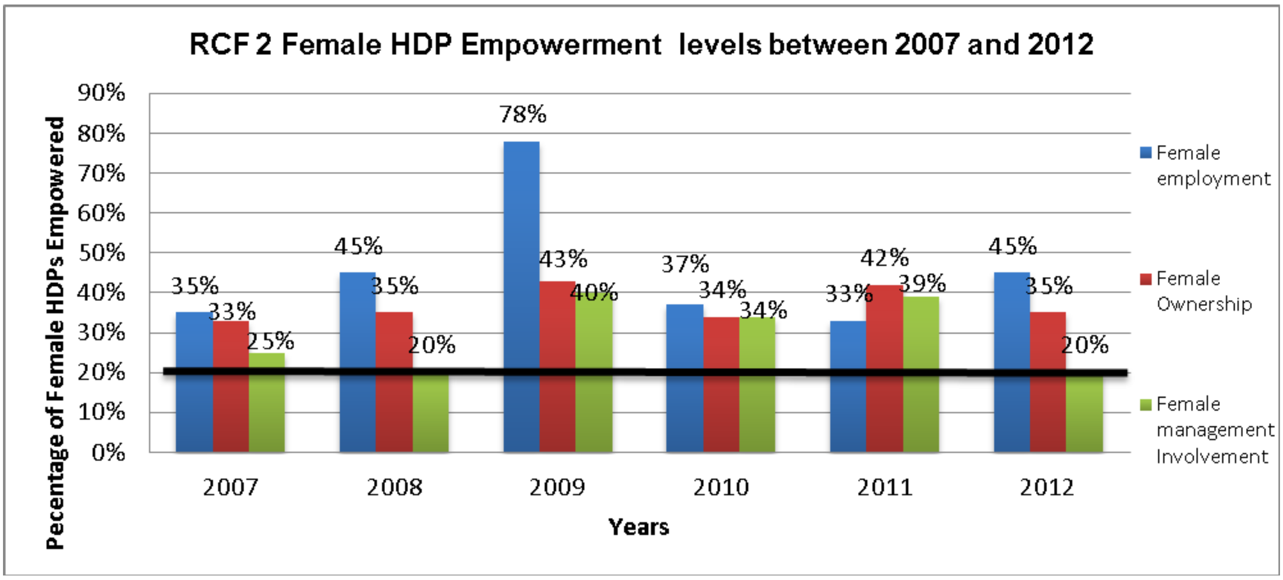
Twenty two out of the sixty three approved investments are 100% HDP owned with fifteen being more than 50% HDP owned. The expected average HDP holding for the portfolio is 57% with minimum HDP shareholding of 25%.

Cases where investees were unable to reach the prescribed RCF 2 quotas were mainly due to poor performance or the business had not yet reached its full operational potential.

[31] «Balloon » means the accumulated principal and interest repayments due by the RCF « investees » which could not be paid when due because of insufficient cash flow and are pushed back to the end of the RCF loan duration

RCF 2 was mandated to ensure that at least 30% of all jobs created, new shareholders, managers and business support recipients would be black women. These performance indicators relating to female HDPs were introduced for RCF 2 in support of the Government’s emphasis on ensuring that measures fostering black economic empowerment have positive impacts on all previously disenfranchised groups and layers of society, especially women. However, female involvement in management is still relatively low compared to female employment or ownership as shown in Figure 8: Performance of RCF 2 with regards Female HDP empowerment per year.

Figure 8: Performance of RCF 2 with regards Female HDP empowerment per year



Source: RCF 2 Portfolio Data

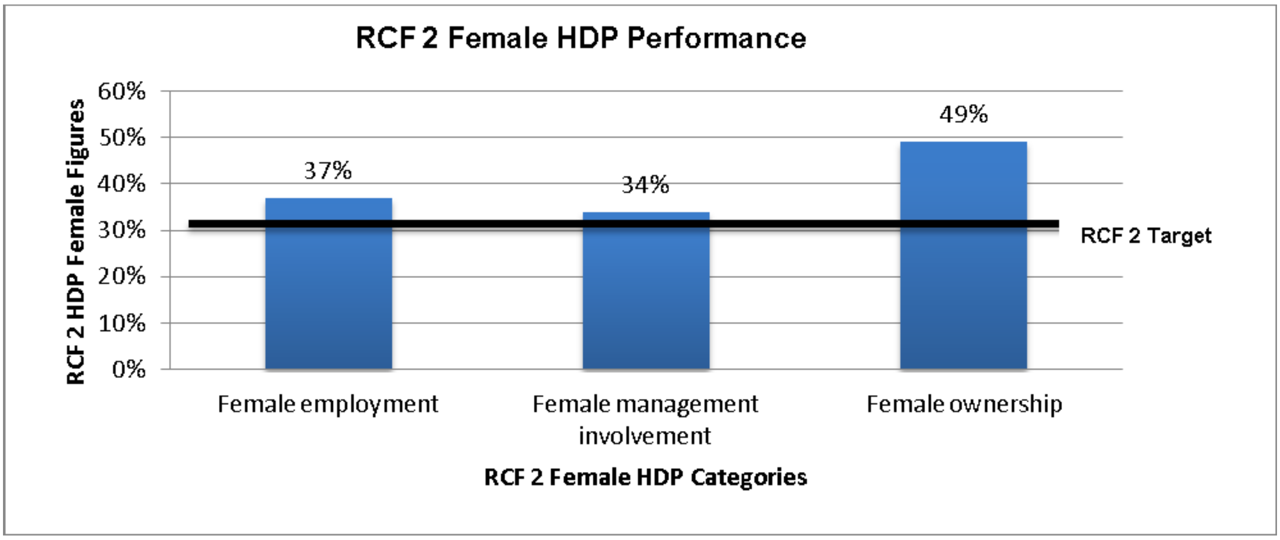
The latest RCF figures in relation to female empowerment through job creation, ownership, involvement in management and training shows the following:

- Female employment: 37%;
- Females involved in management: 34%; and
- Female ownership: 49%.

IDC has not been tracking the number of HDP women that have been trained and therefore we are unable to comment on progress made with regards to this indicator.

Figure 9: Performance of RCF 2 with regards Female HDP empowerment as at end of June 2013 confirms that RCF 2 achieved its minimum target of having at least 30% females in each of its Female HDP empowerment targets.

Figure 9: Performance of RCF 2 with regards Female HDP empowerment as at end of June 2013



Source: August 2013 RCF 2 Quarterly Report

The facility was expected to create 1 870 new HDP shareholders (net of cancellations). To date, 3 703 HDP Shareholders have been created[32]. RCF 2 received seven (7) applications with a Worker’s Trust component and out of the seven (7), five (5) were in the agro industries sector and the other two (2) in Forestry and Wood Products as well as the Textiles sectors.

2.3.5 Result 5: Investees have received adequate Business Services Support

Business Services Support (BSS) was introduced during the implementation of RCF 2 after it was funded by the IDC as a pilot in the RCF Unit.

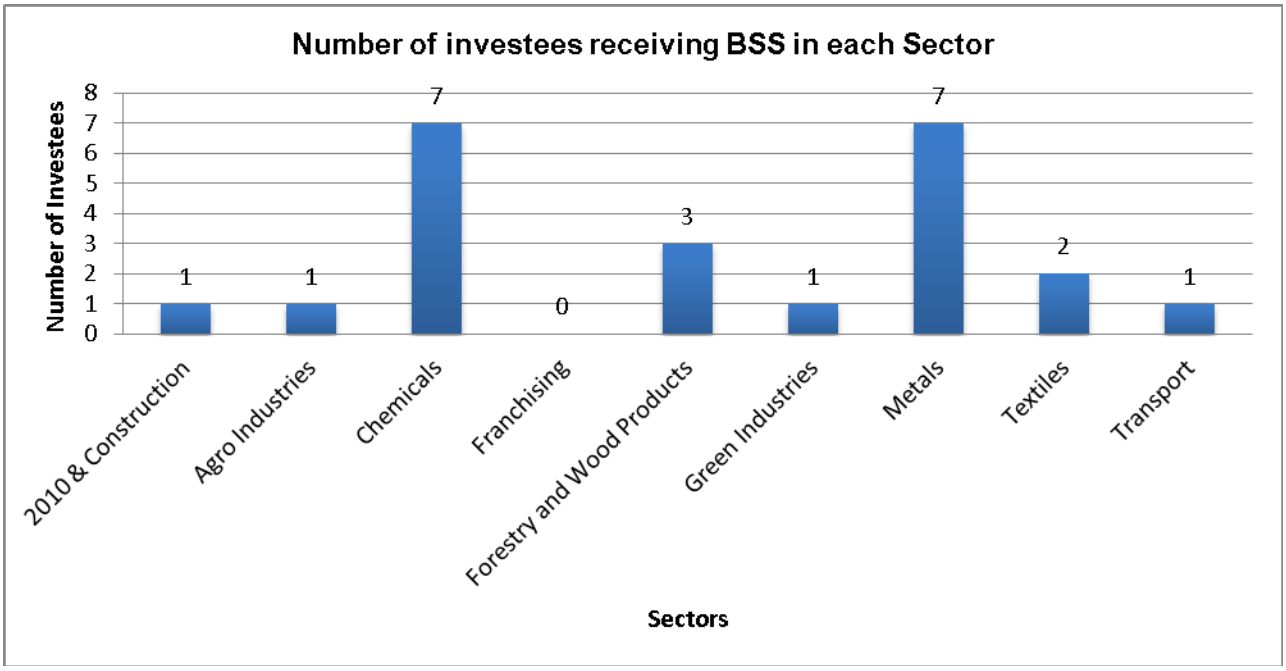
The portfolio information provided to the evaluators showed that 27 (39% of the investees) received BSS at a total cost of R20, 247, 155 (net of cancellations)[33]. This figure is 45 % of the EUR 5million[34] that the IDC contributed and ring fenced for BSS. The investees that received business support were all financed through the direct fund channel as none of the Niche Funds investees received such assistance. The BSS amounts allocated in the RCF 2 approvals of the Niche Funds were earmarked specifically for the investees. One of the Niche Funds, however, indicated a need for some business support especially with some expertise that is fundamental to the success of the Fund[35]. The BSS Client Survey[36] conducted in 2010/11 showed that the BSS was meeting investee expectations although the scores at 3.35 slightly fell short of IDC expectations of a score of 4 out 5. The number

[32] RCF 2 Portfolio Data
[33] IDC RCF 2 Portfolio Data
[34] Converted at an exchange rate of EUR1 to ZAR9
[35] Discussions with the Utho Infrastructure Fund Team
[36] Topline Research Solutions BSS Client Survey 2010-2011

of SMEs that have received BSS is quite low and a possible explanation is that a training needs assessment was not mandatory for investments approved prior to Rider 2 of the FA[37]. The RCF 2 MTR is credited with the paradigm shift that BSS needed to be pro-active in its approach to RCF deals[38].

Figure 10: Number of SMEs supported that received BSS as at end of June 2013 indicates that the Chemicals and the Metals sectors had the highest number of SMEs that received BSS with a combined number of fourteen (14) out twenty three (23) largely because these are highly specialised industries.

Figure 10: Number of SMEs supported that received BSS as at end of June 2013

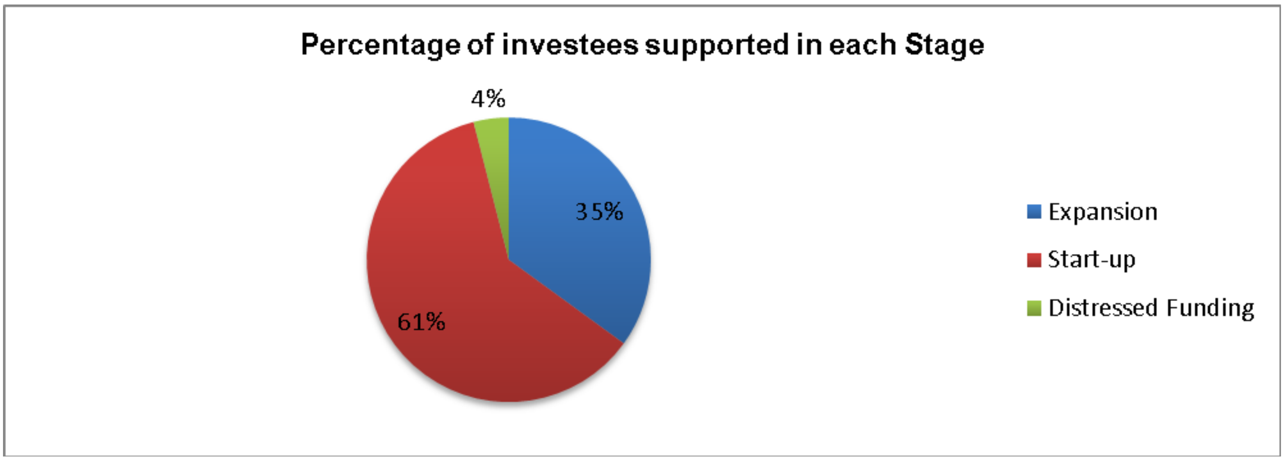


Source: RCF 2 Portfolio Data

Figure 11: Stages in which the SMEs were in when receiving BSS below indicates that that 61 % of the investees that received BSS were in the start-up phase.

[37] RCF 2 MTR
[38] 2010 Audit Report

Figure 11: Stages in which the SMEs were in when receiving BSS

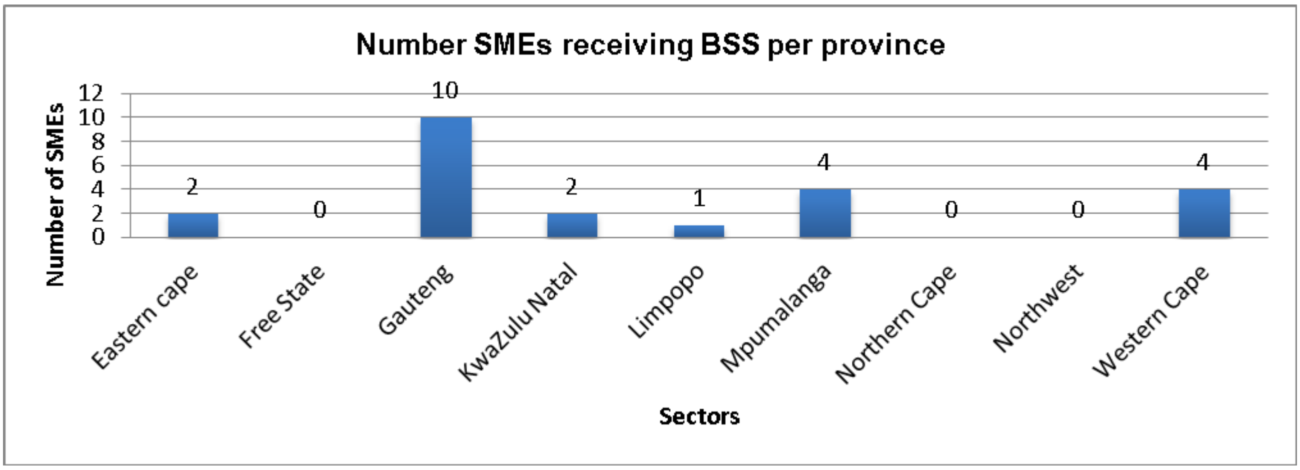


Source: RCF 2 Portfolio Data

BSS in start-ups is vital because the clients need support in building their capacity and understanding their market in order to compete effectively. It is important to note that there were some start-ups that did not take up BSS because it was felt they had the requisite expertise and experience for example, Power FM[39].

Figure 12: Number of SMEs receiving BSS per province as end of June 2013 shows the number of clients per province that received BSS; the majority of the recipients were from Gauteng, which is line with the concentration of the fund.

Figure 12: Number of SMEs receiving BSS per province as end of June 2013



Source: RCF 2 Portfolio Data

[39] Discussions with Power FM representative

2.3.6 Result 6: Increased investment and employment in Africa

RCF initially required the fund to support 15 SMEs involved with operations in SADC countries. However, this was later extended to the rest of the African continent. This objective has since been relaxed after a special request from the IDC for the EU to reconsider the target. In 2010, the EU sent a letter to the IDC completely relaxing Result 6 of the FA[40].

Since the MTR, there has only been one SME that has invested outside South Africa namely, Sun Power Solutions[41]. However, this investee is currently facing challenges.

2.3.7 Result 7: Environment has been enhanced

The FA required the investees to set up an environment and HIV/AIDS protection plan in accordance with the South African law in their entities. The 2010/11 RCF Client Assessment Report noted that generally larger investees have HIV/AIDS policies while the majority have no policies. The report found out that 6 investees have HIV/AIDS policies. It was also established that companies with HIV/AIDS initiatives were excelling at policy formulation but lacked effective implementation of programmes due to cash flow challenges. Despite this finding, RCF does not require investees to have a formal policy but for the SMEs to have activities around HIV awareness and this seems to be the case.

The MTR noted that all investees had designed environmental/HIV interventions to raise awareness on these issues. However, there are no visible Monitoring and Evaluation initiatives put in place by the IDC for tracking this result.

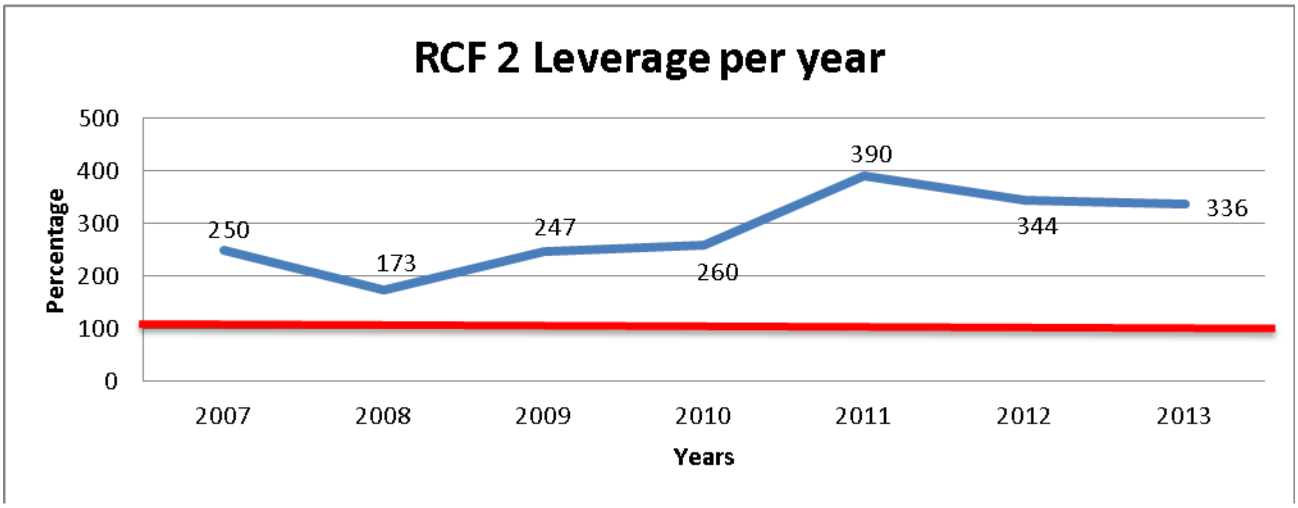
2.3.8 Other results: <u>RCF financing have been leveraged by more than 100 %</u>

- Direct channel

The targeted leverage of RCF funds through the IDC loans was 100 %. As indicated by the Figure 13: RFC 2 Leverage per annum up to end of June 2013 below, RCF 2 funds have been leveraged at a rate that is higher than the minimum requirement over the lifespan of the project.

[40] 2010 Audit Report
[41] 2010 Audit Report

Figure 13: RFC 2 Leverage per annum up to end of June 2013



Source: IDC Annual Reports

➢ Niche Fund Channel

RCF 2 supported four Funds under the Niche Fund Channel but one was cancelled mainly because the owner/promoter failed to meet the terms required by RCF. The approved three Niche Funds committed themselves to selecting SMEs as per the RCF terms and conditions and to monitor the RCF socio-economic indicators[42].

[42] IDC Risk Capital Facility Mid Term Review (2011)

3 FINDINGS

The fundamental finding with regard the relevance of the project is linked to the extreme challenge that the project is aiming at: supporting HDP controlled SME development with related HDP employment with a bias in favour of the poorer regions of the country, justified by the history of the apartheid years.

As an example, agribusiness development in the Eastern Cape region has the best potential results in terms of HDP job creation in a poor area, but the issue of finding capable HDP managers with minimum financial means, willing to settle in a remote rural area, to take risks with business development, providing employment to a scattered rural population with low level of education summarizes the challenge.

3.1 PROBLEMS AND NEEDS (RELEVANCE)

3.1.1 Project rationale

As seen above in Paragraph 1.3.1 unemployment was and remains an important issue in the country with about 30% of the population unemployed.

This unemployment affects mostly the black population, historically disadvantaged during the apartheid years, left out of modern economic activities and often restricted in their geographical location to underdeveloped areas.

Within this context, the Government promoted a long-term strategy to support black empowerment and Historically Disadvantaged Persons (HDPs), alongside its economic development strategy encompassing SME support (Cf. Paragraph 1.3.4), SMEs being considered as the main source of employment and of empowerment of black people.

<u>The programme was in line with these objectives and it remains consistent with, and supportive of the strategic priorities and policies of South Africa</u>

The Department of Trade and Industry (dti), as the main institution in charge of economic development at the time was chosen to be responsible for the oversight of this Sector Budget Support allocation.

As far as the EU is concerned, its Joint Country Strategy[43] “*reflects critically on what value-added development cooperation can bring to South African government-led poverty reduction and development programmes, such as the Accelerated Shared Growth Initiative of South Africa (ASGISA), the Joint Initiative for Priority Skills Acquisition (JIPSA) and*

[43] Cf. The South Africa-European Union Strategic Partnership Joint Action Plan, signed in May 2007

Broad Based Black Economic Empowerment (B-BBEE)” also justified the relevance of the programme.

The programme was relevant at the higher strategic level in that it addressed South Africa’s rationale for Official Development Assistance (ODA) and supported the five main pillars outlined in the ODA Guidelines[44] in the following manner:

- Innovation: assisted the IDC to develop more effective approach to SME development especially within the framework of B-BBEE.
- Piloting and testing: through RCF, IDC was able to develop successful models that are now being rolled out. Piloting and the rolling out of BSS throughout the IDC is one such clear example.
- Risk mitigation: created a favourable environment that encouraged investments in SMEs through cushioning the attendant risks.
- Catalytic initiatives/best practices: RCF's relatively small contribution helped to unlock domestic resources as evidenced by the leverage of IDC’s own funding as co-investments as well as the ZAR17 billion funds that are now earmarked for development funding. Investments in the Niche Fund Channel by other investors were catalysed by RCF’s contribution.
- Skills-transfer and addressing capacity gaps: IDC’s capacity in fund management including developing pricing models is a direct result from the lessons learnt during the implementation of RCF.

3.1.2 Project objectives

Within the above described context, and with the positive experience gained from RCF 1, the objectives of The Risk Capital Facility 2 were fully relevant.

Major objectives as mentioned in Paragraph 1.4.1 were to promote HDP and HDP female employment, management empowerment of black people and HDP shareholding through the provision of development finance to high risk SMEs[45] with a minimum 25% HDP shareholding.

3.1.3 Project structure

- Sector Budget Support

Within the global EU-South Africa context at the time, Sector Budget Support mechanisms were chosen to deliver the programme, rightly aiming to achieve a better ownership through the Government institutions.

[44] The Policy Framework & Operational Guidelines for the Management of Official Development Assistance 2011
[45] i.e. SMEs not bankable with the commercial financial sector

- The Project Steering Committee (PSC)

The wide composition of the PSC, providing significant expertise, under the Chair of the dti is fully relevant to the conduct of the programme.

It is regretted however that the members of the committee were not able to help RCF to implement the Third Party channel, through the active involvement of the Bankers Association representative, a member of the Committee.

It is regretted that the dti did not provide support to IDC to improve such co-operation with the commercial financial institutions, the more so that such co-operation could benefit all IDC Funds under management.

- IDC as the executive authority

The choice of IDC as the implementer is debatable since it was a development institution mostly involved with large project support at the time (2006), and new to the SME segment of the economy. The main reason for choosing IDC was its professionalism, its strong financial structure as well as its 100% ownership by the Government. This choice was also justified by the weakness of the financial institutions involved with SME support such as Khula or even the NEF at the time.

This choice proved relevant since IDC remains a very strong institution financially[46] and professionally, the more so that its mandate has evolved over the years to now cover the SME segment of the market: the Small Enterprise Finance Agency (SEFA), (which integrated Khula and SAMAF) being a subsidiary of IDC since April 2012. As described in Annex 7.2, RCF fully relied on IDC’s various departments and SBUs to support its activities.

However, with hindsight, it could have been envisaged to select the manager of the RCF 2 facility through tender, including in the short list, private financial actors like Business Partners or others, trying to build on a private public partnership and increasing leverage with private sector funds. Main drawback of such a choice would have hampered the engagement of the Government Institutions and probably would not have translated into the establishment of a large DFD department and BSS Department within IDC.

- The European Investment bank

The appointment of the European Investment Bank, at the request of the EU appears also relevant, having provided to IDC important capacity building in running a risk capital finance programme and also having provided overall supervision of the risk decision

[46] Despite increases in its non-performing assets, further to a pro-active support of the economy during the recent difficult years, in conformity with the Government policy

process, portfolio management, monitoring and reporting. The fact that most credit applications proposed by IDC/RCF were finally approved by EIB, does also point to the professionalism of IDC and to the involvement of EIB all along the negotiations with the potential “investees”.

The EIB’s intervention helped RCF to formalise more rigorously its credit assessment as well as its reporting. It is hoped that this structured professionalism can be maintained now that the EIB contract has been terminated.

EIB was involved closely with the project and a number of other IDC departments through numerous visits to South Africa and constant contact with the RCF team. The involvement of EIB increased the duration of the credit application process, estimated on average at 30 days by the EIB over the period, decreasing to 21 days by the end of EIB involvement which is considered acceptable by the mission.

EIB was also actively involved with the setting up of a mathematical model to estimate the value of the investments and the effective return necessary to maintain the nominal value of the Fund. This model was adjusted during the programme’s life to take into account experience gained.

Overall, it is recognised by the RCF team, by IDC and the EIB that its involvement provided well appreciated input and capacity building. The mission concurs with this appreciation, based on the concrete support provided: the fund valuation model, advice to the EU and dti, assessment of the project applications, joint management of the RMB account, creation and establishment of the Development Finance Department (DFD), the Business Support Department (BSD) as well as hands on management support when assessing the clients’ needs.

- The provision of risk capital finance versus equity investment

The programme was structured to provide equity or quasi equity support to high risk SMEs which appeared relevant at the time and was supported by the EIB as well as by the mid-term review.

In practice however, the financial instruments used did not resemble much equity or quasi equity (except for a few enterprises, where equity was organised mostly to support Workers’ Trust share ownership) but were mostly made of subordinated loans (often only subordinated to the IDC commitments) with special features such as long term maturity, grace period, whose interest and principal repayments were linked to the availability of sufficient cash flow, including a variable remuneration with uncapped upside, and repayments being pushed back to the end of the loan duration should they not be able to be serviced.

Based on RCF activities, performance and results, it is interesting to note that the high risk lending provided by RCF, in as much as the loans were subordinated, that the interest and reimbursement of the loan principal was usually payable only if and when the cash flow proved sufficient, otherwise rolled back to better time when cash flow would allow or even until the end of the loans, provided effective support to a number of high risk start-ups or early developments. It only remains to be seen if the "balloon" accumulated in a number of cases towards the maturity of the loan can be restructured in an acceptable manner to allow the continuation and development of the concerned enterprises. It is regretted that no significant assessment of this issue has been conducted at the portfolio level and that early negotiations are not engaged with the concerned enterprises to ensure RCF exit or continuous support and enterprise survival/development.

To insist on real equity in the cases assessed by the mission would not have changed the issues in practice, since the equity portion would have had to be small in terms of amount not to crowd out the enterprise promoters, the bulk of the financing having then similar characteristics as the subordinated loans. The fact that the RCF loans were only subordinated to IDC loans and not to commercial lenders did not again prove in practice a drawback to commercial bank support which was not forthcoming in most cases due to the high risk profile of the "investees".

The few cases of real equity mostly linked to Workers' Trust or Community Trusts share finance did not translate into the equity support sought for, since the Workers Trust did not provide an effective Black Economic Empowerment, the share financing often being used by the non-BEE promoters to achieve a high financing leverage disguised behind the Workers' Trust supposed equity.

Main difference which real equity support might have allowed could have been a stronger involvement of IDC/RCF at the investees' management level (in doubt in view of the limited availability of IDC/RCF managers to provide real hands on support to small size investees) and a higher upside in case of success.

The upside attached to the subordinated loans, either as a percentage of the profit or of the turnover does not really provide a significant participation in the success of the investees, being often capped at a maximum of 10 % gross IRR. In practice, through the few cases reviewed by the mission, it appears that either the project was a success and the loans granted could be repaid easily, or the project was not performing as expected for which an equity instrument would not have made much difference.

Finally, let's mention the positive cases exemplified by project finance type of support, linking the loans granted to new ventures to specific contracts secured by the enterprise from reputable large corporations. Such financial support allowed the enterprise to grow while limiting the financial risks to the technical risks of supplying the services contracted for.

Also, worth mentioning, the positive results associated with the involvement of a strong partner in the projects[47], bringing comfort in the processes, mostly through know how regarding new technical developments.

Overall, it is recognised that RCF financial support was relevant in as much as it effectively provided development finance to seventy three (73) non-bankable SMEs, of which forty nine (49) have been successful, having employed the targeted number of persons over various poor regions of the country (Cf. Paragraph 2.3.2).

- The investment guidelines

The investment guidelines were often viewed as too restrictive by the RCF team. It is not the opinion of the mission which considers that they were fully relevant, helping RCF to really target the proper enterprises to be supported, sector wise, size wise, geographically wise, with effective employment prospects, BEE management promotion and BEE shareholding.

It is well appreciated that these guidelines were difficult to meet, especially in the poorer areas of the country where finding reliable capable and financially viable BEE promoters remains a difficult challenge, hence the biased results in favour of Gauteng and Western Cape regions.

- The BSS support

BSS support was to be associated with financial support as one of the lessons learnt from RCF 1. Unfortunately, this support was slow to being organised and delivered; it was only after 2011 that a BSS needs assessment had to be conducted prior to, and accompany the credit proposal evaluation.

The mission estimates BSS to be fully relevant while it was not able to confirm the positive impact such BSS might have had on the beneficiaries. The mission could not appreciate its effect during the visits to a number of the investees, the impact assessment of such support being difficult to organise. It is duly noted that the BSS Department of IDC is trying to develop a methodology to monitor its BSS support impact.

Let’s just note that all beneficiaries met who had access to the BSS grants were satisfied with the results and that all IDC clients can now benefit from potential BSS support, this alone showing an apparent relevance of the grant blending instrument.

- The RCF department

[47] Such as the contract obtained by Pharox Lumens from ESKOM

The delivery of the programme, entrusted to a Project Monitoring Unit (PMU), ring fenced within IDC, benefiting from the support of the various IDC departments appears relevant to the objectives pursued, benefiting from the professionalism of IDC, while at the same time allowing IDC to learn from the process with support from the EIB involvement.

The draw backs associated with this management design, such as positioning RCF staff in the back seat as far as the direct channel is concerned, did not allow to empower the RCF staff vis a vis its investees.

Also, the fact that RCF was a department of IDC did not facilitate the raising of extra funding for the programme as had been envisaged originally.

Finally, this lack of empowerment of the RCF staff, and its limited risk expertise did not allow RCF to dispense with IDC or third party risk assessment support to address the Third Party Channel effectively (Cf. further analysis thereafter).

- The three delivery channels

The rationale behind the three delivery channels was essentially to leverage the funds provided by the programme with private sector support. In that sense, the proposed delivery process was relevant in theory, while in practice, the Third Party channel was not able to garner the commercial financial sector participation.

- The Direct channel

With hindsight, the Direct channel proved an effective route to deliver the development finance support, with RCF funds being leveraged in the process by IDC commitments.

- The Niche Fund channel (NFC)

The Niche Fund channel impact is less easy to assess. In the case of Agri-Vie and Evolution One, the RCF investments helped to catalyse the establishment of these funds, IDC/RCF providing institutional comfort to other hesitant would be investors, as confirmed by the Funds' managers, thereby allowing for leveraging the RCF investment. The leverage of the EU funds however was somehow limited since most of the investors in the Funds supported were public Development Financial Institutions (DFIs) while private investors did not subscribe to the funds. Also it appears that in a number of cases, these Funds' investees have not yet met the socio economic covenants required in terms of social economic results, especially regarding female shareholding and HDP ownership. There are plans in place to achieve the targets and according to Agri-Vie; it was unrealistic to assume that the development indicators would be achieved in less than one year of the investments as it takes time to reach the targets.

The case of the Utho Capital Infrastructure Fund is different in the sense that the RCF/IDC funds were the sole investment alongside NEF in the Fund, thereby not providing leverage with non-government funding. However, the investment allowed the creation of a 100 % BEE managed equity fund which would not have been possible without these investments[48], thereby supporting BEE shareholding, management expertise as well as the final investees. This again confirms the relevance of the NFC in supporting the overall objectives of the programme, especially for HDP managed Funds.

<u>- The Third Party channel</u>

The case of the Third Party channel, while appearing relevant as already mentioned did not prove effective; no deal having been concluded under this channel. Main reasons mentioned by RCF to explain the negative results concern the cost of the due diligence which would have to be effected on each investee, by IDC or a third party, in view of the limited capacity in this regard of the RCF team, but even more difficult was the refusal by the commercial financial institution to get involved with the monitoring of the socio economic indicators unless for a significant fee, or even to be subjected to RCF/IDC due diligence review, while Business Partners found the decision process on “investees” support too lengthy.

The mission is surprised that commercial lenders have not been more interested by this “first loss” type of financing which would have comforted their own lender risk position, unless the client risk target was too off the mark for commercial lenders. It appears from contacts made with some financial institutions that the main draw backs consisted of the heavy administrative burden to run the Facility for the Financial Institution (FI), the cumbersome initial due diligence to be conducted on the financial institution itself, and the further risk assessment by IDC/RCF/EIB, all of which being slow and time consuming. The benefit for the FI being rather small[49] in terms of amount or number of potential HDP controlled SMEs when one consider that a Bank like Standard Bank approves 800 SME credit application per month and Business Partner, between 350 to 750 per annum.

It is therefore recommended that all stakeholders should be associated from the start in the design of the Facilities, to ensure that a viable process is organised, satisfactory to the parties.

The mid-term review suggested that the Third Party channel should be utilised to address the smaller end of the market through i) the Direct channel, provided IDC is able to simplify

[48] It should be mentioned that the BSS allocation to Utho is restricted to the benefit of its investees, while the mission is of the opinion that the fund manager itself, being new to the function should be actively supported with appropriate BSS
[49] 30 % of Euro 47,23 million for the Third Party channel, i.e. about Euro 15 million to be disbursed over five years, i.e. Euro 3 million per annum spread over three partners, i.e. about Euro 1 million per annum per partner: about two or three clients supported per annum per private financial institution partner is probably not worth the negotiation and administrative effort on the part of the commercial financial institution, unless it is a small financial institution

its credit risk assessment to reflect the smaller SMEs targeted, ii) a kind of Niche Fund channel, or Direct channel, using Khula as the “co-investor” or iii) still pursuing the Third Party channel through financial institutions targeting the smaller end of the market, hoping that IDC would provide the simplified risk assessment. These proposals did not materialise, since Khula faced a significant reorganisation, being finally merged within the Small Enterprise Finance Agency (SEFA). The fact that SEFA is now a subsidiary of IDC should allow efficient assessment of risks at the SEFA level.

- SME investments outside South Africa

<u>This target does not appear relevant to the BEE SME support objectives. The fact that RCF was to support high risk development providing BEE employment was difficult to reconcile with the support of SMEs expansion in the rest of Africa or even Southern Africa, unless such investments were complementary to domestic BEE SMEs development.</u>

The fact that IDC involvement outside South Africa, in the rest of the continent, is specifically focused on large projects probably did not help to promote BEE SME support outside South Africa. In this regard, IDC could play a role to promote South African sub-contractors and SME suppliers to participate in such large projects, in the same spirit as detailed in our “Value chain” proposal detailed in Paragraph 6.2.2.

Nevertheless, the mission met at least one case where the RCF investee had an effective investment opportunity in Ghana, but was not aware of RCF potential for international development support. In addition there was another investee, Sun Power Solutions who made an attempt to invest outside South Africa but was not successful.

Following a request from IDC, the target was revised via Rider 1 to the FA and became a best effort. The EC in 2010 further decided that this KPI would not be considered during the final evaluation.

3.1.4 Main issues regarding the programme relevance

<u>The main issue concerning the Programme relevance relates to the number of SMEs which were to be supported: 70 enterprises only. This has been achieved albeit over seven years instead of four, i.e. ten enterprises per annum with about 1000 direct employment created per annum. Indirect employment probably should multiply this number by two, but no assessment has been done in this regard. This definitely is a major limitation of the programme and could question its rationale. This comment however has to be mitigated as already mentioned by the real challenge to find acceptable “investees” meeting the investment guidelines.</u>

<u>This limited number of enterprises supported is also mitigated by the fact that RCF proved very influential, at the IDC level, whereby it taught IDC the way to develop risk capital</u>

finance specific facilities, the number of Funds having increased from one at the beginning (RCF) to thirteen at present with an accumulated value of about ZAR 17 billion under DFD management.

Finally, the number of enterprises supported by RCF mostly through the Direct channel, about ten per annum should be compared to the number of clients supported at the IDC globally estimated at about 300 per annum, i.e. about 3 % of IDC deals can be considered as resulting from the RCF catalytic role. This may appear small except if you consider the RCF role model with regard the setting up of IDC’s other thirteen funds valued at ZAR 17 billion.

The second main issue linked to increasing the RCF outreach in term of number of enterprises supported concerns the difficulties met in delivering RCF investments through the Third Party channel as discussed above (Cf. Paragraph 6.2.2 hereafter about recommendations for the future in this respect).

Finally, usage of the term “cost” per job created is misleading, since it in fact concerns RCF financing amount per job created, not counting the investment provided by the other actors, based on the principle that the investment would not have happened without RCF involvement and that other actors’ financial support is not concessionary, but is purely commercial. Such limitation while putting a welcome cap on the RCF share/risk of the total investment, increasing with the number of potential jobs to be created, did not allow an objective assessment of the capital intensiveness of the projects supported, nor the real costs per job created which should be based on the RCF concessionary rate and accepted losses subsidy per job created over the RCF loan/investment duration. This has been roughly estimated by the programme (Cf. Paragraph 3.3.3 for further discussion of this point).

3.2 ACHIEVEMENT OF PURPOSE (EFFECTIVENESS)

3.2.1 Budget support versus programme structure and the stakeholder involvement

This section seeks to establish the extent to which the RCF 2 was effective in attaining its objectives. In so doing, a number of specific issues related to the implementation of the programme will be considered. Key to this analysis will be an assessment of the effectiveness of individual stakeholder roles in the programme.

Firstly there is a need to emphasise that RCF 2’s design did not take the form of a classical project due to the challenges that were experienced during the implementation of RCF 1 such as the incompatibilities between the EU and IDC procurement procedures which led to a substantial amount of funds being decommitted. Thus, the RCF 2 approach was to put together a Sector Budget Support Programme although it still maintained the fund structure. To this end the finance was ring-fenced and elements such as the need for policy dialogue, disbursements of funds in variable tranches depending on achievement of targets were excluded from the Financing Agreement.

- Stakeholder Management and Participation

There is evidence to believe that the stakeholders' involvement in the management of RCF 2 was largely effective with regards to communication, risk management and other issues. Key stakeholders in the programme were the EC, dti, IDC, EIB, National Treasury, EDD and the investees who were the end beneficiaries. A brief analysis of stakeholder participation and management is given below:

- European Commission

The European Commission's primary role was to fund the programme. Other roles that the EC played included: participating on the Project Steering Committee as an observer and assessing conditionalities regarding tranche releases and commissioning of result monitoring mission, the MTR as well as this final evaluation. The EC provided support and guidance to the dti with regards to the management of the FA which was subsequently revised twice through Riders. The EC was also instrumental in the design of RCF 2 through using lessons learnt from RCF 1.

- The Department of Trade and Industry

The Government of South Africa through the dti was the owner of the RCF programme. The dti played a key role in the steering of RCF 2 and was responsible for chairing all the PSC meetings. However, the dti could have been more effective to coordinate the adoption of the ToRs of the PSC and to liaise with the South African Revenue Service (SARS) as a facilitator in talks about the RCF's tax exemption status. Furthermore, the dti could also have been more proactive in initiating broader dialogue in terms of learnings with regards to SME financing modalities even though dialogue was not a precondition for tranche release. Despite these short comings, there is evidence of dti's ownership of the programme and hence the success encountered. The learning from this successful experience of managing a donor supported programme by a government department could provide useful insights for the International Development Cooperation Directorate in National Treasury.

- Industrial Development Corporation

The IDC was the implementing agency of the programme and its role was managing the RCF 2, appraise applications, market the RCF 2 and conduct performance appraisals. It should be noted that the IDC was the secretariat for the PSC.

The IDC was highly effective in managing the project due to three main factors: the commitment of IDC in ensuring that the programme succeeded by creating additional posts and units. (IDC created a separate unit to manage the programme and resource the team). In addition, the IDC had the added advantage of having wide experience in the development finance arena. Again there was a close symbiosis between the different units within IDC i.e. PIMD, BSS and other SBUs. Other positive developments include:

- Design of the Financial Model;
- Commissioning of an annual assessment undertaken in 2010/11 though plans for further annual assessments were stalled due to lack of funding;
- The BSS has created a learning agency (its e-Learning programme did not successfully take off and has been shelved).

The RCF 2 reporting has been effective and was noted as having improved significantly overtime. However, the evaluation team experienced challenges to access certain investees’ documents that were requested in order to have a global view of RCF portfolio. This is an area that requires attention going forward.

It is noted from the EIB’s February 2012 presentation to the PSC that the RCF 2 at some point experienced high staff turnover which resulted in the loss of institutional memory. This left a few staff members to manage the facility which has grown. In addition these staff members are also responsible for other Funds.

With regards to monitoring the Fund, there were concerns that the PMID is not adequately resourced to visit and monitor all the RCF 2 investees at least once a year. As a result the last time all the investees were monitored was in 2010/11 through an external consultant. IDC was of the view that such a comprehensive exercise was not only costly but required additional management time to review and follow up the results. It was then decided that the client assessments would be undertaken bi-annually.

Another major weakness was the failure to systematically capture lessons learnt from the investees as well as profiling of success stories.

- European Investment Bank

EIB's main role was offering technical advisory services in the form of providing independent expertise. The EIB also had the function of monitoring quality control for the EU and dti and provided an annual performance review. The EIB created an independent database which was tracking financial and non-financial indicators. EIB's role was instrumental in building the capacity of the IDC and through the RCF there have been technical exchanges between the two institutions. There was effective collaboration between the EIB and IDC with the latter presenting its approach to "pricing financial instruments with development indicators" to EIB management and staff in 2009, while the EIB liaised with IDC when enhancing its measurement and reporting on development indicators.

It is reported by both the EIB and the RCF that the collaboration between IDC and EIB led to a low rejection rate as the two parties worked closely and effectively in the management of the portfolio. The two partners also successfully managed the joint bank account. EIB's involvement resulted in the following value addition:

i. The structuring of the Niche Fund Channel deals;
ii. At approval, the joint review/structuring of RCF instruments to reinforce their equity nature;
iii. Support to IDC in driving the BS paradigm shift;
iv. Assistance in drafting the TOR for the second annual survey (provided to address the shortcomings identified in the 1st Annual Survey); and
v. Development and follow-up together with IDC of an action plan to address key recommendations from the MTR;
vi. Involvement in the design of enhanced reporting system / financial model;
vii. Assistance in identifying/resolving gaps in the implementation of WT and in the monitoring of HIV plans.

- Economic Development Department

The EDD was created in 2010 and is now the parent department for the IDC. The Department is also responsible for the coordination of SME policies. It is noted that the Department was not really involved with RCF 2 although were aware of its existence. One can argue that this lack of proactive involvement is regrettable as the Department could have drawn useful policy lessons on SME support from the implementation of RCF 2.

- National Treasury

The National Treasury (NT) through the Directorate for International Development Cooperation is the key Department that is responsible for all incoming ODA in

South Africa and is responsible for ensuring that development cooperating partners abide by the Aid Effectiveness Principles. The Department has relationships with other government departments such as the dti and EDD. Developmental issues among these departments are interrogated and discussed at the cluster meetings. The NT acknowledges that their limited involvement in RCF 2 was due to the perceived success of the programme. The evaluation mission believes this was a missed opportunity for the NT to gather best practice principles that could possibly feed into future ODA programmes.

- Investees

As the recipients of RCF 2, the investees are important stakeholders of the programme. Generally it should be noted that the investees were not aware of the RCF 2 funding. They only became aware of the RCF 2 during deal structuring. Investees such as Power FM failed to take up opportunities outside the country since they were not aware that the RCF also funded projects outside South Africa. In future there is need for an intensive media drive to conscientise the nation and HDP entrepreneurs on the RCF 2 especially in provinces such as Limpopo where there was low uptake of RCF products.

Box 4: The Power FM case

Background

Power FM is an English medium, talk-led commercial radio station, with music at various intervals, broadcasting in the Gauteng Province. Power FM is owned by MSG Afrika Media, Ndalo Media, Zico and other investors.

Power FM was licensed in December 2011 but only began operations in June 2013. The reason for the delay was the process of seeking capital on a loan basis and not getting funding from an Investment Fund because of a “selfish view” that the work put in was worth the wait and did not want to give the value away. However, had it not been for IDC and NEF funding, MSG would have had to settle for an equity investment in Power FM because they had many approaches from potential investors.

Entry into the market

The overall emphasis of Power FM will be on talk between 60% and 70% of air-time being speech-based programming.

The radio station saw an opportunity to be a catalyst and to offer a comfortable place for long overdue frank talk about key South African issues as well as concerns in the hearts and minds of its target audience. The market had a gap for a talk format explicitly catering for the needs and interests of black people in Gauteng. The primary target audience will be black males and females between the ages 25 and 49. Given the history of the media, there is no platform to facilitate such a conversation with credibility because of compromises to either the owners, institutions past or being seen to stand for a certain political ideology.

The media sector like many other sectors in the South African economy is white dominated. The difference between the media and other sectors is that it is not only white dominated now but has been for generations. A lot of the existing established media entities are second to fourth generation businesses. There have not been any post-1994 black-owned media businesses. Being the only talk radio station licensed after 1994, Power FM has a dual outlook to its sector which is:

i. Transform the media's role in society with a view to facilitate a safe space for every South African to hold authentic conversations and express themselves on what is happening in the country rather than in a closed environment between individuals. These discussions could be on the direction of the economy or the country's past but people do not openly discuss them in public for fear of being judged as being anti or pro-apartheid or "sucking up to the current administration". Another example could be black South Africans who sacrificed their lives fighting for the liberation of the country who think this is not the country I fought for. There are also young people who are thankful for the liberation heroes but do not feel they are the ones who will take the country forward.

ii. Ensure that the business is sustainable.

Missed opportunity

Power FM has growth aspirations in the rest of the African continent and was presented with an ideal opportunity to achieve this in Ghana. MSG required R15 million to take over a struggling radio station in Ghana but failed to raise this amount because South African banks are cautious when it comes to investments on the continent. Like most of the RCF 2 clients, they did not know the details about RCF 2 and in this case, the fact that the facility had a provision to support South African SMEs wishing to do business on the continent.

This was a missed opportunity because MSG has the experience and expertise to run radio stations in South Africa as well as other business interests on the continent.

- Project Steering Committee (PSC)

The PSC's specific role as outlined in the TOR[50] is mainly to provide the project management with guidance and policy direction. There is no doubt that the PSC achieved remarkable milestones with regards to coordinating the different stakeholders. Meetings were well attended but it was noted that certain institutions such as the National Economic Development and Labour Council (NEDLAC) and NT did not regularly attend meetings and this could have robbed the programme of valuable perspectives from the different stakeholders. RCF unit's support to the PSC has been remarkable; this has been achieved through improved reports over time, however without a clear global portfolio review. A review of the minutes of the PSC shows that it has been effective in delivering according to its mandate. Going forward, the PSC might miss the independent view that was provided by the EIB.

[50] Department of Trade and Industry and Industrial Development Corporation Limited: Risk Capital Facility Project Steering Committee; Terms of Reference (2011)

3.2.2 Delays in implementation, underutilisation of funds, absorption capacity, marketing of RCF products

As pointed out in the Mid Term Review[51], RCF 2 experienced a two year implementation delay. This was due to delays in finalising agreements between the various implementing parties which consequently led to a slower disbursement rate. It was also argued by some interviewees from IDC [52] that the delays could also have been a result of stringent guidelines which manifested in the slow rate of approvals. It was thus suggested that, in future guidelines and conditions should be kept at a minimum as this had a negative impact on intended outcomes as few investees can meet all the requirements. The present mission is of the opinion that present investment guidelines are satisfactory and do meet their purpose, e.i. to channel the funds to the targeted SMEs as already mentioned page 70.

As of June 2013 disbursements to beneficiaries were still at 78% of total commitments. Table 11: RCF outstanding commitments as of end of June 2013 below shows the figures:

Table 11: RCF outstanding commitments as of end of June 2013

Description	Amount in ZAR
Total Approval	475 621 974
Cancellations	82 621 237
Total approvals (net of cancellations)	393 000 737
Write offs	22 300 000
Exits	4 000 000
Disbursement to beneficiaries	308 142 238

Source: RCF portfolio data

- BSS disbursements were at 22% of total commitments. Part of the reason for low disbursements include the fact some businesses were still in the process of being set up and in some cases, the proposed training schedule was clashing with the investees" operational calendar, while the main reason is linked to the slow start of this component at the beginning of the programme.

- Marketing of RCF 2 products

[51] Mid Term Evaluation of the EC-funded Private Sector Support Program Support to the Risk Capital Facility 2-SA/21.031700-05-01
[52] Interview IDC

Marketing of RCF 2 products has been satisfactory, although some investees did not have adequate knowledge about the fund. The RCF unit marketed the Fund through the following:

- DFD Brochure;
- RCF Brochure;
- IDC Calendar for marketing;
- Road Shows;
- IDC website; and
- Ad hoc presentations to organisations who wanted to gain a better understanding of the RCF

In future, it is important that the RCF applies different communication methods so as to cater for grassroots level SMEs so that they can have a better understanding of the funding sources and targets. Investees interviewed during the mission did not fully understand the financing structures especially the special features and implications of the RCF component.

3.2.3 Characteristics of investees, small versus medium SMEs

The main focus of RCF 2 was to provide funding in the SME sector in order to enhance Broad Based Black Economic Empowerment (B-BBEE) and to create jobs. The fund targets SMEs with employees numbering 10 to 200[53], other conditionalities concerned turnover and total assets (CF. Annex 7.6) which were increased to consider inflation and allow for more deal flow.[54]

RCF did not categorise the SMEs in line with the classification provided by the National Small Business Amendment Act of 2003 and 2004. In addition there was no benchmark set right from the beginning in terms of the characteristics of the investees which could have been used to monitor progress against such indicators.

The data below shows the value of funding given to SMEs as an attempt to give an overview of the types of SMEs that were funded. As shown in Table 12: Number of investees supported per channel and SME size below, most SMEs that were funded through the Direct channel with amounts ranging between ZAR1-5 million.

[53] Risk Capital Facility Financing Agreement
[54] Risk Facility 1 Closure Report

Table 12: Number of investees supported per channel and SME size

RCF Amount (ZAR)	Direct Channel	Niche Fund
Less than 1 million	6	2
Between 1 million and 5 million	29	7
More than 5 million	18	1

Source: RCF reports

It is difficult to categorise the SMEs based on the loan amount, however, one can safely state that the majority of investees were small businesses. It is regretted that the Programme did not classify its investees as per their size to eventually draw lessons for the future.

3.2.4 Jobs created, HDP employed and empowered, HDP share ownership increased

The evaluators are satisfied with the achievements of RCF 2 in meeting the targets for job creation.

It is important to note that some of the investees have not yet reached peak operating levels and it remains to be seen whether they will be able to create the promised number of jobs, empower HDPs or increase the HDP share ownership. However, their applications indicated that they had plans in place to achieve their developmental targets. The use of Workers’ Trust in some of the investees was supposed to be a key route to increasing HDP share ownership but it is not clear as to their level of involvement in management. This issue is further discussed in Chapter 5. Jobs created were mainly in the agricultural industry and this is a positive development considering that the agricultural sector is the fastest growth sector in the country, provided some of the important developments funded in this sector prove viable.

The evaluation notes that there is limited monitoring and assessment of the RCF impact in terms of the achievement of the facility’s development targets. The RCF 2 SBU relies on PIMD for monitoring of the investee performance but they have a mandate to carry this out for the whole IDC portfolio meaning only a limited number of RCF 2 clients can be visited. The portfolio data with HDP figures provided was based on the client assessment of 2011. As a result, information on clients approved after the detailed assessment and the progress made to date is not known.

3.2.5 BSS delivery and training

Business Services Support (BSS) was introduced during the implementation of RCF 2 after it was funded by the IDC as a pilot in the RCF Unit. The idea was to make BSS play a complementary role in making interventions more successful. The IDC has also established an IDC Training Academy Unit for its clients including RCF 2 investees;

however the number of RCF investees trained is not monitored. The BSS offer to investees comprises of management consultancy and mentoring, socio-economic development and training services. These services are geared to ensure material economic and social empowerment for RCF transaction business owners, their board members, management, staff, communities and cooperatives. The main support required by clients from RCF was mainly on management and mentorship[55].

Box 5: The case of Astradeals

Background

Astradeals is a start-up SME located in Polokwane, Limpopo Province. It was established by entrepreneurs, Joe Chuene and Joco Kritzinger for the initial purpose of providing oxygen gas to the welding industry and later to the medical and other industries.

Motivation for the business

The market is monopolised by three multinational companies, Air Liquid, Air Products and Afrox. The Astra Deals plant is the only South African owned enterprise which will manufacture oxygen gas in the country. If this succeeds, there are plans to franchise it and IDC will be asked to support that process.

IDC through RCF 2 provided R2 million in subordinated loans at 6% interest rate for capital expenditure as well as start-up costs. The loan was sought from the IDC because other financial institutions such as commercial banks were concerned with the risk especially due to the low equity contribution by the shareholders.

Business Support from the IDC

Astradeals benefited a great deal from the IDC's BSS because it assisted the SME with meeting the requirements to operate in the industry. The main support received was in the following areas:

i. Obtaining the required certification to operate in a highly regulated industry
ii. BEE Certification

BSS was delivered through a highly knowledgeable sector specialist who acted as a mentor to management and the expectation is that this will be a continuous process. The BSS was valued at ZAR125, 000 funded on a 50-50 basis between IDC and Astradeals. This is a classic example that shows how BSS played an important role in assisting the company to set up and according to the owners of the business, without such support they could have made mistakes and it could have taken them a longer time to commence operations. However, it must be noted that this project is under legal action mainly as a result of delays faced during start-up of operations.

[55] Discussions with the Business Support Managers at IDC

➢ Missed opportunities

To some extent RCF 2 is credited with the paradigm shift to understand and acknowledge that BSS must be pro-active in its approach to RCF and the IDC deals[56]. In addition, to some extent, the RCF 2 could also be credited with contribution to the growth and use of BSS throughout the IDC for its clients[57]. Currently the BS team at the IDC head office is working on improving and expanding its working relationship with the Post Investment Monitoring Department. Plans are also underway to appoint additional outsourced business consultants to meet the evolving demands of the investees. Investees now require business support from pre-investment to exit [58]. The BSS Client Survey[59] conducted in 2010/11 showed that BSS was meeting investee expectations though a 3.35 score fell short of IDC expectations of a score of 4 out 5.

It emerged that BSS is concentrated on start-up investees. However, there is a paucity of data to link BSS with growth and sustainability of RCF 2 investees. The BSS Survey of 2013 however gives an indication of the impact of BSS to investees. Survey was conducted to all IDC investees not only RCF1 clients. The results indicate that on average BSS has contributed to the short and long term sustainability and improvement of financial performance of businesses.

However, despite these successes, the number of SMEs that received BSS is quite low (27 SME net of cancellations) and a possible explanation is that a training needs assessment was not mandatory for investments approved prior to Rider 2 of the FA. The investee Assessment Report (2011) pointed to several lessons that could be considered as a way of going forward with regards to BSS in future initiatives. These lessons included:

- BSS is not adequately capacitated to provide support from pre-investment, post approval, post disbursement and exit so there might be a need to employ at least two BSS staff dedicated to RCF investees. BSS should commence immediately after the initial verification of a funding application and a need to include RCF funding has been established.
- Investees have major challenges in the early stages of the business (when profitability and cash flows are low) thus BSS should take two approaches: proactive where BSS anticipates challenges that investees could face and finds solutions to those challenges and reactive where BSS is driven by an investee situation.
- Some investees recommended that BSS should, to some extent be the equivalent of strategy development or a diagnosis and implementation and monitoring function

[56] 2010 Audit Report
[57] Discussions with the Business Support Managers at IDC
[58] RCF 2 MTR
[59] Topline Research Solutions BSS Client Survey 2010-2011

in a large organisation/corporate. In large organisations such an intervention is often staffed by full time and highly experienced personnel.

- o Clients require BSS across all facets of business operations but key areas that emerged included:
    - Understanding the Client’s Bigger Picture: Some clients have a larger vision to their business than what is initially presented to the IDC and engagement of a coach and mentor could help clients in articulating their vision which could be further developed into a future project.
    - Sales and Marketing: Numerous investees failed in this area.
    - Processes and Systems: Some clients have business knowledge but cannot afford to employ a person with systems and processes knowledge.
    - Detailed Review of the initial funding model: Sometimes initial financial and production forecasts are out of sync with the reality on the ground. As a result lengthy processes of applying for more funding might possibly lead to the business becoming insolvent. BSS might be able to assist in such a situation by conducting a detailed review of the financing and production process model.

As a pilot, RCF must continue to champion different innovative approaches to BSS and should therefore be very flexible in the deployment of BSS. While BSS was not provided for the Fund Managers in the case of Niche Funds, there is a clear case for this support to strengthen Utho Capital SME Infrastructure Fund manager and the case in Box 6 below is another motivation for BSS support to another Fund, Evolution One, for concept development.

Box 6: The case for Business Support to the Niche Funds themselves

Business Support – Evolution One Evolution One niche fund requires Business Support at two levels – the fund manager level and niche fund investee level. The Fund manager invests significant amounts in research and development to develop potential viable business models. The Evolution One target industry, clean technologies, is new and has no established business models. Funded businesses are often concept based investees which are sometimes initiated by the Fund Manager and still need to be tested and developed. We would recommend that a portion of the BSS allocation for Evolution One be earmarked for concept development.

Source: 2010/2011 RCF Client Assessment Report

3.2.6 Financial instruments used

As already outlined in Paragraph 3.1.3 above as far as relevance is concerned, the RCF investment guidelines insist on using equity or quasi equity financial instruments, while most of the operations were funded through subordinated loans, subordinated only to IDC with special features such as principal and interest repayment schedule subject to cash flow availability.

While in practice, these loans did not provide a similar support as real or quasi equity, in practice, they achieved the intended support since most of the projects either were successful and the beneficiaries did pay back the loans earlier, or they faced difficulties and the outstanding amount at the end of the loan period will most probably have to be treated as quasi equity anyway.

The mission did not identify any investment which in practice proved just profitable and where effective equity would have made a difference. The high risk and high development nature of the projects supported did not require fine tuning of the financial structure.

The "balloon" resulting from the postponement of interest and principal repayments for the enterprises with insufficient cash flow will have to be negotiated and transformation of the due amounts into equity could probably be an option for continuing support of the viable enterprises.

The fact that most loans were only subordinated to IDC financing again was not that detrimental to the business funded, since commercial banks were usually not involved in the support of these high risk operations.

Finally, it appears that the initial recommended equity financial instruments for high risk developmental project might be a theoretical view and that subordinated term loans with significant grace period and/or automatic delays in the repayment of principal and interest when cash flow is insufficient provides the necessary financial support.

The main issue in this regard seems to concern the management support usually associated with shareholding which did not sufficiently accompany the management of the projects at the beginning. BSS providing short term consulting support could not provide the kind of hands on support that a number of the investees seemed to have required.

3.2.7 Pricing

Pricing has been initially fixed to produce an After Tax Internal Rate of Return of 10 %, so as to maintain the nominal value of the Fund, but it soon appeared that it was not competitive compared to other development financing facilities made available by IDC and also proved too high a burden on the beneficiaries.

Also, initially, most RCF facilities were interest based without the benefit of equity upside in case of a successful investment.

The pricing levels and structure were amended over the years to address the above issues. Global interest rate was reduced to a gross[60] IRR of 10 % p.a. with half of the interest structured as an upside based on a percentage of the profit or turnover, computed as per the budget, further to active EIB involvement on this issue. It was recognised that such IRR should allow the Fund to maintain its nominal value over time.

While this scheme did not provide for the sharing of higher profit in case of very successful projects, the mission confirms that the pricing structures used met the requirements of the project, keeping it simple and affordable, while maintaining the value of the fund.

3.2.8 RCF financing leverage and catalytic impact

The expected leverage to be achieved by RCF was a minimum of 100 %. This has been widely exceeded, reaching about 300 % or more, through the Direct channel thanks to IDC’s involvement or through the Niche Fund channel, thanks to the co-investors in the Funds. It must be pointed out however, that due to the failure of the Third Party channel, the commercial financial sector did not participate in leveraging RCF funding.

The Niche Fund channel is a special case whereby the RCF investments were catalytic in attracting public financial investors to the Agri-Vie and the Evolution One Fund, both funds having included socio economic criteria linked to RCF investment guidelines. The fact that some of the final investees did not meet some of the criteria, mitigates this apparent leverage. The case of Utho is different in as much as it did not attract private investors.

It is difficult to assess the catalytic effect of RCF as far as financial support to the projects is concerned. It is however the opinion of the mission, based on a number of investees visited and assessed that without RCF involvement, the IDC would probably not have financed a number of the “investees”.

On the Niche Fund channel, the RCF investments in the funds have most probably helped Agri-Vie and Evolution One attract further investors, especially at the time when the Venture Capital Fund industry in South Africa was still at the development stage.

The case of Utho Capital Infrastructure Fund is different in as much as the other investors in the fund are only Khula and the fund manager itself. The positive point however, is that a new Fund Manager, fully BEE has been supported.

Finally, the main weakness rests with the failure of the Third Party channel which did not manage to enlist the cooperation of the private financial sector to enlarge the outreach of the RCF programme.

[60] The fact that RCF profit might not be subject to tax would mitigate this factor if this is confirmed in the future

3.2.9 Effectivenes and adherence to investment guidelines

Based on the assessment of 63 investees, the mission confirms that the investment guidelines were effective in supplying development finance to the targeted businesses.

In most of the projects funded, guidelines have been adhered to, despite the real challenges to identify proper BEE businessmen with financial means especially in the poorer regions of the country.

Requests to modify the guidelines only concerned the increase of the “cost” per job and some slight amendment regarding a couple of projects where leverage did not reach 100 %.

The mission is satisfied that despite the challenges, the important BEE shareholding, BEE management and BEE employment covenants were usually met, except for a few cases when the BEE shareholding cum management were met through important artificial Workers’ Trust share financing, in the case of Amathole Berries and Primolitos.

Box 7: The case of MAZWE rejected RCF credit application

Mazwe is a successful Micro Finance Institution supporting women, with a dual focus on consumer micro finance as well as development micro loans. In 2008, the MFI approached IDC to obtain a ZAR 10 million equity injection (which would have been provided by RCF) and a ZAR MT wholesale loan, both to finance its expansion, especially after having signed a contract with the Passenger Rail Agency of South Africa (PRASA) to provide micro loans to their employees.

The credit application was rejected on the basis that there was no significant direct employment creation and that a significant part of the activity was non developmental.

Financial support was nevertheless organised by IDC, using the Women Enterprise Development Fund to replace RCF.

It is agreed that MAZWE was outside the investment guidelines, whereas, job creation could only have been expected at the end beneficiary level, through development funding granted to micro entrepreneurs.

Despite the fact that some MFIs might have real development objectives, the mission would not advise RCF to finance MFIs, being of the opinion that MFIs are very special enterprises whose management and process need very special skills and capacity.

SEDA whose activities encompass supporting MFIs, should be better equipped to support this segment of the market.

3.3 SOUND MANAGEMENT AND VALUE FOR MONEY (EFFICIENCY)

In this section, the efficiency assessment concerns not only the project team responsible for the management and implementation of the Programme, but also the other stakeholders involved in the project Governance.

3.3.1 Project steering committee (PSC)

- No specific issues related to the PSC role and function. Its composition is widely spread and provides access to a large spectrum of competence. It is regretted that no commercial financial institution representative was involved (apart from the Banking Association) to increase the chances of the Third Party channel's success.

- As already mentioned in this report, it is regretted that the PSC did not require the setting up of yearly work plans by RCF which could have ensured that the objectives for the year are well defined and allow for benchmarking the results.

- Finally, it is regretted that the PSC did not insist to have a better global view of the RCF actual performance in terms of social development impact as well as the actual financial position of the fund globally at least on a yearly basis, based on a thorough analysis of the portfolio which was only concluded in May 2010/11, with involvement of the EIB at the design level.

3.3.2 IDC management of the programme

- IDC has chosen the option to have RCF as an administrative department taking a back seat in the relationship with the beneficiaries. This management structure had the advantage for RCF benefiting from the capacity of the various IDC departments, be it through the sectors, the risk management, the post investment monitoring or the work out and restructuring departments. <u>With hindsight this decision proved relatively efficient as far as the direct channel is concerned, while it implicitly restricted RCF support to IDC clients only; the investments through the Niche fund channel, managed directly by RCF allowed for non IDC client support, albeit with the RCF representative on the Funds investment committees being IDC managers.</u>

- RCF has been keeping track of the proposals channelled by IDC to RCF for the last couple of years. This confirms that the number of potential clients referred to RCF by IDC was much lower than anticipated (300 per annum, revised downwards to 450 over the duration of the programme, i.e. about 70 per annum); reasons mentioned being that RCF was more costly and more restrictive as far as its covenants were concerned than other facilities managed by DFD. In fact the anticipated number of proposals to be received by RCF was initially widely off the mark, having in mind that the whole of IDC usually contracts about 300 deals per annum, but more importantly, the purpose of the Facility (and therefore the covenants) was particularly challenging as already indicated which explains the difficulty to identify worthwhile projects meeting the requirements.

➢ IDC’s effective management of the RCF financing was not always as effective as it could have been, even if the RCF supported enterprises were of a high risk nature.
It is difficult to list the deficiencies in the risk appreciation reviews; however, based on a few number of cases reviewed and visited by the mission, with the benefit of hindsight, the following weaknesses were spotted as contributing to the underperformance of the enterprises supported:
- Absence of real BEE management with professional expertise in the sectors concerned; the BEE requirement sometime provided through Workers’ Trust support was no replacement for the absence of a BEE effective shareholder cum manager;
- Absence of a knowledgeable partner when the process required special expertise or to ensure swift off take of the production;
- Absence of a sufficient pilot phase when the project implied new developments;
- Absence of contacts with and/or incentives for commercial lenders to ensure their involvement in due course in the project;
- Failure to deepen the opportunities for the investees through building networks with other State Owned Enterprises (SOEs) or working with corporates that are running BEE supplier development programmes.

Similarly, the following strong points have been noted in a number of cases:
- Structure of the financial support as a project loan, based on a significant supply contract(s) from a reputable institution, giving time for the enterprise to establish its operations and diversify its clientele outside of the initial contract;
- Presence of a strong partner involved in the business, such as a professional franchiser or a larger group as a significant shareholder.

Box 8: The case of Amathole Berries compared to Agni Afro Asia

Amathole berries, promoted by a white businessman not experienced in agriculture, had a large agricultural development project in Eastern Cape Province to produce blueberries with a high BEE employment component.

Agni Afro Asia was promoted by several BEE businessmen active in the collection of scrap metal, to develop the processing of the scrap metal, adding value to the production, with a significant secondary impact at job creation with scrap metal collectors.

Both projects went ahead, the first one without significant BEE involvement except for the Workers’ Trust 40 % shareholding entirely refinanced by RCF, 40 %equity by IDC, and no partners with expertise in the growing of the blueberries; the second project secured the participation of a large Indian group, (further to RCF refusal to intervene without a partner providing experience with process) with expertise in scrap metal processing, which also provided 40 %of the equity. The foreign investor presence in Agni Afro Asia allowed the project to dispense with the RCF initially projected support.

In both cases, the projects benefited from training and BSS support, in the second case through a consulting firm, the purpose of which was to support the BEE shareholders in their negotiations and running the operations against a more experienced foreign partner, while the Blueberry project dispensed substantial training to its BEE workforce.

At present, Agni Afro Asia project is fully on track while the Amathole Berries project is impaired although it does not appear on IDC's list of impairments; only solution being to find a strong partner experienced in the sector to take over the project, without any local BEE partner to accompany a possible renovation.

As a lesson learnt: RCF's credit refusal could lead to an improved project structure which is conducive to success, while RCF support, if misguided, could produce failure and duress for the beneficiaries.

- As already pointed out in the mid-term review, the IDC management fee appears low compared to the effective cost of managing the programme. However, the support effectively given to IDC financing in terms of risk support does provide some extra compensation difficult to assess. The fact that the IDC management fees are linked to the reflows introduces a welcome incentive to have the fund perform satisfactorily.
- Finally, the fact that RCF is part of a wider department, where officers are responsible for various funds did not allow having a precise estimate of the management costs involved in managing RCF compared to the work load. RCF does maintain analytical accounting re RCF operational costs and IDC fees (CF. Box 9: RCF operational expenses and IDC fees). The number of staff in the DFD department: 33 persons, managing 13 different funds for a global amount of ZAR 17 billion points however to an efficient cost/benefit ratio. Furthermore, a management fee of 10% of reflows for a 12 year Fund means less than 1% per annum, which is on the low side, compared to the Venture Capital industry's usual fee structure.

Box 9: RCF operational expenses and IDC fees

	Actual FY 2008	Actual FY 2009	Actual FY 2010	Actual FY 2011	Actual FY 2012	Actual FY 2013	Budget FY 2014
STAFF COSTS	5,527,200	5,454,120	6,756,120	7,153,834	6,628,751	7,540,776	8,779,549
SEMINARS & TRAINING	91,440	109,644	99,900	103,796	107,740	72,774	76,922
TRAVEL COSTS	246,000	194,181	354,500	222,866	199,830	70,000	73,990
CAFETERIA	16,575	49,009	38,080	39,565	37,445	38,800	41,012
OFFICE COSTS	355,328	387,308	350,104	474,668	539,401	569,607	735,869
COMPUTER COSTS	190,344	207,475	218,064	263,050	317,617	335,404	419,687
PANEL	169,000	81,000	129,107	221,745	181,242	262,742	277,718
OTHER LEGAL & AUDITS	63,840	67,926	78,778	81,850	114,260	89,718	32,469
MARKETING	261,000	284,490	303,551	376,099	450,391	140,000	147,980
INFORMATION RESOURCES	5,079	7,344	13,080	13,590	14,107	14,897	15,746
RCF 2 ANNUAL MONITORING			100,000	400,000			600,000
CONTINGENCY							280,024
TOTAL EXPENSES	**6,925,805**	**6,842,696**	**8,441,283**	**9,051,063**	**9,057,184**	**9,134,717**	**11,480,965**
Management Fees (RCF 1)	2,250,378	1,592,114	966,477	326,384	191,274	215,534	0
Management Fees (RCF 2)	107,675	243,888	563,549	467,351	81,280	730,875	0
Total Management Fees	**2,358,053**	**1,836,002**	**1,530,025**	**793,735**	**272,555**	**946,409**	**0**

Source: RCF 2012 annual report

3.3.3 Cost per job created and programme effectiveness

Despite the absence of such measurement by the project, the mission has computed the following rough estimate:

Cost of the concessionary funding: maintaining the nominal value of the fund, over the average duration of its support to investees estimated at seven years represents a missed income estimated at 20 %per annum i.e. based on an average outstanding of ZAR 500 million, a cost per annum of about ZAR 100 million.

Compared to the creation of 6,000 jobs, this represents a cost of about ZAR 17,000 per job created per annum. If one considers that the indirect number of jobs created per each project is equivalent to the direct jobs created by the project itself, the yearly costs can be estimated at half the mentioned amount.

Another way to estimate the cost of the jobs created would be to compare the annual cost of the programme to the number of jobs due to be created by the projects funded during that year, i.e. a once off cost of ZAR 100,000 per direct job created (on the basis of about 1000 jobs created per annum), or half that amount if indirect jobs are considered.

It would be interesting for RCF/IDC to make a more precise computation of the cost per job created, taking into consideration the effective number of jobs created every year compared to effective funds allocated and the real concessionary costs of the financing provided.

<u>It is difficult to compare this rough estimate with the cost per job created of other programmes on which the mission does not have precise data. The National Treasury and the European Union may be able to compare the various programmes they supervise/fund to assess the relative efficiency of RCF with regard to job creation.</u>

3.3.4 EIB involvement

- It is widely reported by the RCF team that the involvement of EIB was positive in terms of capacity building and learning process for IDC as far as fund management is concerned. It is difficult to quantify such successes provided through on the job involvement, which translated into thirteen specialised development Funds being created within IDC, more or less on the RCF model for a total amount of ZAR 17 billion.

- Reporting by the EIB about the project progress through its yearly reporting was comprehensive despite its weaknesses as far as the global evaluation of the fund socio economic and financial standing at any one time, mostly represented by the difficulty to assess the value of the payments relegated to the end of the loan duration when “investees” cash flow was not sufficient. It is regretted that recommendations by the EIB regarding this reporting issue, notably the split of the reflows into four lines: capital, interest, upside and bullet were not taken into consideration.

- It is regretted that the management fee of the EIB was fixed as a monthly amount regardless of the results of the Fund or of its involvement. It did not incorporate success incentives, which could have taken various forms, at the socio economic level, at the financial level or at the Third Party channel level, or a combination of those.

- The physical distance between the EIB and RCF did not appear to reduce its efficiency. The numerous trips to South Africa and the frequent telecommunications allowing for a close interaction between the two institutions.

3.3.5 Post monitoring issues

- The fact that the follow up of the “investees” resides with the Post Investment Monitoring Department (PIMD), or the Work Out and Restructuring Department (WRD) in case of impairment, does not allow for a close and direct involvement of RCF in the follow up of its clients. The fact that PIMD does not systematically produce a yearly review of the “investees” performance in term of socio economic and financial results does not allow RCF to assess comprehensively its portfolio performance easily.

- The RCF facility to be used as equity or quasi equity support did provide a kind of “first loss” buffer to IDC and other lenders in case of failure of the projects due to RCF subordinated loan characteristics. Should the “investees’” situation translate into cash flow deficiency, IDC would again benefit from RCF funding buffer since RCF principal and interest payments were usually only due if the cash flow was deemed sufficient. In such cases, the amount due would be postponed to the end of the loan duration.

  Should the projects stand a chance to survive, provided some loss is taken by RCF (in exchange for equity?), there might be a conflict of interest between IDC and RCF as to the proportion of the loss that each funding party should bear, since IDC is in fact managing the commitments of both entities. It is however foreseen that this conflict of interest issue should be easily solved in practice.

3.4 Achievement of wider impact (Impact)

3.4.1 Direct impact

RCF 2 has played an important role in supporting HDP controlled enterprises, creating opportunities for lower level SMEs to participate in the economy; most importantly RCF 2 has unlocked blockages regarding access to funding. It is however, regrettable that learnings from the experiences gained during the implementation of RCF have not found a way of formally feeding back into the SME development policy space.

Paragraph 2.3 has already discussed the direct socio-economic results of the RCF 2 to investees in terms of the number of jobs created, SMEs empowered and HDP developed to name just a few of the indicators. These objectives have to a large extent been achieved and in some areas such as employment creation, targets should be exceeded provided the investees remain on track.

However, the review team were concerned with the quality and reliability of data. In some instances the data for indicators was not updated prompting the review team to rely on data which is out of date. It is thus difficult to give a complete and accurate picture of current status of the programme in the absence of reliable data. It is recommended that through a yearly portfolio review, the effective impact of the results achieved be examined to draw lessons for the future.

3.4.2 Indirect impact (including at the Government strategy level)

The most important indirect impact is the creation of the Development Fund Department in IDC which was a major transition and transformation from the Risk Capital SBU, a unit that had previously mainly focused on managing RCF. Through managing RCF, IDC acquired skills and knowledge in fund management and as a result the new SBU, DFD has been mandated to manage a range of off-balance sheet funds as well as IDC ring-fenced on balance-sheet Funds, thirteen in total amounting to ZAR17billion.

Another indirect impact is the introduction of Business Support services within IDC which was a direct result of RCF. Previously IDC did not provide business support services but due to RCF, the institution now has a dedicated team responsible for business support for the whole of IDC. Through this unit, IDC now conducts ex-ante a business support needs assessment on all its applications and upon approval where such needs are identified, the team engages and appoints external service providers to deliver the services on a cost sharing basis and the BSS unit monitors such interventions.

Over and above these notable impacts, RCF 2 has also had an indirect impact on the IDC in the following manner:

- Based on the lessons learnt, IDC is now able to support SMEs in an equity environment;
- RCF propelled the SME agenda within the IDC;
- Allowed the IDC to do investments in Funds through the niche fund channel;
- Up sides allowed the IDC not to just take a share in the business but to benefit from exceptional successes. Some of the IDC funds such as the Women’s Entrepreneurial Fund also now include an upside;
- Enabled the support of a small niche fund, Utho Infrastructure SME Fund that is fully B-BBEE owned and managed by an HDP woman.

One other indirect impact is the strengthening of the relationship between IDC and EIB which translated into capacity building for both parties.

3.5 Likely continuation of achieved results (Sustainability)

3.5.1 Revolving issue

RCF 1 has not been revolving in as much as its reflows have not been utilised for new investments/lending. IDC preferred to use RCF 2 funds for the new operations, so as to be able to secure the drawdown of the three tranches made available under RCF 2.

RCF 2 reflows similarly have not been used for new investments since the programme has still some funds left for investment from the third tranche.

Due to the need to capitalize the Technology Venture Capital Fund, ZAR 100,000 of the RCF 1 and RCF 2 reflows were allocated to this other fund managed by DFD.

The decision to apply the reflows either to RCF revolving operations or to other Facilities is a political decision based on the respective merits of the Facilities’ objectives, taking also into consideration the commitments vis a vis the EU as to the funds application.

The revolving issue for RCF 1 and 2 is described in our views for the future of RCF in Paragraph 3.5.3 thereafter

3.5.2 Sustainability

The sustainability issue can be considered at three levels: the likely development of the enterprises funded and supported, the continuation of the Risk Capital Facility and the capacity built at the IDC level.

- At the investees’ level

It is difficult to draw any significant lessons from the RCF 2 investees, their development, achievements and prospects having not been reviewed so as to have a global view of the "investees" development prospects, except for the 2010/11 global portfolio review, which was not kept up to date since, and which did not assess the financial viability and financial value of the "investees".

Based on a sample of the investees assessed and visited, the prospects for development can be estimated as follows: about 25 % of the enterprise funded will have an above budget growth pattern, 25 % will have a growth pattern in line with their budget, 25 % will struggle and some will disappear over time, while about 25 %will disappear. These rough estimates are in line with the project's own estimates which considered that about 30 % of the RCF commitments will be impaired.

However, it is important to note the observation made in the 2010 RCF 2 Annual Monitoring report[61] that excluding the Niche Funds, there were 11 main contributors to the potential growth of the fund and a failure of 50% of these investees would result in a 20% overall write off of the fund which could significantly impact on sustainability.

Sustainability from RCF 1 performance having a longer view of the investees has not been assessed by RCF team recently; only eleven enterprises are still invested (Cf. Annex 7.3).

- At the IDC level

<u>The fact that RCF was originally a Department of IDC managing only one fund: RCF 1 and that ten years later, the RCF Department is managing thirteen funds for ZAR 17 billion, built on the same structure as RCF is proof to the capacity building brought by the programme to IDC and the sustainability of the proposed model.</u>

Furthermore, the institutionalisation within IDC of the Business Support Services to its clients, within a full-fledged department again points to success of the RCF grant component as an added support to the lending tools. This is however, subject to further study of the BSS's effective impact on the beneficiaries, which is difficult to assess in view of the recent deployment of BSS.

- At the RCF level

The RCF funds should maintain their nominal value in ZAR and should therefore be able to use the reflows to continue their activities with a challenging target, i.e. BEE controlled enterprises with a BEE management and employment impact including in the poorer regions of the country, as per the assessment of the RCF team.

However, this prospect is still subject to the repayment of the "balloon" by a number of clients whose cash flow has been insufficient to pay interest and/or principal when due. It is regretted that RCF has not reviewed more precisely the situation in this regard and the

[61] 2010 RCF 2 Annual Monitoring Report-Clients Assessments

mission is not able to confirm that the expected gross IRR estimated at 5.4% per annum for the fund could be met.

The « balloon » is the principal instalments and interest due and accumulated which could not be paid in time due to weak investees' cash flows and which were therefore pushed back to the end of each loan duration. It has not been possible to have an idea of these amounts which most probably bear most of the risks, unless a client per client review is organised, as it should be done at least once a year. The 2010/11 portfolio review subcontracted to a consultant did not assess the financial viability of these "investees".

The evaluators estimate that 60 % of the "on track" clients have not been able to pay back instalment and interest due to insufficient cash flow, based on the fact that effective reflows only represented about 40 % of expected reflows in the latest quarterly reports.

If one estimates that 40 % of the portfolio is not on track (in value terms) and that 36 % of the portfolio repayments have been pushed back to the end of the facilities, only 24 % is "current" at this time. It would be interesting to have a better view of the clients with accumulated amounts due and start assessing what could be the forthcoming rescheduling/renegotiation of the facilities.

The erosion of the actual value of the funds over time through inflation, concessionary interest and high risk profile is an accepted feature of the programme; it would be interesting to better assess the evolution of the real available amount over time.

3.5.3 RCF 1 and 2 future within IDC

The target of RCF, as defined in the investment guidelines is the result of an economic and political decision, based on the very special post-apartheid situation of the country, whereby the costs of the programme in term of concessionary interest and high risk financial support is warranted by the social and economic requirements to support black economic empowerment. This target is fully in line with the B-BBEE Government policy targeting support to the HDP.

Within this context, and having in mind the challenging investment guidelines already described at length, the mission recommends that the RCF programme be continued as long as BEE special support is required, using the reflows to support the continuation of the facility.

Possibly, in view of the identified successes showed through "project" finance type of support, RCF may privilege such approach in its support to the HDP SMEs, developing its focus along lines similar to the proposed Value Chain approach detailed in Paragraph 6.2.2.

The above recommendation cannot take into consideration the competition for funds to support the different social and economic needs of the population in South Africa, such as the need for technology development, for youth support, for support to the poorer segment of the population etc. It is not the responsibility of this mission to address these complex political decisions, which translates into various fund allocations.

3.6 MUTUAL REINFORCEMENT (COHERENCE)

<u>RCF 2 achieved success in aligning its outcomes and activities with other EC, South African government and donor funded programmes.</u>

3.6.1 With other EC programmes

The RCF is inherently complementary with the Employment Creation Fund in that it supported creating jobs for the economically disadvantaged as well improving capacity and skills in the productive sectors of the economy. However, at an operational level, the dti seems to have failed to effectively coordinate the two programmes as there was no attempt to start a discussion forum to glean lessons learnt and best practices and possibly find ways to harness common positions on future collaborations with regards to SME development and employment creation initiatives.

3.6.2 With other donor programmes

There was mutual reinforcement between the RCF 2 and other donors. For example RCF 2 co-funded two niche funds with other donors as shown in Table 13: Other Donor commitments to Niche Funds below:

Table 13: Other Donor commitments to Niche Funds

Niche Fund	Donor	Amount (ZAR)
Agri-vie	Kellogg Foundation	140 million
Evolution One	IFC (World Bank)	200 million
	Finn Fund	80 million
	Norfund	80 million
	Africa Development Bank	100 million
	Swiss Investment Fund for Emerging Markets	80 million

Source: Information extracted from Investee Reports

However, apart from co-financing the Niche Fund initiatives there does not seem to be an attempt by the above donors to share lessons learnt on the overall impact of SME development in South Africa.

Other development cooperating partners whose programmes have been complemented by RCF are the USAID, KfW who have been providing funding support for SME development. USAID has been working with private banks to provide credit guarantee schemes.

3.6.3 With other Government Institutions

The evaluation came up with mixed findings on the issue of coordination between RCF and other SME support institutions as explained below:

- SEDA: No collaboration exists despite the fact that they are providing non-financial support (BSS), which is very similar to IDC‘s offering. It is managing a number of programmes to support SMEs in non-financial areas which could be enhanced through access to the financing arm of RCF/IDC.
- NEF: There is a good cross referral system as well as co-funding between the two institutions. Currently there is a deal for a hotel that has allowed the two to work together because there was an equity component required for the BEE partners. NEF provided R30 million.

3.6.4 With other IDC development finance programmes (regrouped in DFD SBU)

There seems to be little cooperation between SEFA (now a subsidiary of IDC) and the RCF/IDC although executive members from each organisation sit on each other’s boards.

However, on a positive note it should be noted that the RCF unit has grown and is currently managing 13 funds worth ZAR 17 billion and the funds are doing well so far. The staff has been increased from 9 to 33. The unit’s name has also changed from RCF SBU to Development Funds Development. There has been very strong coherence between these funds and RCF.

4 VISIBILITY

The issue of visibility has to be considered at two different levels: i) in the EU perspective, whereby EU programmes must have visibility and promote the understanding of EU development support in the countries of intervention, ii) in the South African Government perspective, to ensure the transparency of its policy and iii) at the level of the Programme itself for the information of the (potential) beneficiaries.

- Visibility at the EU level

The main issue arises from the fact that RCF 2 is structured as a Sector Budget Support Programme (SBSP) and therefore the funds are allocated to the Government which is the owner of the funds and the implementer.

The main challenge, however is that the EU Budget Support Guidelines[62] issued after the design of the project cannot really be used in retrospect as a yardstick by this evaluation to make an assessment of whether or not there was adherence to the guidelines and in any case, neither the FA or the ODA guidelines makes any reference to visibility requirements during implementation and as such it becomes more of a courtesy on the part of the partners to acknowledge the contribution made. It should be noted that the EU Budget Support Guidelines does not expect beneficiaries to publicise the support rendered but instead refers to EC's own internal publicity measures related to the FAs and performance reviews as disbursement conditions and assessments in agreement with partner countries. The guidelines also refer to joint press statements regarding payments made and the results achieved. Consideration will be made on this point in relation to possible future activities.

This being said, it is regretted that in the vouchers, leaflets or other marketing documents made available to the public, to present the RCF programme, no mention is made of the EU significant financial support. Furthermore, the beneficiaries of RCF support were usually not aware that these funds had been granted to the SA Government by the EU, including the grant portion.

- Visibility at the beneficiary level

It is regretted that the support that the RCF is granting to its end beneficiaries is not made more visible, through the granting of some certificate or prize, showing that the beneficiary is financially supported by IDC/RCF, giving visibility and credibility to the beneficiary. One could even imagine that the beneficiaries could use signboards, inside or outside their

[62] Budget Support Guidelines, programming, design and management- a modern approach to Budget Support 2012

office, could use such “award” in their letterhead and promotional material, as suggested by one of the beneficiaries.

- Global visibility

It is also regretted that a public conference is not organised, annually for example, with the beneficiaries, which would provide an avenue to communicate about the programme, make it more visible, share experience among the beneficiaries and draw lessons learnt (Cf. Paragraph 6.1.2).

At such conferences, success stories could be profiled to provide examples to would be BEE entrepreneurs in the country.

Finally, it is also regretted that modern media have not been utilised to widen the outreach of the programme, the more so that one of the beneficiaries of RCF is a radio station which would welcome advertisement from such a reputable institution.

5 MAIN CONCLUSIONS AND KEY LESSONS LEARNT

- Sector Budget Support Programme with Project features

The decision to structure RCF 2 as a Sector Budget Support Programme (SBSP) with project type features and EIB support did achieve capacity building at the IDC level, proven by the extraordinary developments of the various funds managed by DFD. The dti's involvement through the MOA with IDC and its Chair of the PSC also provided useful feed back to the Department in its economic development policy understanding, as reported by the dti management.

As pointed out earlier, RCF provided an opportunity for SMEs that were previously excluded to participate in the economy.

The experience learnt at the policy level of unblocking access to finance for these SMEs has been invaluable.

Beyond this, it is not clear to the evaluators how else dti's or EDD's policies on SME development have been impacted through learning gained from RCF so far. Perhaps it is still too early for this to take off given the stages at which most of the investments are at. Measure need to be put in place quickly to capture the learnings as the programme is evolving to see how this can influence SME development policies going forward.

Usage of the SBS modality promoted ownership by South African Government institutions and was in line with the Paris Declaration, Accra Agenda and the post Busan aid effectiveness declaration.

- Finance instruments used: not an equity fund but a development finance risk capital facility

Facility is subordinated to other lenders, mostly IDC, thereby providing a risk buffer to these other lenders furthered covered i) by the clause whereby interest and principal repayment may be postponed until the end of the facility if the cash flow is sufficient to meet RCF repayments schedule and ii) by the remuneration upside of the facility linked to successful development by the enterprise. It therefore takes a quasi-equity risk, being exposed to a kind of “first loss” position if business fails. In that sense, it achieves its purpose of being a risk capital facility supporting high risk enterprises and providing comfort to other lenders.

The arguments developed in the MTR that real equity would be more supportive of the enterprise was not a real issue in practice since either the enterprises were very successful and repaid easily the RCF facilities, or they failed and could not repay anyway.

The advantages of real equity as opposed to subordinated loans would be important mostly for high growth businesses needing their whole cash flow to finance their expansion.

- Leveraging private sector financing

More attention should have been drawn to this important issue, which would have given more outreach to the programme. The failure of the Third Party channel despite the efforts of the RCF team proves that it is a difficult goal. Because this is not an issue for the RCF team alone, IDC and the dti should have been involved at the highest level to try and advance this cooperation.

- Cooperating with other SME support programmes

Relationship with SEDA seems to be weak, whereas it is implementing a number of SME support programmes which could benefit from development finance, since these programmes usually do not include a funding component.

SEFA should also be an important partner for RCF, providing prospects to be funded, subject to further negotiations.

Cooperation does not seem to have been organised with International Development Finance Institutions supporting directly or indirectly SMEs' access to finance, with a view to try and increase the outreach of the RCF, except through the Niche Fund channel.

- Maintaining nominal value of RCF over the period of the programme

This objective is fully understood and accepted, the depreciation of the value of the Fund representing the development costs associated with the Facility covenants. However, it is regretted that the RCF team does not provide a better assessment of the value of its investments during the life of the Facility, especially linked to the value of the "balloon" accumulated at the end of the facilities granted, providing some lessons learnt linked to the difficulties met by some of the investees.

<u>Having this uncertainty in mind, the pricing finally arrived at: gross IRR of 10 %, made up for a significant part of a percentage of the turnover achieved is coherent with the development purpose of the Facility.</u>

- BSS

Business support needs and implementation must continue to be improved on both pre and post investment. Impact measurement, a difficult exercise should continue to be researched while the availability of BSS to critical partners of the "investees" should be allowed, eventually with some financial participation of the "investee" itself.

Niche Funds have no incentive to support the adoption of BSS by their investees due to the existing conditions; flexibility could be introduced by providing an interest free loan to finance the beneficiary 50% own contribution; Niche Funds managers themselves do not have access to BSS to improve their capacity.

- Documenting Best Practices (Case Studies)

This could be viewed as a missed opportunity for RCF, successful exits as well as good investments that are meeting the development indicators should be documented as case studies. The IDC only recently started a Knowledge Management Unit with a Lessons Learnt Portal that should identify critical themes from all lessons.

It must be noted, however, that the RCF Write off reports includes a standard paragraph on lessons learnt.

- Delays in the disbursement of the funds

Main reasons for the delays appear to have arisen from the negotiations to finalise the various MOAs among the stakeholders, without the involvement of the private potential financial partners like the financial institutions which should have joined in through the Third Party channel.

In this regard, attention is drawn once more to the importance of having the private partners associated to the design of the programmes from the start to ensure that the objectives and the delivery processes meet their requirements without creating conflict of interest.

- Flexibility in the investment guidelines

Despite RCF complaints about the rigidity of the guidelines, some flexibility has been introduced on a limited number of criteria with the active support of the EIB. Because all special cases can never be identified in advance, the PSC should have had the power to waive some of the requirements, on a case by case basis, under duly justified arguments.

In this regard, the number of jobs to be created was usually limited to the direct number of jobs provided by the enterprise, without taking into consideration the indirect jobs to be created, and possibly in the case of developmental Micro Finance Institutions, the potential job creation at the end beneficiary levels. This in fact excluded MFIs from being targeted under RCF.

- Cost per job created

“Cost” per job as defined in the RCF investment guidelines is in fact a maximum RCF “investment” per job created, which implies that high capital intensive industries could be excluded, or that RCF involvement/risk shall be limited to a maximum, indexed on the number of jobs created. The flexibility which was introduced in this respect is welcome. It would have been interesting to also compute the total investment per job created to possibly draw lessons based on the capital intensity of projects versus job creation and sustainability.

An analysis of the type of projects and associated risks with the higher "cost" per job created would have been interesting.

Real cost of job creation should in fact be computed differently: Cost of the concessionary finance given by RCF over the estimated duration of the investment, compared to normal cost of finance, divided by the number of job created… This would allow comparing the cost efficiency of the programme per job created to other job creation focused programmes.

- RCF operational process

The principle of RCF's reliance on other IDC departments allowed it to benefit from their expertise, while taking a back seat in its client management follow up. The mission concurs with this approach which had more advantages than inconvenient.

An unfortunate result of this approach, however, is the weak empowerment of RCF staff vis a vis their clients, behind PIMD or the WRD. As a consequence, the RCF depends on IDC departments: marketing, risk assessment while post investment reviews are not done systematically on a yearly basis. RCF is therefore in a weak position to conduct global portfolio review. The latest one having been subcontracted to outside consultants in May 2011.

Furthermore, the front role played by IDC discourages the non IDC clients to be considered, especially the smaller enterprises.

Given the capacity challenges within IDC's Post Investment Monitoring Department, it has not been possible to monitor regularly all the RCF 2 clients. Measurement of the development impacts further down is going to be difficult without an accurate and up to date data base for the portfolio. The database developed by EIB could be taken over by RCF and utilised to track progress and it is important to perform annual assessments on all the clients with the results being systematically reviewed.

Regarding the Third Party channel, as already mentioned, it is regretted that IDC did not take a more active role to support RCF efforts in this regard. Increasing the outreach and impact of the programme through cooperation with private financial institutions should continue to be explored, at a higher level.

- Characteristics of projects financed

Further to the review of some investees, it appears important to have “real” BEE shareholders cum managers involved in the running of the enterprises, not counting Workers’ Trust as providing the HDP shareholding covenant, due to their usual lack of management experience and effective ownership of the shares (until the loan used to acquire them is repaid after many years), depending on the role of the trustees in this respect.

Also, the importance of going through a pilot phase when considering business developments implying new processes should have been relied upon more seriously, especially for the larger projects in new development areas.

The effectiveness of supporting new businesses in the form of project finance linked to a specific contract with a reputable large enterprise, reducing start up risks has been duly appreciated in a few examples; such a process could eventually be upgraded into a more systematic approach in cooperation with large public and private enterprises, somehow similar to the BEE enterprise support requirements imposed on private businesses (Cf. Paragraph 6.2.2).

Financing Franchisees at the RCF level has produced mixed results. It is understood that IDC has decided to stop supporting such businesses. The evaluators do not support such extreme decision, especially in the poorer regions of the country where businessmen could benefit from the support usually associated with such structures.

Finally, the mission is fully aware of the importance of supporting enterprises in the poorer regions of the country despite the challenges it represents; linking such support with other programmes would help to identify such rare good cases of new developments.

- The special case of the Workers’ Trust financing

The few cases reviewed by the mission related to Workers’ Trust support showed that in the reviewed cases, such structures were utilised to increase the funding leverage of the projects, while apparently meeting the BEE shareholding requirement. In practice, this allowed the project to dispense with a real HDP shareholder involved in the management of the enterprise, increasing the financial leverage to unsustainable levels while pushing back into the distant future the repayment of the Workers’ Trust financing.

- Exit strategies

Due to the large number of investments where RCF repayments and interest that are due have been postponed (estimated at 60 % of “on track” investees), accumulating in a "balloon" at the end of the facility, some indication should have been tabled in the facility agreement with the borrowers as to how such repayment would eventually be organised, to prepare the client shareholders to the negotiation for repayment which might imply exchanging the overdue amount for equity and/or securing increased collaterals and/or extending the loan duration on improved terms and conditions.

- Catalytic impact and job creation per the different channel

<u>Catalytic impact must not only be assessed at the funded projects' level, which would not have happened without RCF, but also at the IDC level with the huge increase of funds now managed by the DFD under RCF type schemes. In that sense, RCF 1 and 2 are definitely a success.</u>

<u>Increased involvement of commercial lenders was however not successful; it remains an issue which should be tackled at the dti/IDC higher level in view of its importance to increase the outreach of all public financing programmes.</u>

The catalytic impact of RCF has usually been estimated especially at the Direct channel level. In addition to the submission of an application to the IDC credit committee, RCF also attached a separate cover sheet that captured additionality of the funding in the request for EIB approval. Going forward, it is recommended that a specific analytical paragraph to assess such catalytic role should now be inserted in each credit application in addition to the "cost" per job created information as EIB is no longer involved in the application process.

The catalytic role of RCF was more easily justified in the case of the investments in the niche funds.

Finally, it must be stressed out that a significant number of jobs to be created depends on a handful of clients. It is regretted that RCF does not follow more precisely the job creation impact of these few major investees.

- Visibility

Finally, the importance of providing visibility to the programme should also be highlighted, to attract more project proposals, but also to outline RCF/IDC support to the beneficiaries of the programme, providing the latter with visibility and consideration.

6 RECOMMENDATIONS

Based on the key issues and lessons learnt described in the preceding chapter, the mission makes a number of recommendations to the stakeholders in the RCF programme. Also taking advantage of the evaluators' involvement with the programme, and within the context and strategy of the Government, some initial recommendations are tabled for possible future support to SMMEs access to finance in South Africa.

6.1 RECOMMENDATIONS TO THE STAKEHOLDERS

6.1.1 Recommendation to the EC

- Devote more time to engage with the National Treasury to draw lessons learnt and ensure that other EU programmes such as the Employment Creation Fund continue to meet the Government development priorities and policies.

- Continue participating in the PSC till the end of the investment period and draw lessons on SME development when considering other planned private sector support programmes. In future ensure that the policy dialogue perspective which is a key tenet of Sector Budget Support is well ingrained in any similar programmes. Explore twinning, exchange visits between EU and South African entities that are involved in SME development support.

- Enlist the cooperation of the EIB, not only as an adviser/supervisor of specific EU Programmes when relevant, but try to find ways to leverage EU grant development programmes with the commercial financial sector and Development Finance Institutions, possibly using EIB attractive lending schemes.

- Engage the cooperation of the dti and IDC to ensure some visibility to the RCF support towards the general public as well as potential black entrepreneurs.

- In the future, the advisory and supervisory role played by EIB should be subjected to a tender process to ensure an open playing field and best value for money. Interest from commercial banks or other financial institutions might thereby be attracted to such programmes, increasing private public partnership.

- Involve key stakeholders both public and private institutions in the design of any future private sector or SME development intervention in South Africa.

6.1.2 Recommendations to the Government stakeholders (National Treasury, dti, EDD…)

- To assess the efficiency of RCF in terms of job created, it would be interesting to compute and compare the estimated cost per job created under the programme to the equivalent figure for other job creation programmes. The National Treasury which oversees a number of such programmes might have the information to assess such cost efficiency.

- To widen the impact of the programme, more consideration should be given to involve commercial financial partners in availing themselves of the benefits of development financial programmes at various levels; since this objective does not only concern RCF but all IDC development finance support, a high level working group between the dti, IDC and commercial financial partners should be established. It is understood that IDC is keen on joining in with commercial banks in its development finance efforts, and the DFD should be part of the exploratory workforce to address these issues.

- The PSC should also consider inviting from time to time private financial institutions to try and garner synergy with the financial institutions with a view to increase the outreach of the Facility.

- At least once a year, the PSC should organise a "learning workshop" and should invite the IDC's knowledge management/learning institute to present case studies on successful as well as projects that are under stress. Managers of such projects could also be invited to attend including representatives of other financial institutions that are involved in supporting SMEs.

- Finally, it is recommended to invite EDD to become a member of the PSC due to the role that they also play in SME policy development and since they are now IDC's parent ministry.

- In the future, during the programmes preparation phase all stakeholders should be included, especially the private financial institutions, to ensure that the objectives and the delivery process (Third Party channel) do meet the parties' requirements.

6.1.3 Recommendations to the EIB

Now that the EIB involvement with the RCF project is terminated, the recommendations listed hereafter might be useful, should the EIB consider further similar advising/supervising involvement or other cooperation with the EU:

- Because the EIB is involved with the support of SME access to finance through long term credit facilities granted to commercial banks in developing countries, it should be in a good position to support blending EU grants and development finance instruments such as RCF alongside its facilities to commercial banks, to ensure a wider outreach for programmes similar to RCF; in this respect, the mandate of EIB regarding RCF could have been enlarged to encompass the development of the Third Party Channel through the beneficiaries of its[63] long term SME credit lines.

- While the contribution of EIB to the RCF support is widely recognised and appreciated, it is regretted that it did not succeed in ensuring that RCF prepares yearly work plan and provides a more thorough analysis of the RCF portfolio situation, at least on a yearly basis, in financial as well as socio economic terms, so as to have a more accurate appreciation of the results and impact.

6.1.4 Recommendations to IDC

- Consider the possibility to increase the interaction with the commercial financial institutions to enlist their support for development finance, making the DFD special development facilities available to such institutions so as to widen IDC/DFD/RCF outreach. Organise a task force at the proper level, in close cooperation with the dti (see above) to address this issue.

- In the future, IDC and commercial lenders should be associated with the design of the development facilities ex ante, especially with the identification of prospective targets (investment guidelines) acceptable to commercial lenders and meeting the development criteria, while obtaining their agreement on the implementation process.

- While the creation and provision of BSS facilities to IDC/DFD/RCF clients is well appreciated, it is recommended that such support be made available not only to the beneficiaries but also to their main suppliers and out growers with the joint financial support from the IDC/DFD/RCF clients themselves.

- The management of impaired investment is a time consuming process. It is suggested that these difficult investments with a chance of survival, needing hands on management support be referred to a dedicated Management Support Department to be created within IDC, providing hands on management support to the clients with a chance of redress. Advice and back up could eventually be garnered from IFC Asset management Company schemes. Subject to further feasibility, such a pilot scheme could be tried with RCF clients.

[63] Or other DFIs SME wholesale credit lines made available to South African banks

- Ensure that the IDC filing system allows consultation of the client’s and IDC client related documents produced by the various IDC departments and SBUs by the RCF officers, easily.

- Ensure that PIMD has the necessary manpower to review annually the RCF “investees” re the social and financial conditions so that RCF has the information to conduct a global portfolio review based on these individual yearly assessments.

6.1.5 Recommendations to the DFD/RCF

- Define clearly and in writing the tasks and the responsibilities of the person in charge of RCF within DFD emphasising the important task of portfolio management and assessment.

- Ensure the preparation of yearly work plans for RCF so as to have objectives against which to measure performance, assess deviation from the plan and suggest remedial actions. In such plan, SMEs could be categorised in line with the classification provided by the National Small Business Amendment Act of 2003 and 2004, thereby providing a further benchmark regarding the characteristics of the investees.

- Ensure that at least once a year, the global performance of the programme is assessed, completing a portfolio and global performance review and computing the real impact of the fund by assessing the socio economic results and potential value of the portfolio, having in mind especially 1- the important “balloon” represented by principal and interest repayments pushed back to the end of the facilities granted and 2- the concentration of jobs to be created and number of shareholders on a handful of “investees”. The 2011 portfolio review contracted through an outside consultant was informative. It should be the work of RCF officers yearly based on information supplied by the IDC departments and niche funds as well as through on the spot visits. It is important to perform annual assessments on all the clients with the results being systematically reviewed.

- Consider creating a special category within the on-track investees by differentiating those up-to-date as far as principal and interest payment are concerned and those which have delayed there repayment obligations until the end of the facilities;

- Ensure that lessons learnt are regrouped in RCF quarterly or annual reports, the more so that “lessons learnt” is a standard clause on the clients’ write off reports. To regroup them in the reports would give them more pre-eminence.

- Prepare exit scenarios well in advance, together with the WR Department for the clients showing an important financial burden due at the maturity of the RCF commitment, so as to plan as much as possible for a solution allowing the clients' survival and RCF repayment.

- Organise yearly conference with beneficiaries to draw lessons learnt, show off success stories and give visibility to the programme and its EU funding source towards would be beneficiaries, making increase use of the media;

- Consider providing RCF beneficiaries with some visibility signs and award documents which could help their visibility vis a vis their clients and bankers, promoting the EU support visibility at the same time as well as through mentioning the EU support in the Programme marketing and information documents.

- Ensure that the filing system is improved to give easy access to the clients' and IDC clients' related basic documents such as the beneficiaries' business plans and the PIMD or WRD business reviews.

- Consider supporting the adoption of BSS by the Niche Fund investees by providing an interest free loan to finance the beneficiary 50% own contribution.

- Measure the total investment per job created as a complementary indicator of the capital intensity of the projects undertaken; also compute the real costs (in term of concessionary interest rate and higher risk taken) per job created to allow comparison with other job creation focused programmes.

- Include catalytic role assessment of RCF proposed commitments in each credit application, to justify its mobilisation by IDC.

- Review the effectiveness of supporting Workers' Trusts for high percentage shareholding, increasing leverage without real BEE shareholders and BEE management in the projects funded.

- Liaise more regularly with other programmes supporting job creation and SME support, especially the programmes managed by SEDA.

- With the support of IDC which might be interested for its other clients, liaise with large public corporations, to support BEE controlled enterprises which could benefit from suppliers' contracts with the financial support of RCF/DFD/IDC; this specific support by state owned enterprises like Eskom or Transnet or others could be formalised into an MOA with IDC, possibly in cooperation with the SEDA Supplier Development Programme which has the same objectives. One could even imagine a new specific fund for such developments, Cf. recommendations for the future in Paragraph 6.2.2 thereafter.

6.2 Recommendations for future financial support to SME finance in South Africa

6.2.1 Context

Within the context described in Annex 7.1 here above, i) considering that unemployment remains a crucial issue in South Africa, ii) considering that micro, small and medium size enterprises are the best conduct for employment creation and iii) that access to finance remains an important barrier to SMME development, it appears legitimate to retain improving access to finance as one of the focus of the Government enterprise development strategies.

The Report on the Review of Government Support for Small business, dated December 2011, prepared by the dti identifies a number of strategic areas to improve the environment for small businesses. Among the various barriers and related actions proposed, Chapter three described a number of proposals to increase the supply of financial support.

Some of the measures do meet with our recommendations for future support to SMMEs access to finance, based on our assessment of the situation as described thereafter.

6.2.2 Recommendations for future support to SMMEs in South Africa

As per the TOR, during the course of its evaluation, the mission has identified some area where support to SMME access to finance could make a difference.

It is recommended to continue the support of HDP SMEs through the RCF facility, using the reflows to provide risk capital finance. Opportunity to increase amounts available for such support should only be considered when the Facilities (RCF 1 & 2) will have fully used all the reflows.

The following proposed avenues to improve SME financial access are only very preliminary proposals to be fully researched in cooperation with all stakeholders with regard their objectives and implementation processes. Attention is drawn to the fact that these various initiatives do have some complementary impact, either for the small and medium enterprises or for the micro enterprises.

- Market segmentation

For an effective support, the SMME market should be segmented. The mission proposes to consider different approaches depending on the segment of the market considered:

- High growth potential SMEs, including start-ups, with a potential for high growth and high employment, which would normally only represent 1 % of the SMEs;

- Lifestyle SMEs with a limited potential in term of growth, but which constitute probably 95 % of the SMEs, and therefore their growth can be significant globally in both financial and socio economic terms;

- Micro enterprises, usually informal, with limited growth prospect and low employment, but which again represent important numbers, including most female entrepreneurs.

- High growth potential SMEs, including start-ups

High growth potential SMEs, including start-ups are already supported by a number of incubators, angel investors and venture capital funds, including IDC Venture Capital SBU.

It is not recommended to organise special support programme for this segment of the enterprises, its attractiveness to angel/seed funds not being easily improved by partial aid finance while grants already do support these operations through the various incubator programmes already implemented.

Main recommendation in this respect would be for IDC to try and increase the outreach of its Venture Capital Unit through the opening up of its VC Fund to commercial investors and links with the existing incubators in the country.

The current initiative of the Banking Association to establish an SME Equity Trust Fund is worth following up closely to see how it can be supported to increase leverage.

- “LIFESTYLE” SMES TRANSPARENCY

Access to finance for SMEs is not easy in South Africa as widely reported (Cf. Paragraph 1.3.5) mostly due to the lack of transparency inducing reluctance and high collateral requirement by the commercial banks.

Improving transparency for SMEs is normally a long process based on improving the management capacity of the SME owners, convincing businessmen of the benefits of transparent accounting vis a vis their banks and suppliers, despite the potential for tax increases.

A proposed indicative programme could be based on an extensive rating system for existing SMEs, developed by specialised institutions such as Dunn and Bradstreet, Standard and Poor’s Company, Global Credit Ratings company or other private information suppliers Such rating would not only give a mark on the SME rated, but would be based on an in depth review of the enterprises’ management and process, highlighting the strong and weak points, allowing the owners to have a professional assessment of their business and if communicated to the enterprises’ banks and suppliers, facilitating the risk assessment and due diligence through improved transparency.

To convince the SMEs of the advantages to be rated, a grant programme could be organised to co-finance 75 % of the initial rating costs during the first year (when the exercise is the most expensive), being reduced to 50 % during updates in year two (less expensive in view of the initial work undertaken the previous year) and 25 % for year three. Hopefully, the enterprise experience of the benefits associated with this rating system shall convince it of the benefits to be gained from such rating and will maintain it up to date in the future.

Blending the above described grant support to access to finance could provide increased incentive for the development of this SME rating scheme. This could take the form of cooperation with International Development Finance Institutions granting SME refinancing credit lines to commercial banks, making it a condition for the credit lines to favour rated SMEs.

It should be made clear however that such a scheme would mostly concerned “bankable” SMEs which cannot access commercial bank funding due to their inability to present transparent and clear financial information on their situation and development plans. Start-ups would not normally benefit from such credit rating assessment, not having reached a stage when past performance gives indication on the professionalism and capacity of the entrepreneurs.

This public private partnership, already under investigation by the dti has already been successfully developed in India through SMERA Ratings Limited[64] (formerly SME Rating Agency of India Ltd.), a joint initiative of the Small Industries Development Bank of India (SIDBI), Dun & Bradstreet Information Services India Private Limited (D&B) and leading public and private sector banks in India.

SEDA which is already providing SMEs with numerous support programmes at different non-financial levels, together with SEFA[65], could jointly manage such a programme, while the private sector shall be the main stakeholders to ensure its success. It is reported that a scheme with some similarities has been developed in Ghana[66].

An added feature of this programme could include for the rated enterprises benefiting from new bank support, a partial grant to finance a hands on support technical assistance covering the weaker aspects of the enterprises identified by the rating agency, including management training and financial reporting to the bank. Such a secondary scheme appears to have been developed with success in Tunisia, at a cost.

[64] Cf. http://www.smera.in/about/about.aspx
[65] Subject to these organisation capabilities in this regard
[66] Cf. http://www.sbksbi.com/blog/2013/6/18/business-development-services-ghana.html

Obviously, the above proposal is just an initial idea whose feasibility, like the other proposals, has to be assessed in cooperation with all the stakeholders: the SMEs, the financial institutions, the credit rating companies and the Business Development Services providers while a detailed study of the Indian model could provide useful lessons learnt in this respect.

- PROJECT FINANCE SUPPORT THROUGH THE VALUE CHAIN APPROACH

During the evaluation of RCF, it was noted that a number of the success stories concerned SMEs or start-ups which benefited from a significant contract from a reputable buyer, giving an opportunity to IDC/RCF to structure a kind of project loan, giving sufficient financial resources to the enterprise to honour the contract, based on the safety provided by the assignment of the contract proceeds. This exceptional contract and the financing attached to it allowed the enterprises to develop and grow other activities ensuring their future after the main contract is terminated.

Proposal would be to try and systematise such an approach with the main large public and private groups in the country, improving the production capacity in term of quality, cost, volumes etc. of their existing suppliers, providing through a RCF type of development Fund the required financing, secured against a contract from the main buyer. Such approach could even apply to new suppliers which would be supported to achieve the quality level to be considered as a supplier.

SEDA is already running a programme on this basis, since a few months, called the Supplier Development Programme, providing support to SMEs to increase their engagement with larger clients in terms of management capacity, productivity increase, technology upgrade or product development. The proposed programme should be associated with such a Supplier Development Programme to provide the required financing.

Again, SEDA and possibly IDC or SEFA, or even a private partner like one of the international audit firms, depending on the enterprises targeted and the capacities of these institutions could oversee and manage such programmes. Tied to this proposal is a suggestion made by ABSA about setting up an independent Enterprise Development Fund, major banks could contribute to such a fund that would support enterprises financed under the value chain approach. In addition, there could be a number of SMEs that can participate in the value chain and provide goods and services to SMEs that have contracts with state owned enterprises or other corporates.

A Programme providing identification of potential SMEs in collaboration with the large enterprises, needs assessment, technical assistance support and financial provision could be devised with the strong involvement of the financial institutions and the large groups willing to participate in the Programme, the main support needed from the Development

Partners being the grant support element to conduct the needs assessment as well as advisory on how to structure the project finance scheme on a wide scale involving both private and public institutions.

The EIB and other Development Financial Institutions SME credit lines channelled through commercial banks could even be harnessed to enlarge the financial support impact of such a scheme.

- MICRO ENTERPRISE IMPROVED ACCESS TO FINANCE

Micro enterprise development finance in South Africa is not a well-developed and successful instrument to provide access to finance to micro entrepreneurs. Consumer type of micro finance seems to crowd out development finance which suffered some set-backs recently.

The mission still considers the need to provide finance access to the micro entrepreneurs as an important economic and social success factor and therefore recommends that support to selected Micro Finance Institutions (MFIs) with the proper strategy be organised. It is suggested that equity investment together with strong Management support be provided, possibly associated with lending facilities from Development Financial Institutions.

Such support could take the form of a Development Finance Programme which could be managed under the supervision of SEFA or other private fund manager, in a format similar to DFD, or in the form of investment in an existing MFI equity fund which would target South Africa among other markets (due to the possible limited size of one single market), or if such Fund does not exist in the region, through the creation of such a regional specialised fund, with a very strong management and process support element.

The predominant component of such support should concern management and process development to ensure that the MFIs have the proper organisation, software and capacity. The institution which supports the MFI sector in South Africa is SEFA which absorbed SAMAF recently. It is not known if SEFA would have the capacity to manage such developments in view of its recent reorganisation.

As a side line to this MFI support, improving the Credit Bureau operations to include MFIs clients in its reporting would also help the sound development of these financial institutions. Finally, one could even see a link with the proposed formalisation of micro enterprises as suggested thereafter.

- SUPPORTING THE FORMALISATION PROCESS OF THE INFORMAL SECTOR

In South Africa, like in many countries the informal sector is constituted of a significant number of people who operate business facilities outside the formal structure while wishing to take advantage of State benefits.

Furthermore, these micro entrepreneurs do not fully realise that being outside the formal sector does not allow them any chance of growing their businesses, while exposing them to abuse.

It is hereby proposed to consider the establishment of a specific simple and affordable registration process giving these micro entrepreneurs a formal existence, allowing them to open bank accounts (regulating banks to open accounts at minimum costs for such simply registered companies even with minimal balances), to invoice officially up to a certain maximum turnover (to avoid competing with larger formal businesses), and to recruit officially up to three or five persons again on very simple terms, paying a minimum amount of a single tax based on their turnover and employees' salary. Despite this, basic formalisation will certainly not provide the Government with much income; it should provide the micro entrepreneurs with an insight into the benefits of being formal and increase the formalisation of the economy.

To add to the attractiveness of such status, MFIs' facilities and other grant programmes could be made available on more favourable terms only to such formalised micro enterprises.

Such development has a very important political impact and would require a strong commitment from the Government to be achieved and obtain the cooperation of various Government departments and ministries to succeed. It is obviously subject to further study and assessment.

Could SEDA which is already segmenting its activities with SMMEs along four categories per number of employees[67] be entrusted with such programme?

The evaluators have not met such developments in an emerging country so far. It is reported that Brazil has developed such a scheme which appears successful through a

[67] Micro enterprises : from 1 to 5 employees
Very small enterprises : from 6 to 20 employees
Small enterprises: from 21 to 50 employees
Medium size enterprises: from 51 to 200 employees

Federal Government initiative that created the legal entity Individual Entrepreneur (EI) in July 2009[68].

[68] Cf. http://infosurhoy.com/en_GB/articles/saii/features/economy/2011/01/04/feature-03

7 LIST OF ANNEXES (ATTACHED TO ANOTHER DOCUMENT)

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Final Evaluation of the EC-funded Private Sector Support Programme titled "Support to the Risk Capital Facility 2" – SA/21.031700-05-01

SOUTH AFRICA

Final report annexes

November 2013

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7.1 Annexe: Project political, economic and social background

7.1.1 Overall Context

- Political context

South Africa is a politically stable country with a non-racial democratic system. The country enjoys a multiparty political system, active opposition, a solid constitution and an independent judiciary. Further, South Africa exerts a lot of regional influence through active leadership of the African Union (AU) and supports growth and development through the AU's New Partnership for Africa Development.

At the core of the country's developmental economic strategy is an array of policies that seek mainly to provide a stable and progressive socio-political environment for the South African population. The government has also provided for **an integrated outcomes approach to governance** that is aimed at improving government planning decisions. According to the Outcomes Approach guide[1] "*The defining feature of this administration will be that it knows where people live, understands their concerns and respond faster to their needs*." As such the government has been organised into clusters that "*ensure proper coordination of all government planning, decision making and service delivery*". Government integration through inter-ministerial committees results in different clusters which include the economic and employment cluster. This cluster deals with issues of government's macroeconomic strategy, including issues relating to the second economy. The cluster's key objectives are:

- Sustainable economic growth;
- Job creation;
- Redistribution of income;
- Human Resource development and skills development;
- Competitiveness of the economy;
- Research and development;
- Spatial development;
- Stable financial system; and
- Economic Governance

The cluster is chaired by the Minister of Rural Development and Land Reform with the Minister of Science and Technology as deputy and comprises 12 ministries including Trade and Industry (dti) and Economic Development (EDD). The two departments, dti and EDD work together closely when it comes to SMME development.

- Economic context

South Africa is a multiracial country with a population of 51.8 million inhabitants. According to Stats SA[2] black Africans are in the majority at 79 % and females are slightly more than males by 4 %. The country has the largest and most diverse economy in the continent and until the global recession, South Africa has enjoyed economic growth for more than a decade. According to Stats SA nominal GDP at market prices during the second quarter of 2013 was R836 billion which is R23 billion more than in the first quarter. However, the dti's Medium-Term Strategic Plan 2011-2014, cautions that:

[1] www.thepresidency.gov.za/dpme/docs/guideline.pdf
[2] www.statsa.gov.za/publications/populationstats.asp

The fact that the positive growth has been driven mainly by international commodity price increases and credit-induced consumption-therefore not being sufficiently underpinned by growth of the production sectors of the economy is an indication of a deep seated structural problem facing our economy. The unsustainable and resultant problematic nature of the growth path has necessitated an up scaled and refocused Industrial Policy Action Plan (IPAP).

- Social context

Despite the apparent successes the government still faces a plethora of challenges. South Africa remains a racially unequal and dual society with respect to wealth and income distribution. South Africa's Gini coefficient of 0.58, points to a significant social and economic divide between the first and second economy. The second economy contains millions of the very poorest — mostly black people, marginalised and unskilled, who take up informal activities simply to survive. There are also disparities in living standards. Most South African cities are surrounded by vast, high-density informal housing which are populated mostly by blacks and coloureds. An article entitled "Study Finds Protests are Spiralling"[3] noted that "*2012 could be remembered as the year of service delivery protests.*"

Further, South Africa has a high crime rate compared to other countries in the region. South Africa's rates of violent crime are high, although rates for murder have steadily fallen (from 69.5 per 100,000 persons in 1994 to 30.9 in 2011/2012, according to the South African Police Service statistics). The country faces a variety of other challenges some of which are related to governance. Corruption is very high and the country is ranked 69 out of 176 on the Corruption index.[4]

7.1.2 Employment, a major challenge

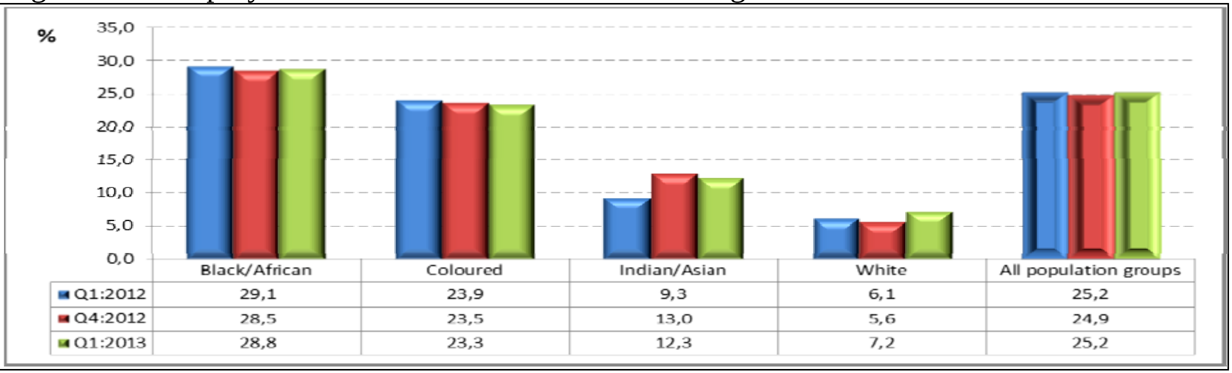
Despite the positive economic growth, unemployment rates in South Africa still remain unacceptably high. According to Stats SA Labour Force Survey; [5] the number of unemployed South Africans for the periods Q1: 2008 to Q1: 2013 averaged 4.3 million. Unemployment is highest among the black population at nearly 30 %. The unemployment rate for women remained higher than the national average between Q1: 2008 and Q2: 2013. Figure 1: Unemployment Rates in South Africa according to Race below shows unemployment rates according to race for the period 2012 to 2013.

[3] City Press: Study Finds Protests are Spiralling available at www.citypress.co.za/news/study-finds protests are spiralling accessed on 07.10.2013

[4] Source:en.wikipedia.org/wiki/Corruption-Perceptions Index

[5] Stats SA labour Force Survey

Figure 1: Unemployment Rates in South Africa according to Race



	Black/African	Coloured	Indian/Asian	White	All population groups
Q1:2012	29,1	23,9	9,3	6,1	25,2
Q4:2012	28,5	23,5	13,0	5,6	24,9
Q1:2013	28,8	23,3	12,3	7,2	25,2

Source: Stats SA website

There are several reasons that attempt to explain the unemployment statistics. Bisseker (2012)[6] gives an overview of some of these reasons. Some of these are briefly explained below:

- High margins in product markets and wages in labour markets have resulted in uncompetitive domestic costs of production, eroding external competitiveness and excluding parts of the population from formal economic activity. This has constrained South Africa's ability to diversify its exports into areas that go beyond its comparative advantage of exploiting its mineral endowment.
- The relatively high wages and profits for insiders have resulted in higher consumer price levels and unemployment for outsiders. In addition, labour market arrangements have set entry-level wages above the productivity of inexperienced workers with little marketable skills, including through relatively high minimum wages.
- The struggle for dividing rents between highly concentrated, oligopolistic firms and strong and politically influential labour unions has resulted in large economic losses associated with frequent labour strikes[7].

- The Jobs Fund: as already mentioned, reducing unemployment is a very important goal for the South African government which has set up initiatives such as the Jobs Fund. The Jobs Fund has been funded to the tune of 9 billion dollars and is managed by the Development Bank of South Africa (DBSA). The fund is aimed at creating permanent rather than temporary jobs. It is hoped that the proposed initiatives will create over 65 000 new permanent jobs in South Africa by 2015. In addition, these initiatives will also place 42 000 unemployed people in existing vacancies. To date the fund has approved 54 initiatives, including innovative business incubation models to develop SMME's, training programmes which overcome barriers to first time employment for unemployed youth, and supply chain diversification initiatives aimed at previously excluded businesses. The Job fund has partnered with different Non-Governmental Organisations such as Microsoft South Africa, Fetola's Graduate Asset Programme and Awethu to name just a few.

- Another job creation initiative is the Expanded Public Works Programme (EPWP) which was launched in 2004 and is currently still being implemented. The programme covers all spheres of government and state owned enterprises. EPWP Projects employ workers on a

[6] Bisseker, C. (2012) " Working but Still Poor" Accessed 0n 04.10.2013
http://www.financialmail.co.za/economy/2012/10/04/working-but-still-poor
[7] Cf. IMF article IV, South Africa 2012: http://www.imf.org/external/pubs/ft/scr/2012/cr12247.pdf

temporary or on-going basis either by government, by contractors, or by other non-governmental organisations under the ministerial Conditions of Employment for the EPWP or learnership employment conditions. The EPWP creates work opportunities in four sectors, namely, Infrastructure, Non-State, Environment & Culture and Social. According to the ZAF EU Evaluation report Volume 1,[8] the following are the successes of the programme of the EPWP.

i. Since 2004/05, it has provided almost 3.8 million job opportunities in total, 2 million of which on infrastructure projects with over 800,000 in environmental and cultural projects.
ii. The programme has been particularly successful in reaching its targets for both women and youth but has not met its targets for the disabled.

However, despite the success of both phases (551,000 person years of work in Phase 1 and 600,000 in phase 2 as of 2012) substantially more jobs will need to be created in order to reach the target of 2 million full-time equivalent jobs.

- The Community Works Programme (CWP) is yet another initiative that is aimed at job creation. The CWP was started as a pilot project in late 2007 to address high unemployment. It is based on the recognition that policies to address unemployment and create decent work will take time to reach people living in marginalised areas with few opportunities. According to the ZAF EU Volume 1 report, the programme has come close to meeting its targets in both 2009/10 and 2010/11. The report notes that the programme has created almost 24,000 full time equivalent (FTE) jobs in 2010/11 with 71 % of participants being female and half are young people.

7.1.3 The SMMEs landscape in South Africa

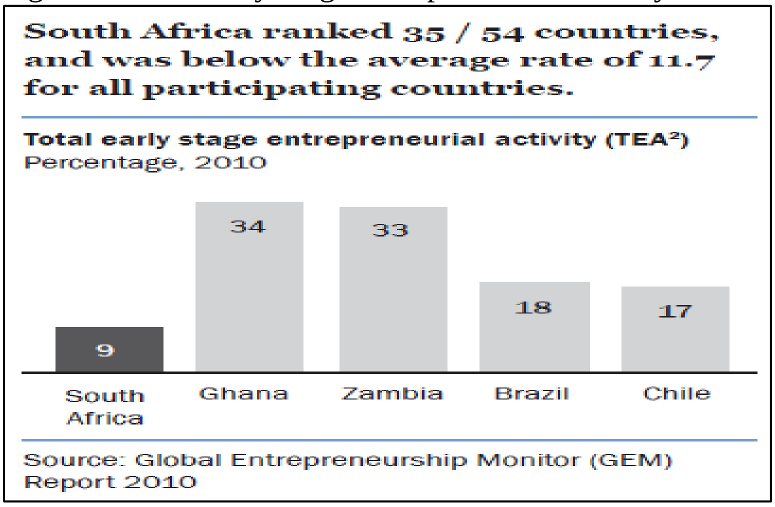
The promotion of SMMEs is provided for under the White Paper on the Promotion of Small Business (1995) which sets out the government's policy on the development and promotion of small business in South Africa. This was followed by the National Small Business Enabling Act in 1996 which defined SMMEs and provides for the establishment of support institutions for SMMEs, note that the act was amended in 2003. The new Integrated Strategy on the promotion of Entrepreneurship and Small Enterprises is also a key strategic document which gives 'renewed impetus"[9] to the small business sector and seeks to bring into life the government's policy of promoting small businesses. According to Elizabeth Thabethe, the Deputy Minister of the dti[10] "*the new strategy provides a framework that can be used by all role players that seek to make a contribution in assisting the entry of new players into the formal economy, strengthening growth and sustainability of existing enterprises and creating necessary linkages in the continuum of enterprises graduation from local micro to globally competitive businesses.*"[11]

[8] ZAF European Commission Report Volume 1
[9] dti: (2011)Rethinking Small Business Support in South Africa: Report on the Review of Government Support for Small Business
[10] Quote extracted from dti report entitled "Rethinking Small Business Support in South Africa: Report on the Review of Government Support for Small Business"'
[11] www.thedti.gov.za

Further in his 2011 State of the Nation address, President Zuma stated that "*the small business sector is a critical component of the job creation drive*". The New Growth Path released in December 2010 by Ebrahim Patel, the Economic Development Minister, set job creation as a priority, with a target of creating five million additional jobs in the next ten years. It aims to reduce unemployment from 25 % to 15 %, largely through the development of small businesses.

There is strong evidence that small and growing businesses are critical for job creation and employment in developing economies. De Kock et al (2013)[12] points out that "*There is vast agreement on the direct link between job creation and poverty reduction*". In addition the same writer points out that "*The sector provides most of the jobs, creates most of the new jobs and has the highest employment growth rates*". However, in South Africa figures show that there is no upward trend in the number of enterprises paying corporate income tax in South Africa over this period, i.e. South Africa is not creating large numbers of micro, small and medium firms. For manufacturing the picture is similar – across all size categories there were fewer firms in 2010 than in 2007. [13]

Figure 2: Total Early Stage Entrepreneurial Activity



On the other hand, the rate of entrepreneurship seems to be growing in South Africa. The Global Entrepreneurship Monitor (GEM) data suggests that the proportion of owner-managers in the South African population increased by about three times between 2001 and 2012. However, in comparison to other countries these proportions remain very low – in 2012 the proportion of owner-managers in Brazil was 15 % whereas in South Africa it was only 2.3 %. The involvement of Historically Disadvantaged Individuals (HDIs) in entrepreneurship also seems to be increasing. Between 2008 and 2012 Statistics South Africa's Quarter Labour Force Survey (QLFS) indicates that the number of Black individuals who were self-employed and employing other people increased by 6 % and although the number of females fell by 9 %. This increase has been more widespread than just entrepreneurs in micro firms: Black individuals who were self-employed with firms with more than 10 employees increased by 35 % and females increased by 13 %, over this period. Figure 2: Total Early Stage Entrepreneurial Activity above shows comparisons of total early stage entrepreneurial activity in five countries.

[12] De Kock et al(2013) "Is Small Still Beautiful" Literature Review of Recent Empirical Evidence on the Contribution on the Contribution of SMEs to Employment

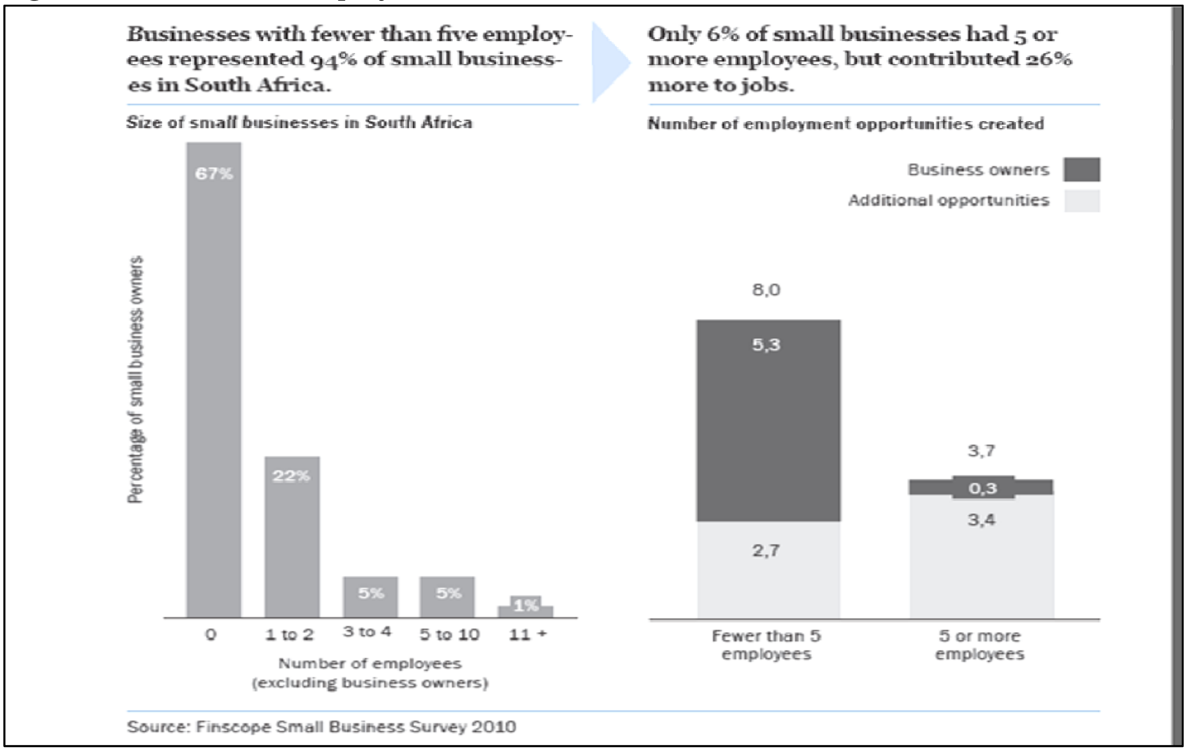
[13] Source :Evaluation of Budget Support in South Africa Draft Final Report 2013

As already mentioned SMMEs also contribute to employment growth through the following, DeKock et al points out two ways in which SMMEs contribute to employment:

- Short Term: Job creation by incumbent /and or new SMMEs in a certain year
- Long Term: Spill over effects due to increased competition and innovation

Figure 3: SMMEs and Employment Creation below shows employment figures by SMEs in South Africa

Figure 3: SMMEs and Employment Creation



SMMEs experience a plethora of challenges which are both policy and operational related. However it should be noted that SMMEs do face different challenges at various stages of their growth cycles. Table 3: SMME Challenges below gives an overview of the major challenges that SMMEs in South Africa face.

Table 1: SMME Challenges

Challenge	Description
Lack of overall small business policy leadership	• Small business lacks a clear champion at the highest level of government resulting in government supported SMME agencies not being allocated sufficient resources to execute mandates.
Approach to policy Formulation	• The relationship between national and provincial government is not as strong as it should be; • Perception that the national small business policy is really a Dti policy rather than a policy for the country as a whole; • Development of the 2005 integrated strategy was not as inclusive as the development of the 1995 white paper; and • South Africa has no clear goals for SMME development which sets measurable targets and milestones to be achieved.

Role of provincial and local government	• National SMME strategy does not give enough guidance to provinces and the roles are not clearly stated in the Act and in the 2005 SMME strategy.
Unclear mandate of SMME institutions	• Scope of institutions such as SEDA need to be reviewed as it is felt that they are under on-going political pressure to extend their operations beyond what their resources and operational capacity can accommodate.
Inadequate Resources	• Support institutions such as SEDA feel that their budgets are not commensurate with the mandates they are expected to fulfil for example its budget of ZAR 400 million since the institutions' merger
Weak Coordination and integration of small business support	• Within small business development circles, the institutions are not very well coordinated
Weak monitoring and evaluation of small business support	• South Africa lacks an overarching framework for monitoring and evaluating the operations and impact of small business support institutions and programmes
Overlapping Institutional roles	• Having several institutions targeting the same market with largely similar offerings creates confusion .e.g. there is a role overlap between the small business activities of the National Empowerment Fund (NEF) and SEDA
Operations	• For example there are complaints that SEDA's Board takes too long to make decisions that enable the organisation's incubation programme to respond to open new incubators
Lack of SMME business data	• There are huge discrepancies in data statistics. For example the Dti and Fins cope's figures on small businesses vary significantly
Limited Use of Innovative SMME models	• Financial institutions can use alternative such as project financing, leasing and factoring
Underdevelopment of Microfinance Sector	• South Africa has an underdeveloped and undercapitalised microfinance industry which has failed to scale up to meet the needs of the SMME sector

Source: Rethinking Small Business Support in South Africa: Report on the Review of Government Support for Small Business

- Government Support for Small Business

At an operational level, SMMEs face a multitude of problems. The Finscope study (2010)[14] points out that when starting, 44 % of business owners cite money-related matters and 50 % cite business strategy as their main obstacles. Even the "money-related" challenges are less a problem of availability of capital, and more to do with entrepreneurs' lack of awareness of financing instruments and limited skills and knowledge on who to approach. Without support, the likelihood of these entrepreneurs creating competitive and sustainable businesses is slim. The other challenges that were presented by the dti report[15]include:

- Application processes tend to be bureaucratic;

[14] Finscope South Africa Small Business Survey 2010 available at **www.btrust.org.za/..../o-nsbs-finance-small-business-survey** -final rep accessed 07/10.2013

[15] dti(2011); Rethinking Small Business Support in South Africa: Report on the Review of Government Support for Small Business

- High transaction costs;
- Lack of awareness about the procedures involved in accessing finance;
- Lack of risk capital;
- Underdeveloped microfinance sector;
- Inadequate scale of public sector support programmes.

While capital does play a crucial role in the development and sustainability of SMMEs, we find that the enabling environment is detrimental to growth as shown below:

- Crime and theft: Finscope survey revealed that crime and theft are ranked as the third highest obstacle to growth for business owners.
- Labour regulations: These are inflexible, impose a high minimum wage for staff and often result in difficulties with unions and strikes.
- Poor infrastructure: high energy costs and lack of consistent electricity supply, high cost and/or limited availability of transport.
- Competition: Competition is ranked as the third greatest obstacle to growth for businesses. This shows that businesses are unable to deal with natural market competition by finding defensible niche markets and products. The economic slowdown has had a negative impact on business growth, with 40 % of businesses surveyed for the SBP "SMMEs growth Index 2011"[16] highlighting this as the primary barrier to growth.
- Human Resources: SMMEs lack the ability to grow management capacity and staff base.

In conclusion Guido Boysen,[17] the CEO of GroFin notes that:
"*To fully realise the potential of SMMEs, the sector needs to be approached with a fresh perspective attuned to the challenges it faces. There is a need for the focus to shift from the available collateral in the business to the viability of the business and the ability of the entrepreneur. Each business needs finance tailored to their unique challenges. In addition to this, the business owner needs access to the expertise and market knowledge required to make their business a success*". Guido Boysen, CEO of GroFin Africa (2010)

7.2 The Government and Private sector support strategy (Dti, EDD, National Treasury, GWME, IDC, BP, SEDA, NEF, PICSA…)

7.2.1 The Public sector

As already mentioned in previous sections, the South African government has been working on creating an enabling policy environment. It is hoped that SMMEs will contribute to the growth and performance of the South African economy in critical areas such as job creation, equity and access to markets.

In 2011, Finance Minister Pravin Gordhan stated that government support to businesses would include R600 million for enterprise investment incentives.[18] Support for small businesses would be provided through the South African Micro-finance Apex Fund (R282 million over three years) and Khula Enterprise[19] (R55 million). Patient capital is available

[16] The SME Growth Index is a flagship of SBP Business Environment Specialists and is an innovative study to understand how and small firms grow

[17] Quote extracted from "The Small and Medium Enterprise Sector; Catalyst for Growth in South Africa

[18] http://www.southafrica.info/business/economy/policies/budget2011a.ht

[19] NB: Khula Enterprise has since been amalgamated into SEFA

through development finance institutions (DFIs), micro-finance institutions, Corporate Social Investment Grants and foundations.

The venture capital (VC) space is growing with an estimated R2.6 billion invested in the VC asset class between 2000 and 2010, 50 % of which went to businesses in the start-up phase. Enterprise Development (ED) is one of the elements contained within the Broad Based Black Economic Empowerment (BBBEE) scorecard, and has a target contribution of 3 % net profit after tax per annum. Corporations would contribute a large amount to the sector through enterprise development. For example, Standard Bank South Africa contributed R35 million in 2010.

Core components of the Government's strategy include;

- To establish a one-stop shop and single funding agency for small and micro-business through the consolidation of Khula, South African Micro-Finance Apex Fund (SAMAF) and IDC funding, amongst others;
- To improve access and reduce the overhead costs of government in order to make more resources available to end-users;
- To fully implement government's long-standing commitment to pay small business suppliers within 30 days, with clear consequences (fiscal penalties) for non-compliance by public entities;
- To integrate small and micro-enterprise support systematically into all sector strategies; this is critical to ensure a space for smaller enterprises in the value chains of major industries and to support the development of clusters and sectoral regulations and market institutions that meet the needs of smaller producers;
- To initiate a red-tape elimination campaign to simplify regulated procedures and forms and remove any bias against smaller producers, for instance in zoning requirements, with results reported to Cabinet on a quarterly basis;
- To strengthen access to micro-finance for small enterprises in order to bring more citizens into economic activities and thus widen the enterprise pool in the country as one key step to promote the growth of new enterprises; and
- To address smaller businesses' concerns about access to and the cost of space in shopping malls.

In order to achieve this, the government has put into place several institutions that are meant to improve access to financing for SMMEs. The table below gives a summary of the institutions that are supporting the government with regards to SMMEs financing.

Table 2: Funding Programmes for SMMESs

Institution	**Target Area**	**Loan Facility**	**Services Offered**
National Empowerment Fund (NEF)	Broad Based Black Economic Empowerment	The NEF consists of four funding channels Imbewu Fund: ZAR250 000-ZAR 10million Entrepreneurship Finance: Maximum ZAR5 million Procurement	• NEF is a driver and thought leader in promoting and facilitating black economic participation by providing financial and non-financial support to black empowered businesses and by promoting culture of savings and investment among black people

		Finance: ZAR10 million Franchise Finance:ZAR5 million	
National Youth Development Agency	Youth Development Programmes	ZAR1000-ZAR10million	• Promotes youth development through guidance and support to initiatives across sectors of society and spheres of government • The NYDA's primary target group is young people aged between 14 and 35 years. The majority of beneficiaries should be from low-income households. Emphasis will also be placed on young persons with disabilities. NYDA Enterprise Finance aims to promote entrepreneurship among young people, so it
Small Enterprise Finance Agency (SEFA)	Lower end of SMMEs	The facilities range from a minimum of ZAR50 000 to a maximum of ZAR5 million	• SEFA was established on 1st April 2012 as a result of the merger of the South African Micro Apex Fund, Khula Enterprises and the small business activities of IDC • Delivering wholesale and direct lending; • Providing credit guarantees to Small, Medium and Micro businesses; • Supporting the institutional strengthening of Financial Intermediaries so that they can be effective in assisting SMMEs; • Creating strategic partnerships with a range of institutions for sustainable SMMEs development and support; • Monitoring the effectiveness and impact of our financing, credit guarantee and capacity development activities; • Developing (through partnerships) innovative finance products, tools and channels to catalyse increased market participation in the provision of affordable finance

- Business Development Services

SMMEs experts identify business support as a priority focus area for the South African SMME sector, and a range of individuals and organisations have responded by providing a range of services broadly referred to as business development support (BDS). These organisations have the potential to address the barriers to SMMEs' growth. Business development services are also crucial to the development of SMMEs. The Small Enterprise Development Agency SEDA's mandate is to provide business development services to SMMEs. SEDA offers the following services:

- Tender advice;
- Networking and business links, providing guidance to access markets;
- Technical support for businesses;
- export readiness assessment
- Toolkits on how to successfully participate in exhibitions and trade shows; and
- Improving productivity.

7.2.2 The private sector

The private sector is also actively involved in offering business development services. Some of these key institutions include Shanduka (Black umbrellas).

- Private Sector Partnerships

Private Sector partnerships are also a crucial cog in ensuring that SMMEs are funded. What remains to be seen, however, is whether the combined loan portfolio between these institutions and government sponsored institutions can be consolidated to ensure maximum impact. Table 5: Private Sector Funding Agencies below gives a brief synopsis of some of these institutions.

Table 3: Private Sector Funding Agencies

Funding Agencies	Description
Grofin	• Grofin is a specialised risk financer of small and medium enterprises that require finance in the range of R500, 000 to R5, 000,000. Started in 2003, Grofin targets entrepreneurs looking to start up or expand a business and targets growth orientated enterprises. Grofin's mission is to create sustainable wealth, employment and economic growth (through the development of successful enterprises) while generating attractive returns for all stakeholders; • Offerings include a combination of business development services and a variety of financial products tailored to the specific needs of the business. • The company finances business opportunities in services, manufacturing and commercial sectors; • Grofin also finances franchisees. Target firms do not employ more than 100 employees. Business is generated through a network of intermediaries that refer clients requiring finance
Anglo Zimele	• Zimele provides flexible debt-equity financing (including business development support and the transfer of technical skills) to black-owned enterprises. • The model involves investment funds that provide loans and equity finance to support start up-or expansion businesses. • The goal is to ensure that local black suppliers and local companies contribute to Anglo American’s supply chain.

Business Partners	• Business Partners is a financial institution which specialises in financing SMEs, using the whole range of financial instruments, from pure equity up to simple unsecured overdraft, with a strong Management support. • Created in 1991, the Fund has multiplied its value by 20 while paying dividends to its shareholders. • BP is opened to manage specific funds on behalf of investors targeting SME support for a minimum amount of about Euro 20 million.
Banks	• Commercial banks such as ABSA, Nedbank, FNB and Standard Bank have specialist SME divisions and provide financing for qualifying entrepreneurs

7.2.3 The development partners

➢ Role of Development Cooperating Partners in improving access to finance in SMMEs

The role of development partners in the provision of finance for SMMEs should also be highlighted. Some of the initiatives are explained below:

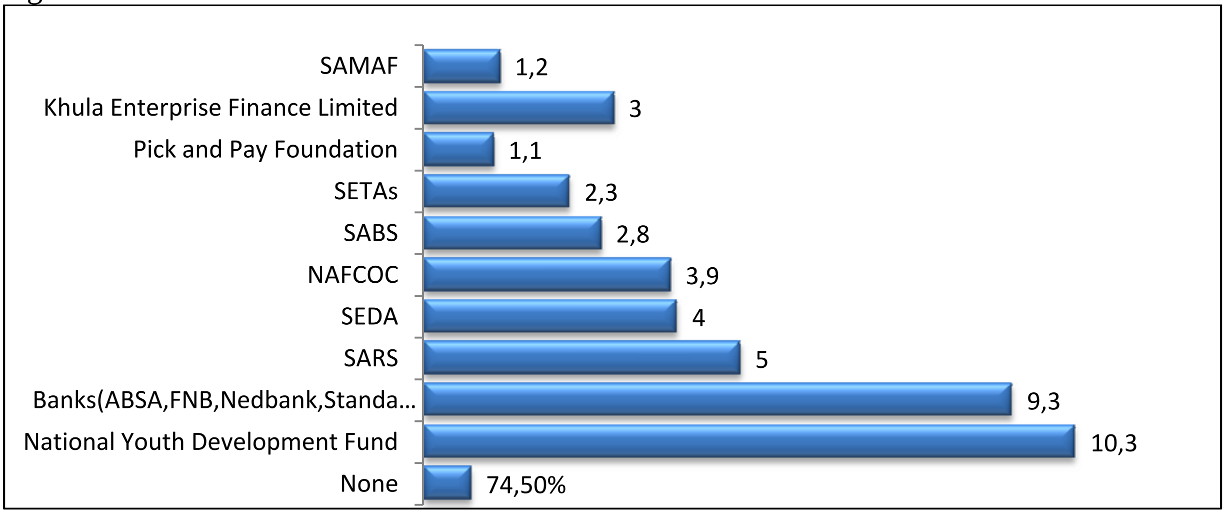
Table 4: Role of Development Finance in Improving Access to Finance

European Commission	• The CWP and the EPWP have been supported by the Employment Creation Fund which is a Sector Budget Support Programme funded by the European Commission • The creation of 45,900 jobs against a target of 41,229 through funding proposal in the framework of the IPAP 2 and NGP supported by the ECF;; • The creation of 33,000 jobs in 2007/8 against a target of 24,000 through programmes put in place by the Industrial Development Corporation (IDC) supported by the SWEEP; iii) the creation of 6,655 jobs between 2007 and 2012 through programmes put in place by the IDC supported by the Risk Capital Facility SBS operation; iv) • The addition of over 700 jobs in 2011/12 as a result of demonstration projects put in place by the Department of Science and Technology and supported through the Innovation for Poverty Alleviation SBS operation. • European Investment Bank Funding of Risk Facility 1&2
United States Agency for International Development (USAID)	• BLUE is a project funded by USAID and established in 1995 in a cooperative agreement with the National Industrial Council • The Blue project aims to increase, significantly and sustainability, the business done between large buyers and small suppliers as its contribution towards normalising South Africa's economic structures Blue offers SMME loans, micro-insurance, education loans, short term loans, personal loans and debt consolidation loans
Department for International Development (DFID)	• Provision of funding for SMME research in African markets
KFW, Proparco and	• Offer credit lines for SMMEs

other IDFIs	

SMMEs are not aware of organisations that give support and advice to small business owners. There is a need for both the private sector and the government sponsored finance institutions to carry out a campaign to conscientise SMMEs on the available funding options. As shown by Figure 4: Awareness of SMME Finance Institutions below a majority of the SMMEs are not aware of the finance institutions that can aid in their development.

Figure 4: Awareness of SMME Finance Institutions



Source: Finscope Study 2010

7.2.4 The financial Sector in South Africa

The South African Financial sector is characterised by a sound regulatory and legal framework. It boasts of a number of banks both domestic and foreign institutions. These banks/institutions provide a full range of services that are commercial, retail, merchant banking, mortgage lending, insurance and investment institutions. The banking system remains the main source of capital to start and grow businesses. Finscope estimates that 47 % of business owners are formally banked through commercial banks.

The 12th PwC report entitled Strategic and emerging issues-African Banking[20] also gives some important insights into the South African banking industry that may directly and indirectly affect SMMEs. Some of these factors include:

- From a macroeconomic perspective, there is justification for concern over the possibility of sharp rises in money market interest rates and higher unemployment;
- Corporate banking, flow businesses (foreign exchange and rates) and business banking are the most important wholesale market segments;
- Traditional retail banking (deposit taking and transactional banking), electronic banking and personal banking are the most important retail market segments;
- Traditional retail banking is viewed as the most intensely competitive market segment and banks believe a fundamental change in strategy and positioning is required to compete aggressively in this segment; and
- Rapid expansion in unsecured lending is the second-most important development in the South African banking industry. Interestingly it was also considered to be the second-biggest weakness in the industry.

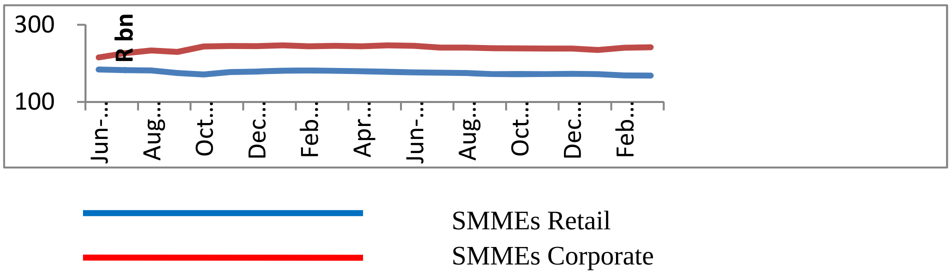
[20] www.pwc.co.za/en/assets/.../pwc-banking-industry-survey-june2009.

- The likelihood of new entrants into the South African banking market is regarded as low. However, the likelihood of a foreign entrant is considered to be higher than the establishment of a new local bank.
- Regulatory reform is regarded as the most significant development, most pressing issue and most significant weakness in the banking industry. The sheer scope of current and planned reforms that will impact the industry are top of the mind for bank executives.

➢ SMME Lending Patterns

In South Africa, large banks contribute 95 % of all lending to SMMEs[21] and according to the dti report entitled "Rethinking Small Business Support in South Africa; Report on the Review of Government Support for Small Business December 2011" points out that commercial banks are less likely to finance micro and small enterprises and start-ups preferring instead to focus on larger formal SMMEs and established businesses. Figure 5: Bank Lending Trends in South Africa below shows the lending patterns of South African Banks up to 2010

Figure 5: Bank Lending Trends in South Africa



Source: World Bank: Bank Financing of SMMESs in five Sub-Saharan African countries; The Role of Competition, Innovation and the Government Policy Research Working Paper 6563

A comparative analysis of South Africa with other countries will reveal that South Africa is lagging behind other countries with regards to SMME lending. Comparatively the study found out that banks in Kenya, Rwanda and even Tanzania seem to be more involved with SMMEs than banks in South Africa and Nigeria. (An in-depth study of these best practises might benefit the SMMEs sector in South Africa). Further the World Bank Africa Region Survey report mentioned above also points out that; the share of SMMEs lending, the overall loan portfolios of banks varies between 5 and 20 %. Table 7: SMME Lending Patterns in selected African countries below shows these trends.

Table 5: SMME Lending Patterns in selected African countries

Banks Involvement	**Kenya**	**Nigeria**	**Rwanda**	**South Africa**	**Tanzania**
SMMES's share of total bank lending	17.4%	5.0%	17.0%	8.0%	14.0%
Contribution of SMMESs to banks net income	20.5%	11.0%	20.0%	15.0%	16.0%
% of Revenues derived from					
Credit	68.0%	22.4%	71.0%	27.0%	73.0%
Deposit and Account Management	12.7%	53.2%	11.4%	50.0%	12.0%
Other transactions and fee based services	19.3%	24.4%	17.6%	23.0%	15.0%

Source: World Bank: Bank Financing of SMMESs in five Sub-Saharan African countries; The Role of Competition, Innovation and the Government Policy Research Working Paper 6563

[21] World Bank: Bank Financing of SMMESs in five Sub-Saharan African countries; The Role of Competition, Innovation and the Government Policy Research Working Paper 6563

7.3 Structure of the RCF programme

7.3.1 Project structure

- Sector Budget Support versus traditional Programme structure and duration

The sector budget support approach is justified as follows in the Technical and Administrative Provisions annexed to the Financial Agreement:

Sector budget support is the appropriate modality for the EC support because:

1- *A medium term financing plan is in place foreseeing financial support to SMMEs;*
2- *There is stable national macroeconomic environment;*
3- *There is satisfactory performance of public financial management both at National level as well as at the level of the implementing organisation, the IDC. In this context the provision of sector budget support will take place in an appropriate environment in a way that will strengthen public budgeting and planning, sustain ownership and reduce the transaction costs of aid;*
4- *The instrument of budget support is chosen so as to be able to continue to provide a further financial injection into the capital base of the RCF, a highly successful programme, originally set up with financial support from the EPRD.*

The European Commission uses the Sector Budget Support approach as a way of working with the South African Government, up to 80% of its commitments.
The RCF 1 Programme was followed by the RCF 2 in the form of a Sector Budget Programme to allow for more flexibility as well as to recognise the ability and capacity of the South African Government and its various institutions dealing with the support of HDP SMEs.

The recent set up of the Economic Development Department (EDD) has slightly modified the original set up. EDD responsibilities encompass the setting of the general economic development policy of the government[22] as well as coordinating the various actors involved in this respect. As far as support to SME access to finance is concerned, the fact that IDC and its SEFA subsidiary are under the supervision of EDD[23] implies its involvement with the follow up of such programmes. In this respect, it is recommended to invite an EDD representative to the Project Steering Committee. Due to the historical involvement of the dti with RCF and the various MOA governing their relationship, it is not suggested to modify the arrangement for the foreseeable future.

- The RCF legal structure

The RCF was structured as a ring fenced entity within the IDC organisation. The possibility to create a separate legal entity was reviewed by a Technical Assistant. It was finally decided not to establish such separate entity, to avoid delays, increased administrative and tax burden, in a context whereby the South African Government wanted to limit/reduce the number of existing government institutions.

The disadvantage of such an IDC ring fenced fund is that it does not facilitate the raising of leveraged finance for the fund from other investors/donors but also potential private entities

[22] Cf. the EDD New Growth Path Framework document
[23] It is worth noting that SEDA is under the supervision of the dti

which would entrust funds to an independent RCF, possibly to improve their social compulsory commitments, as per the various industrial sectors BEE Code of Good Practice[24]. The evaluators recognise that this is a theoretical possibility, the RCF Fund being construed on the basis of a 0 % nominal IRR, which is not attractive to private investors[25].

Finally, the establishment of RCF as a separate legal entity might have translated into less support from IDC units and departments, more responsibilities on RCF officers who might not have the required full expertise needed, and probably less capacity building within IDC. Overall, the mission approves the fact that RCF was construed as a ring fenced risk capital facility within IDC, based on the results generated by RCF at the IDC level.

- The stakeholders' undertakings

  - The dti

As per the FA, the dti shall commit a minimum of ZAR 1.4 billion of development funds towards the support of SMEs through various channels (NEF, Khula, SEDA, SMEDP, GODISA). As per the First rider to the FA, this consideration was waived, having been largely exceeded.

The dti shall organise and head the Project Steering Committee which met quarterly as required.

The dti remains the owner of the funds over which it has overall responsibility and accountability.

  - EIB

The EIB was involved in the programme at the request of the EU. The role of the EIB is described in the EC - EIB Agreement. It consists mostly in i) approving each and every financing commitment proposal presented by IDC, ii) ensuring that IDC manages RCF as per best practice, iii) monitor on a quarterly and annual basis the performance of both the RCF1 and RCF 2 Funds and iv) provide the EC with an independent view on the performance of the RCF 2 Fund. These reports were duly produced on time.

The EIB is entitled to a monthly fee of Euro 42,000 with a maximum of Euro 2.5 million over the life of the programme which appears on the high side. It is regretted that the EIB fee did not include some sort of incentive linked to the successful completion of the programme.

  - IDC

The IDC is in charge of implementing the RCF Programme according to the conditions described in the dti – IDC Memorandum of Agreement which covers the various conditionalities described in the FA and in the EIB - IDC agreement which fixes the Fund investment guidelines.

IDC provided as required € 5 million equivalent as a grant to finance Business Support Services (BSS) over the implementation period.

[24] The Codes of Good Practice contain frameworks for the determining BEE, including the generic scorecard, guidelines and list of BEE agencies, as well how the different parts of the scorecard are to be measured in companies: http://www.southafrica.info/business/trends/empowerment/BEE-codes.htm
[25] However, the ISIVANDE fund seems to have managed to raise ZAR 50 million from Old Mutual to service the Funds targeted women

As per the dti – IDC MOA, IDC is entitled to a management fee covering its yearly real expenses with a maximum of 10 % of the yearly re-flows from both funds. It is worth noting also that IDC is indirectly benefiting from the extra income derived from its loans that the RCF "equity" finance renders possible.

Worth noting is the built in incentive for IDC to perform well since its management fee is linked to the reflows and that it has a further built in advantage through the support given to IDC direct risk lending.

- The Project Steering Committee undertakings

The Project Steering Committee (PSC) shall provide the project management with guidance and policy direction.[26]

The members of the Project Steering Committee are limited to thirteen persons[27], plus special case by case invitees. The PSC members seem to aggregate well targeted expertise while the representative of the EC has observer status. The TOR of the PSC signed in May 2011 are still limited as far as the description of its duties is concerned.

The PSC meets every quarter, based on quarterly reports by RCF. It is also provided with annual reports by the EIB[28] and IDC.

- Disbursement of the funds by the EC

Disbursements were to be done in three tranches of respectively € 20 million, € 13, 5 million and € 13,73 million subject to a number of contracted clauses in the FA. These conditionalities were a mixture of budget support conditionalities and satisfactory programme performance.

The three tranches have been released further to two riders which extended the duration of the programme by three years.

The conditionalities for the release of the three tranches were met, as described in Annexe 7.5

[26] Cf. the FA, page 8
[27] PSC members are:
- dti (Chairman);
- IDC: Divisional Executive
- EC (as observer)
- SAVCA
- Dti
- WDB Investment Holdings
- Business Partners
- IDC: Head DFD
- Banking Association of SA
- SEFA
- National Treasury

[28] Up to the end of 2011

7.3.2 The RCF projected activities

RCF 2 had an implementation phase under the Financial Agreement of three years, already extended by three years as far as RCF 2 is concerned (Rider 1 extended the period by one year and Rider 2 extended it for a further 2 years). The life of the Fund investment period was then to be six years, until the end of 2011. However, as seen here above, new financial supports are still being committed, further to a PSC decision to continue to invest the available funds.

The Fund should have reached the initial nominal aggregate amount of about ZAR 500 million[29] plus ZAR 61 million of accrued interest (at the end of 2011) when all funds should have been invested.

At end of June 2013, total amount disbursed was ZAR 308 million which translates into 78 % of total commitments of SAR 393 million). Funds remaining to be committed amount to ZAR 168 million including accumulated interest amounting to ZAR 116 million. Total value of the Fund amounts to ZAR 561 million, plus eventually the ZAR 60.7 million of interest accrued on the IDC account.

As per the FA, the Programme should leverage the EC funds up to 100 % which was fully achieved both for the Direct channel with the related IDC funding provided and for the Niche Fund channel whereby RCF was one of the smaller investor.

- The SME targets and conditionalities[30]

The investment conditionalities are described in the Financial Agreement for a number of them as well as in the investment guidelines, attached as an annexe to the EIB/IDC MOA. These guidelines have been modified through two riders over the years. The final guidelines integrating the up to date conditionalities are attached as Annexe 7.6.

The RCF clients defined as SMEs in the Financial Agreement (FA) shall meet a number of criteria as far as their HDP ownership (minimum 25 % plus one share effective or within one year of the granting of the loan), their size (less than 200 employees, less than ZAR 62 million turnover - increased through Rider 2 from 35 million turnover, total assets less than ZAR 67 million – increased through Rider 2 from 40 million total assets), their geographical location (outside Gauteng and Western Cape provinces for at least 65 % of the commitments), and the economic sector spread of RCF commitments.

As per the audit at the end of June 2012, all investments supported by RCF complied with the above criteria, except Clear data and Massiv TV which do not comply with the minimum HDP shareholding of 25.1%. Measures are planned to meet these criteria in due course.

The number of SMEs funded by RCF 2 should reach a minimal number each year (amended via the riders: Cf. the log frame in Annexe 7.7). RCF shareholding shall normally not exceed 49 % of the SME share capital. Individual transactions shall be between ZAR 250,000 minimum, and ZAR 20 million maximum, with duration between 8 to 12 years, (30 million and maximum 12 years duration for the niche funds).

[29] Original estimated amount at time of programme launch was ZAR 423 million

[30] For precise data on the conditionalities required, refer to the rider 1 & 2 modified log frame in the annexe to this report as well as to the Annexe A of the EIB – IDC agreement

A minimum of 100 % co-financing by IDC, by niche funds or by third parties to end beneficiaries is the rule.

In parallel, the investees must commit to a minimum number of 6000 HDP job creations, including a minimum number of 30 % women; a number of HDP promoted into managerial position (including 30 % women) as well as a number of HDP (including 30 % women) as shareholders. The investee must also meet health and environmental criteria such as having in place an HIV awareness plan and an environment improvement scheme.

Initially, the RCF investment per job created was to be maximum ZAR 60,000 per job (in fact, the programme amount divided by the objective of 6,000 jobs created.). Since devaluation of the ZAR, that amount increased to ZAR 100,000 progressively. Due to the difficulties to meet this target, the PSC decided to increase that amount to ZAR 300,000 from the end of 2011. This new amount allows tackling more capital intensive investments, but also implies that RCF contributes to a higher percentage in the funding of the projects per job created, increasing its risk support benefit to the other lenders.

- Three financing channels

Three financing channels have been identified with respective weighting to be achieved[31]:

- Direct co-financing with IDC (50 to 60%)
- Financing of Niche Funds (25%)
- Third party co-financing (15%)

Plus a fourth objective: funding of SMEs with an involvement outside South Africa (at least 15 SMEs creating 500 new HDP jobs). This last covenant has not officially been cancelled, however, it is understood that it will not be realised.

- The RCF Marketing

As in the case of RCF 1, RCF 2 depends on IDC Sector Business Units (SBUs) to identify potential clients for the Direct Fund Channel; it therefore proposes its “equity” financing to the various sectoral departments of IDC and the IDC regional offices. It was envisaged in the RCF 2 FA that IDC shall present at least 300 realistic opportunities yearly, sized downwards to 400 propositions over the four year implementation period as per the First Rider to the FA. However, with regard Niche Fund financing and Third Party financing, RCF had to conduct its own direct marketing activities towards its identified targets.

- The financial instruments

In line with RCF strategy, the financial instruments to be used have to be equity or equity related facilities, consisting mainly of shares, preference shares, subordinated loans, convertible bonds. In that sense, this programme was planned to be used as an equity fund to support HDP owned SMEs with HDP employment impact.

The way to deliver the support is described as follows in the Investment guidelines:
“*Instruments – the fund will be used primarily for equity and quasi-equity investments although conditional loans or convertible loans could also be considered.*

[31] For precise data on the weighting required, refer to the Annexe A of the EIB – IDC Agreement: Investment Guidelines

Stakes in Investee Companies – Stakes should normally be minority stakes (maximum 45 % of voting shares) yet large enough to enable the IDC, through the fund, to be an active partner in each investment. Under certain conditions (eg to facilitate a structured buyout) a majority stake could be considered.

Exit mechanisms – mechanisms, such as repurchase of shares by project promoters, sales to strategic investors or listings, should be assessed as part of the project evaluation process, with a target of an exit from equity investments by 8-10 years after the initial investment. Longer periods will be allowed for long gestation projects in sectors such as the commercial agriculture and tourism".

- Pricing

The pricing of the RCF financing was constructed so as to ensure that the nominal value of the EC grant is recovered at the end of the 12 year project duration (not counting inflation). It is assumed that the nominal amount concerns the ZAR amount, including the accumulated interest at the end of 2011, i.e. a total of ZAR 561 million.

To ensure this objective, taking into consideration a delinquency rate of 30 % during the life of the project, the Real After Tax Internal Rate of Return (RAT IRR) had been computed at 10.19 %, which implies a yearly "coupon" of about 19.15 % payable monthly in arrears, i.e. a Global Effective Rate of about 21.1 % p.a. on the financing granted to investees[32].

Since most of the financing granted to the investees are in the form of subordinated loans (85 % of the total number of operations under RCF 2), the pricing was usually based on a market based rate of interest payable monthly in arrears, usually indexed on Ned Bank prime rate (plus a margin), plus a sweetener, most often calculated as a percentage of the budgeted turnover. The objective is to obtain for RCF 2 a Real After Tax (RAT) IRR of 10 %, and at a minimum in case of lower than budgeted turnover/cash flow and therefore zero sweetener: a RAT IRR of 5 %[33].

Due to the difficulty to achieve this target and the competition from other fund sources, flexibility was introduced through an amendment to the IDC/EIB MOA, leaving ample leeway for the fixing of pricing by IDC, to achieve nominal return of 100 % of allocated amount for investment, after taking into consideration IDC fees and expected real delinquencies. Thereafter, the minimum pricing targeted has been a 5 % pa gross interest plus a 5 % gross upside, hopefully resulting in a gross 10 % pa return.

- Training

Over the life of RCF 2 the training needs of relevant clients' staff (as defined in the logframe) in all funded clients should be identified, courses designed to meet those needs and training provided if requested by the client. Part of the training costs has to be supported by the beneficiaries along a sliding scale defined by the BS Department.

[32] The pricing model is developed in Annexe G of the EIB – IDC agreement

[33] The trend has been to increase the upside part of the remuneration as against straight interest, under the recommendation of EIB, with even a partial remuneration based on the valuation of the SME, in a couple of cases recently

In excess of 30 % of the number of HDP persons trained shall be female HDP managers.

- BSS delivery

The Business Support Services (BSS) is the assistance to be made available to RCF investees i.e. owners, managers and staff of RCF investees (clients) to improve the sustainability of the enterprises on a 50/50 cost sharing basis. The investee's contribution can be financed through a low interest bearing loan by RCF.
BSS were not programmed within the RCF 1 but their need was recognised to help HDP SMEs achieve sustainability. The BSP support was consequently planned in RCF 2 with a budget of € 5 Million funded by IDC.

Business support was to take different forms:
- Support to the development of marketing, production processes, business plan and finance, long term capacity building and training…
- Assistance to entrepreneurs when an existing investment requires restructuring

Since 2008, the BSS have been structured into a Business Support Programme Department within IDC to provide such services, not only to RCF investees but also to IDC clients, when necessary.

There is no restriction on the kind of support which can be envisaged, based on sharing the costs on a 50/50 basis with the beneficiaries; the beneficiaries' portion can be financed with a concessionary loan from RCF.

This support is to be delivered by consultants selected by the BSS Department. Consultants are working according to detailed Action Plans approved by the clients and IDC/RCF. The follow up of their output is formalised as follows:
- Reports are to be generated by the consultant after providing business support to the clients according to frequency, timing, and conditions clearly specified in advance;
- All reports are meant to be simple, brief, complete and comprehensive and shall precisely aim at reporting on the details contained in the Action Plan. The report shall clearly identify status of actions to be/already undertaken and progress to plan;
- The reports are addressed to the investees for comments.

The appointment of consultants approved by IDC is following precise modalities, fixing all necessary contractual details (among them monitoring, control mechanisms, payment, follow up and reports) in order to secure the development of the assignment in the best possible conditions.

The BSS Department also appoints the consultants required by the Niche Funds' investees.

7.3.3 The RCF 2 unit

- From an RCF 2 dedicated unit towards the Development Fund Department (DFD) of the IDC

Initially, the RCF 1 and 2 units were made up of a team solely dedicated to the implementation of the RCF programmes. In 2008, the RFC team has been transformed into an IDC Department in charge of Development Finance. In 2013, the name of the unit was changed to the Development Finance Department which now manages thirteen different funds, with various focuses.

While the RCF organogram still identifies the officers in charge of RCF 2, in practice, the RCF officers are involved with the different funds managed within the DFD. This unfortunately does not allow following the costs associated with running the RCF programme. Despite the fact that the team has an increased work load in view of the other funds that it now manages, the evaluators feel that the increased responsibilities provide positive returns such as increased professionalism, coherence among the IDC investment programmes and economies of scale.
A person has been designated as in charge of the RCF fund within the DFD team; however, it is not formalised in his task description nor in his title. The responsibility of that person should be formalised and his responsibilities detailed.

Box 1: Funds presently managed by the Development Finance Department

a. Clothing and Textiles Competitiveness Programme – an off-balance sheet programme whose objective is to grow South African-based clothing and textile manufacturers to be globally competitive;
b. Technology Venture Capital Fund – a R135 million off-balance sheet fund whose objective is to assist small businesses commercialize their products through the provision of concessionary funding to small enterprises who develop low/marginal innovative products;
c. Agro Processing Linkages Scheme – a R 100 million ring-fenced on-balance sheet fund whose objective is to support and incentivize agro-processors to source raw materials from resource poor farmers by providing concessionary loans to agro-processors for on-lending to poor farmers and matching any technical support provided by the agro-processor on a Rand by Rand basis;
d. Agro Processing Competitiveness Fund – a R250 million ring-fenced off-balance sheet whose objective is to facilitate increased competition, growth and development in Agro Processing and beverage sector;
e. Gro-E scheme – a R10 billion ring-fenced on-balance sheet fund who objective is to encourage employment creation, thereby expanding South African production capacity through the provision of concessionary funding;
f. UIF Fund – a R4 billion listed private placement bond whose objective is to contribute towards sustainable job creation and retention by supporting job creating projects through the provision of concessionary funding; and
g. Transformation and Entrepreneurship Scheme (an umbrella fund for 5 sub funds)– a R1billion on-balance sheet IDC Fund whose objective is to facilitate development of marginalized entrepreneurs (women, black entrepreneurs and people with disabilities) and enable marginalized groups (workers and communities) to participate in the formal economy.

- Organizational structure and procedures

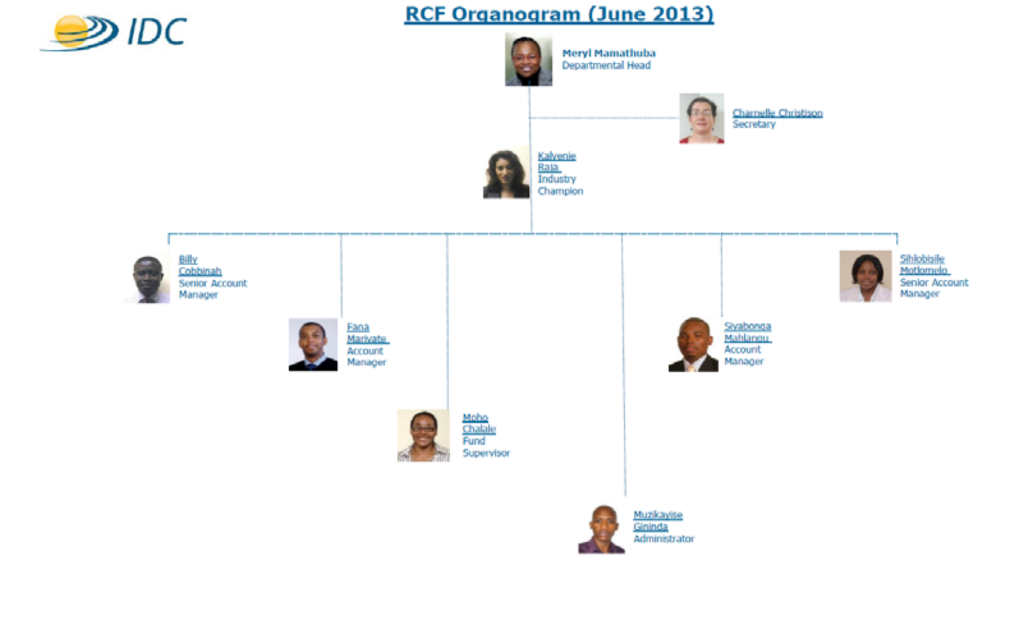
  - The RCF unit organization

The RCF unit has evolved several times during the course of the RCF 1 and RCF 2 projects, with significant staff turnover. The unit initially depended on two and later three Account Officers in charge of the ante phase of the investment and Client Care Officers looking at the post commitment follow up. The team under the responsibility of the DFD head now comprises five account officers, however bearing in mind their involvement with the other IDC funds (see above). The team also has a couple of administrative staff to support the programme reporting requirements.

The members of DFD work as per IDC procedures which include task description.
The Unit is supported by the IDC various technical departments.

The evaluators have been favourably impressed by the systematic electronic filing system of the clients' documents. However, it seems that in practice, the RCF has difficulties in having access to some of the documents of some of the IDC units or department regarding their clients. This should be improved.

The organisation chart is now as follows:
Box 2 : RCF 2 Organization chart[34]



Source : RCF 2

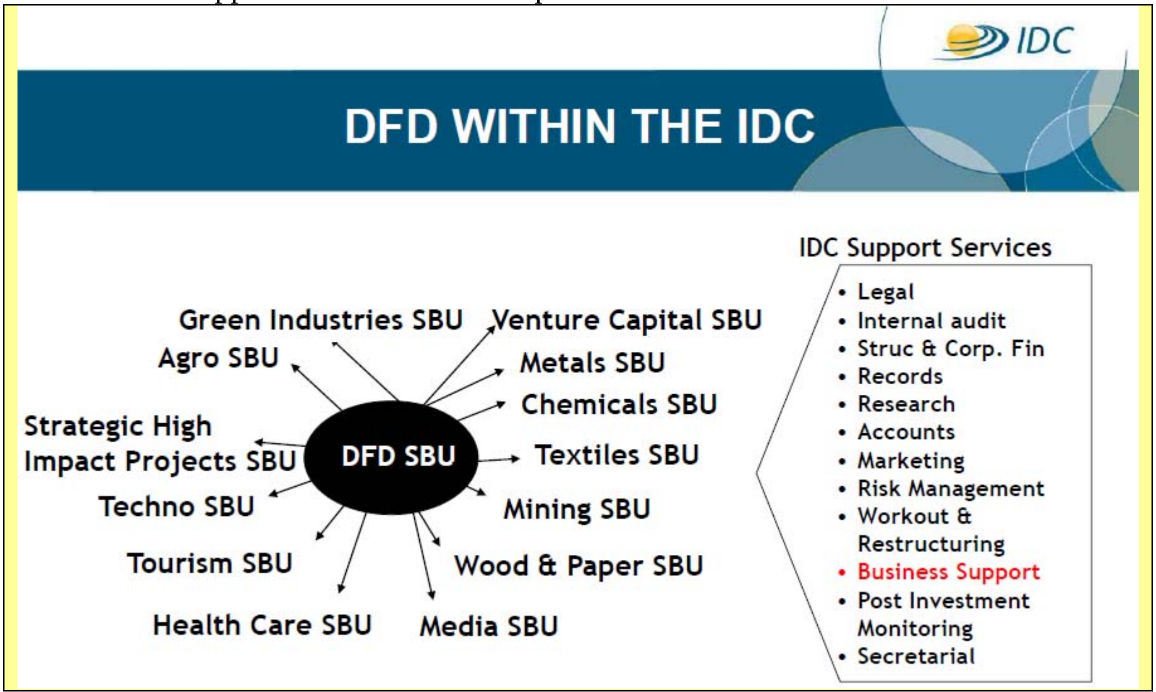
- Support by IDC various departments

The RCF uses the assistance of a number of IDC Strategic Business Units (SBUs) and other IDC Departments in the course of its activities, thereby benefiting from professional expertise in the various fields of operation.

The various departments of IDC intervene to analyse the risks, to provide pricing guidance, sectoral expertise per industrial sector, Business Support Services, accounting, monitoring.

[34] As per the RCF 2009/10 Business Planning , 19 – 21 November 2008

Box 3: RCF Support from IDC other Departments



Source: DFD brochure

- The Business Services Department

The BS Department, supporting RCF 2 and IDC clients, was established as part of the Operations Head Office Department in June 2007, building on the BSS IDC grant associated with RCF 2.

Its activities are to provide BSS to IDC clients, (including RCF clients out of the RCF BS grant). Responsibilities as far as RCF is concerned is to systematically produce the needs assessment which now has to accompany all investment applications, to assess all BSS request, obtain credit committee approvals, organise support from vetted outside consultants, monitor BSS commitments, delivery and results. Impact measurement remains a difficult issue which the department has addressed in the past through satisfaction survey conducted with the beneficiaries. A couple of years ago, the BSS Department commissioned a survey by independent experts. It presently tries to develop an impact measurement scheme, with the help of IDC Regional offices.

BSS is delivered on the basis of 50 % payment by the beneficiary, eventually funded through concessionary loan, out of RCF resources. BSS to final investees of the Niche Fund is organised directly by the funds themselves, out of the BSS allocation which has been granted to each of them, however, the BS Department remains responsible to vet the appointment of the consultants. This BSS support is monitored by the BSS Department.

Main support concern management and mentorship support, but no area is forbidden, all needs are considered and eventually addressed. At this stage, training to important partners of the client, such as out growers or critical suppliers cannot be considered, even if the client and the beneficiary were to co-finance the BSS.

Total amount of BSS delivered yearly by the Department reached about ZAR 21 million, about 10 to 15 % of which would concern RCF.

Future development envisaged by BSS would be to support clients' specific developments, such as the addition of side businesses by Workers' Trusts in conjunction with the project they are associated with. Problem in this regard is that IDC minimum facility is ZAR 1 million, which might be increased soon, to leave some space for the Small Enterprise Finance Agency (SEFA). In this regard BSS does not support SEFA for the time being, while contacts are undertaken with this new organisation within IDC group.

- Risk Management Department

The Risk Management Department is a powerful department in charge of risk management and risk assessment, providing complete due diligence on proposed risks, including the technical, financial, managerial, environmental, anti-laundering, and market risks of the proposed operations as well as assessing the proposed facility in its entirety, i.e. including the terms and conditions, the warrantees issues and providing pricing recommendations.

It conducts its due diligence on all financial operations whatever their size[35]. The proposed operation is then presented to the Credit committee.
Furthermore, an Investment Management Committee is meeting monthly[36] to review the doubtful loans (payment delayed by more than 6 months) and ensure that the proper recovery/restructuring actions are undertaken by the units in charge.

This department is not really aware of the specific high risk features of RCF funding which is mostly used as subordinated loans. Also, the absence of commercial bank support alongside IDC and RCF is not considered as a negative factor, syndicating IDC commitments is not usually considered for smaller enterprises with a high degree of development risks.

The department recognises that it often approves RCF operations with bullet repayment features, without really insisting on assessing the possible exit strategy for such highly back loaded facilities. They recognise a similar approach when considering long term capital funding in favour of Workers' trust or Community trusts' share financing, when repayment relies on the dividends from the investment. It is considered that exit from such patient capital investment will be better negotiated nearer to the due date when results from the investment can be better appreciated. The mission understands this position. It may be interesting however to envisage what could be the various exit possibilities depending on the performance, to prepare the beneficiaries to possible solutions such as loss taking, extension of the financing or transforming debt into investees' equity.

As discussed above, this department also makes recommendation on the pricing of the proposed facilities, however, not for RCF since the conditions of the fund are already decided in the investment guidelines. Usual IDC pricing is usually based on an After Tax IRR of 6 to 10 % plus 50 % of the added value on the share capital funded without any cap.
The department does not have simplified due diligence and risk assessment for the smaller "investments".

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[35] The recent development of SEFA as an IDC subsidiary will probably take responsibility for financing up to ZAR 5 million in the near future, thereby providing relief to the risk department on small enterprise risk assessment.

[36] Three times a year to review equity commitments

- Post Investment Monitoring Department (PIMD)

The RCF commitments follow up falls under the responsibility of the Post Investment Monitoring Department, except for the niche funds commitments which are under the direct supervision of the RCF team.

The PIMD within IDC is in charge of i) organising all the necessary checks and due diligence necessary before the funds can be disbursed and ii) monitoring all IDC loans and investments, financial covenants and other social and environmental conditionalities with the exception of the niche funds investees, iii) valuating the equity investments using either the discounting cash flow or the price earning valuation and iv) monitoring the BSS programme plan approved at the time of the credit application. These follow up are reported quarterly, per client.

The Post monitoring unit will monitor the financial and socio economic performance of the IDC clients as defined in their contracts. The monitoring will be done on a client per client basis and will not be aggregated per type of operations or per unit within IDC. It will be up to the RCF unit to aggregate the information to have an overall view of its impact as well as to follow up on each investment to redress any flaw in the investee commitments and/or performance. It must be noted however that the PIMD is not conducting formal annual review on all IDC/RCF clients due to its work load.
The Post monitoring unit is also in charge of identifying the problem loans when a payment is delayed by more than 6 months. It then alerts the RCF team if necessary as well as the Workout and Restructuring DEPARTMENT if required.

PIMD is not involved in effectively supporting the management of the clients, even in the case of a real equity investment (which are exceptional even for RCF clients). Should PIMD identify a management problem or some other issues, it will then refer the matter to the RCF team and BS Department which shall provide support usually through outside consultants.

Lessons learnt by PIMD regarding SME finance in general are:

- Importance of a good management
- Well managed cash flow
- Effective BSS support
- Good market analysis

- The industrial sectors strategic units

The IDC operations are structured along sector lines of business covering most of the various industrial and services sectors, thereby providing specialised expertise on the various industries.

These sectors usually identify the potential deals proposed to RCF, on a co-financing basis, or do provide financing support directly. Usually, it is the Sector Unit which identifies the potential RCF support and prepares the credit application, including for the RCF part, ensuring that the RCF conditionalities are duly applied. It is worth noting that in a number of the cases identified, IDC is also investing directly as an equity investor, such investment being booked in IDC accounts. Such investment translates into Board representation which is assumed by the IDC sector representative.

The IDC sector does request BSS from the BS Department to support its clients, such as RCF funded Workers' Trusts.

The Agro-Industries sector unit was particularly active with RCF support, since a number of the investments supported implied strong employment creation. In a few cases, RCF was required to finance on a long term basis at a reasonable cost the share equity entrusted to the project Workers' Trust; interest rate was usually set at 5 % per annum, with or without upside, net of tax, which translates in a high 12 % pa gross rate, most of the interest being carried forward when the project will start to pay dividend. The main issues in this regard concerned the absence of involvement of the Workers' trust in the management of the enterprise for lack of competence, the difficult exit strategy for RCF due to the high leveraged induced by the Workers' trust financing, while the workers do not feel for a great number of years to have a real ownership in the project. In practice such Workers' trust financial scheme mostly provides leveraged financial commitments disguised as BEE shareholding involvement.

This scheme which was initially developed under RCF 1 became a standard example of Workers' Trust support. It was replicated not only under RCF 2 financing but also under other RCF Agro funds.

As a conclusion, the Agro-industries unit does recommend the extension of RCF 2 in the future.

- The Workout and Restructuring (WR) Department

This Department is in charge of negotiating and designing restructured financial contracts with IDC clients. As such it is in charge of conducting the restructuring negotiations with the RCF clients.

Should there be a chance for the client to recover, they do use BSS to comfort the management through the appointment of consultants, the main drawback being that these consultants are usually short term and the improvements they bring along do not last.

The department also does consider to replace impaired loans by a share in the equity, however with the result sometimes that management loose interest estimating that it is not their own business anymore.

The department does not seem to make any difference between the IDC commitments and the RCF commitments in their negotiation to restructure the facilities, not taking into consideration the higher risk situation of RCF which might imply to take some loss on the RCF portion to the benefit of the IDC commitments.

Finally, the department has no special procedures for smaller enterprises; they do not work with SEFA which is fully independent in this regard.

It was noticed however that the clients visited did not understand this separation of tasks between the Post monitoring unit, the RCF unit and the WR unit.

- The Venture Capital SBU

The Venture Capital SBU, the focus of which is to target investment in High Technology start-ups, operates exactly as a venture capital fund. Its added value compared to the dynamic venture capital industry consists of targeting exclusively start-ups, which is not usually favoured by traditional venture capital funds. Let's mention in this regard that the VC unit has initiated a business angel hub with other investors.

Box 4: The Venture Capital SBU

The Venture Capital SBU (VC SBU) has been created in 2005 as an IDC ring fenced fund. Its capital allocation by IDC was ZAR 250 million initially, increased to 750 million (of which ZAR 700 million are already committed), invested in 40 enterprises, as minority share capital (25,01 to 49,99 % of SME equity) of SME start up, with board representation, for amount between ZAR 1 million up to maximum ZAR 15 million for a first time investment, into companies with a South African controlled unique intellectual property process, with a targeted after tax hurdle rate of 30 %, to finance all required expenses/investments on a step by step basis. As of today, only one investment has been written off.

Instruments used are exclusively equity, eventually accompanied by shareholders' loans, while quasi equity only consists of convertible loans.

The expected financial return is the only requirement; no other social or environmental covenants are included. After about 8 years since the start of the VC Unit, no exit has yet been organised and it is therefore too early to assess the financial performance. It appears however that the expected returns were somehow optimistic. Investment sectors have been defined as high technology sectors.

The 40 investees have on average 10 to 12 employees with the largest having about 80. Investees are sometime supported by IDC specific financing, but usually, the investees rely on the commercial banks for their current financial borrowing needs.
VC SBU intervenes as a "hands on" investor with involvement at the executive management level at least on a monthly basis through a strict shareholders' agreement, based on monthly management reports, with the board members being from IDC but not from the VC SBU, or fully independent from IDC, to ensure independent representation. Should further assistance be required, the VC Unit can access the BS Unit for outside support. The investment management rests with the VC Unit, it is not delegated to the PIMD as for the other IDC departments.

The monitoring of the investments is done quarterly, with an individual and global valuation of the VC SBU investments, to follow the progress of each individual investment as well as the performance/value of the Fund.

Investments opportunities arise i) from direct requests received by IDC (usually through the industrial sectors SBUs), or ii) from referrals by existing investees or by commercial banks or iii) by active marketing on the part of the VC SBU towards R&D departments of universities. This last channel is the most effective.

At this stage they do not have exit strategy experience, but their plan is either for their investment to be acquired by big players in the market or if the SME is successful to accompany the enterprise in its development, until eventually floatation on the financial markets can be organised. They do not have a time frame for their investments.

The VC SBU is considered resource intensive, with about four enterprises managed by one account officer, each officer being also in charge of new deal making, post investment management, administration and contribution to strategic reviews. The VC Unit has 13 account officers at the moment.

The VC SBU had some contacts with the RCF SBU but conclusions were that each entity had a very different focus and did not have cooperation opportunities. The Unit express a willingness to get in touch with EIB to envisage co-investments or exit strategies.

Despite their target is made up of start-ups, i.e. initially small enterprises, there is no cooperation yet with SEFA, due to the recent reorganisation of the small and micro enterprise department. Contacts have been going on with Business Partners as well as with the Technology Investment Agency without concrete results for the time being.

The VC SBU did not try so far to leverage its IDC capital allocation from other investors, building up its track record. A further increase of the fund allocated by IDF is being considered. It is hoped that a further tranche of ZAR 500 million be allocated to the VC Unit.

7.4 Annexe: Brief RCF 1 portfolio analysis

RCF 1 Results

1. <u>Access to finance for SMEs and emerging entrepreneurs enhanced</u>

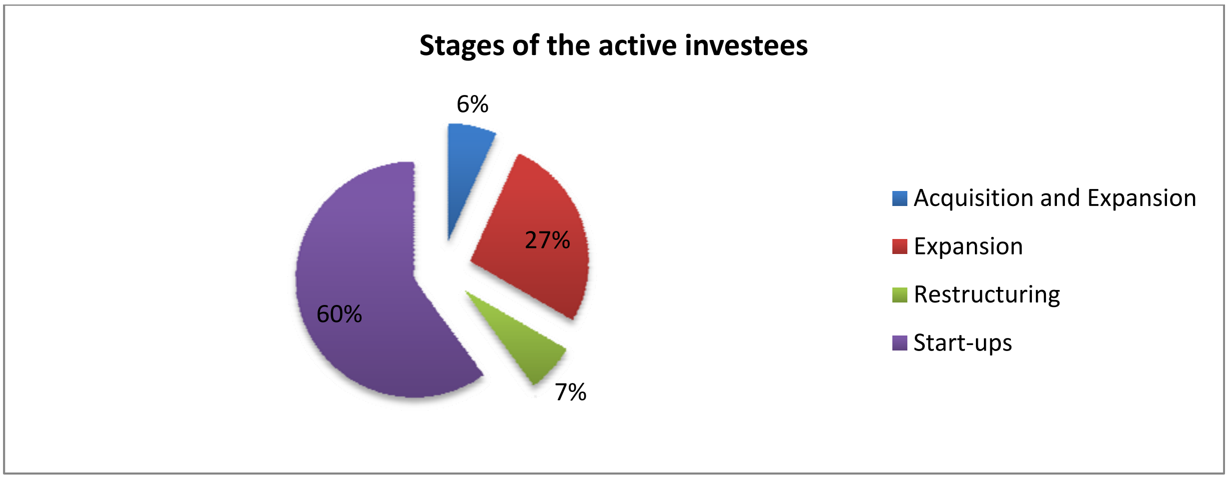
From the portfolio data provided, RCF 1 supported a total of 70 SMEs including write offs and exits to the value of ZAR 512,131,244. The overall picture of RCF 1 according to the portfolio data is as follows:

- Active (17 investees including 2 Niche Funds, 24%);
- Write offs (30 investees including one Niche Fund, 43%); and
- Exits (23 investees, 33%)

There are 15 investees; three have been refinanced under the Direct Investment Channel to the value of ZAR 279,229,819 in the primary agriculture, agro-processing, brick manufacturing, electronics, healthcare, media, metal products, metals, technology and tourism sectors. There are also 2 investees under the Niche Fund Channel to the value of ZAR 66,200,000.

The active SMEs required financing for the various stages that they were in with most of them, nine are start-ups, one acquisition and expansion, four expansions, one restructuring and this is shown in Figure 1 below.

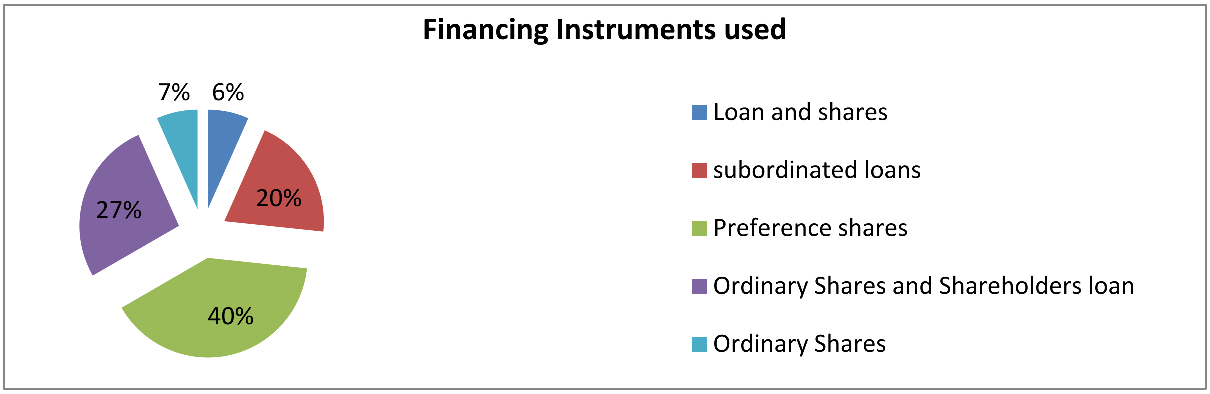
Figure 1: Stages of the Investees



Source: RCF 1 Portfolio data

RCF 1 portfolio has a number of financing instruments for its investees with preference shares, shareholders loans and subordinated loans the most common instruments. Equity or quasi equity is the most dominant form of financing used by RCF1. Figure 2 shows the various instruments used for the active SMEs.

Figure 2: Financing Instruments used for active investees



Source: RCF 1 Portfolio Data

- Exits

RCF 1 saw 23 successful exits to the value of ZAR 57 723 740 and this is 11% of the amount invested in RCF 1. Table 1 shows the sectors and amounts invested per sector in all the successful exits.

Table 1: Number of exits and value per sector

Sector	**Number**	**Value (ZAR)**
Agriculture	2	9 203 740.00
Bakery	1	2 000 000.00
Bricks (specialised)	1	2 300 000.00
Chemicals	4	10 500 000.00
Health Care	2	4 100 000.00
Metal products	2	3 100 000.00
Metals	2	7 500 000.00
Mining	1	3 000 000.00
Paper products	1	2 400 000.00
Techno (Communication)	1	5 000 000.00
Tourism	1	4 000 000.00
Transport (Freight)	2	2 750 000.00
Wood products (coffins)	3	1 870 000.00
	23	**57 723 740.00**

Source: RCF 1 Portfolio data

- Write offs

There were 29 write offs to the value of ZAR 87 971 182 at a percentage of 17% of the total value of RCF 1. Table 2 shows the full list of the investees that were written off in the RCF 1.

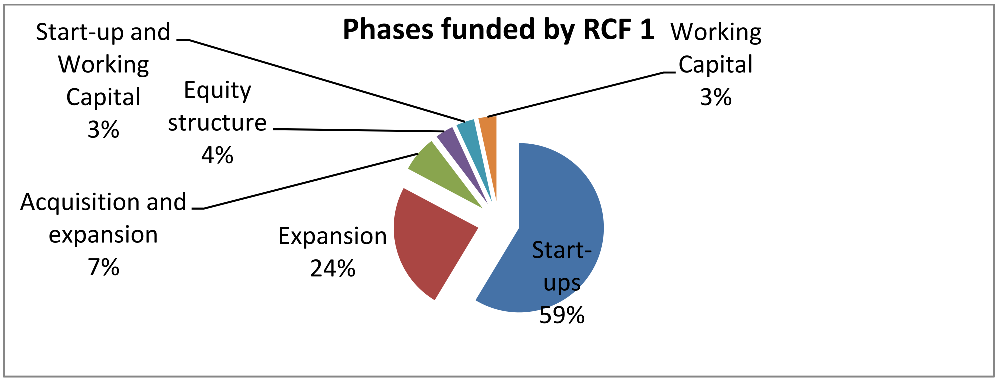
There was also one write off in the niche fund channel to the value of ZAR 21 006 503 in the Forestry and Wood Sector due to fund management dispute which affected investees. The bulk of the write offs under the Direct Channel were agriculture at 25%, followed by textiles at 21% and healthcare at 15%. The failures in agriculture were mainly influenced by the strengthening of the rand which made the exports non-viable. Three investments were written off in the textile sector, the reasons for the write offs were to do with strengthening of the rand in the one case which was financed twice while in the other case, the factory was burnt down and foul play was suspected. In the case of the health sector, RCF 1 supported two investees, one of which was a fraudulent case and in the other investee there was limited assessment of the new business model which led to the company failing to secure adequate markets. This is another clear demonstration of the concentration risk where two investees account for 15% of the write offs. Lack of access to markets as well as currency risks and bad management appear to be the main causes of write offs. It is also important to note that of the 23 SMEs written off, only 1 investee received business support to the tune of ZAR 142 502.

Table 2: Overview of RCF 1 Write offs

Sector	**Regions**	**Value (ZAR)**	**Instrument**
Agriculture (Flowers)	3 in Gauteng and 1 in Limpopo	21 810 025	4 ordinary shares & shareholders loan
Agro- processing (soya)	Eastern Cape	1 720 000	Preference shares
Bricks	2 Gauteng	2 200 000	Preference shares and 1 subordinated loan
Chemical products	Western Cape	300 250	Ordinary shares & shareholders loan
Education	Gauteng	375 000	Subordinated loan
Healthcare	Kwazulu Natal and Gauteng	14 000 000	2 Subordinated Loans
Metal Products (automotive products)	Gauteng and Mpumalanga	1 784 000	2 Subordinated Loans
Metals	Gauteng	2 500 000	Subordinated Loan
Mining (coal)	North West	2 000 000	Subordinated Loan
Mining (diamond)	Western Cape	10 000 000	Debenture
Mining (diamonds)	Northern Cape	3 173 257	Convertible loan
Motion picture (documentary)	Western Cape and Gauteng	1 899 928	2 Venture loans
Techno	2 Gauteng	3 800 000	Preference shares and 1 subordinated loan
Textiles	Gauteng and 2 Eastern Cape	18 149 969	Subordinated Loan and 2 Convertible Preference shares
Tourism (hotel)	Eastern Cape, Northern Cape and KwaZulu Natal	2 558 753	2 Subordinated loan and 1 Loan
Wood & Paper	Western Cape and Limpopo	1 700 000	2 Subordinated loan
		87 971 182	

These investees received RCF funding while in various phases of their various businesses but the majority of were start-ups as shown in Figure 3 below.

Figure 3: Phases funded by RCF 1



Source: RCF 1 Portfolio Data

2. Enhanced support given to sectors with high unemployment/empowerment impact, e.g. tourism, agriculture and rural development

RCF 1 supported the priority sectors and regions outside the highly developed provinces such as Gauteng and Western Cape. Table 3 shows the breakdown of RCF 1 support in the various sectors and regions in the country.

Table 3: RCF 1 support in the sectors per province

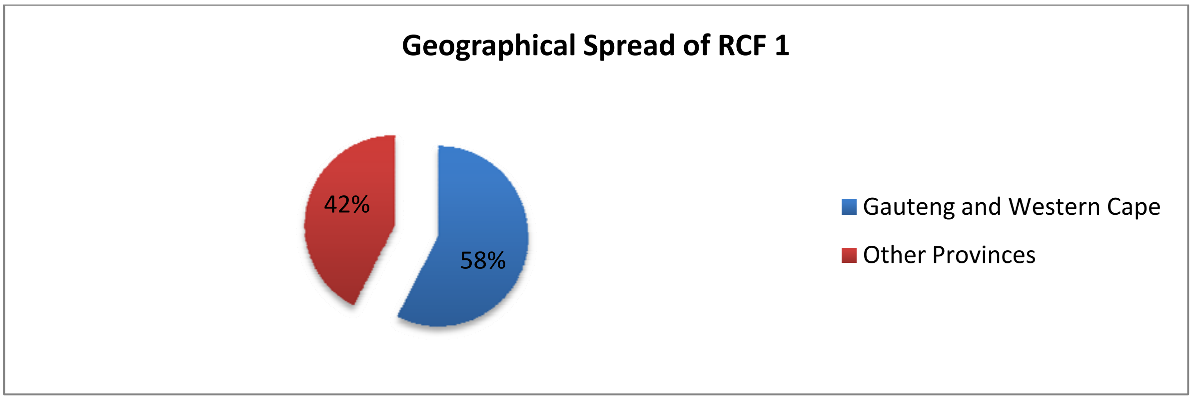
Sector	**Provinces**	**Value (ZAR)**	**Percentage**
Agriculture	2 Eastern Cape, 2 Limpopo, Northern Cape and 3 Gauteng	55 999 965	25%
Agro- processing (soya)	Eastern Cape, Western Cape and North West	15 232 000	6.7%
Bakery	Gauteng	2 000 000	0.8%
Bricks	Mpumalanga, Western Cape and 2 Gauteng	5 040 000	2%
Chemical products	Western Cape, 2 Gauteng and 2 KwaZulu Natal	10 800 250	4.7%
Education	Gauteng	375 000	0.1%
Electronics	Western Cape	720 000	0.3%
Health Care	3 Gauteng, EC and KZN	25 820 000	11%
Media	Western Cape and Gauteng	3 200 000	1.4%
Metal products	3 Gauteng, 2 Western Cape and Mpumalanga	8 027 034	3.5%
Metals	4 Gauteng	13 000 000	5.7%
Mining	Kwazulu Natal, North West, Northern Cape and Western Cape	18 173 257	8%

Motion picture (documentary)	Western Cape, Gauteng	1 899 928	0.8%
Paper products	Gauteng	2 400 000	1%
Techno	Western Cape, 3 Gauteng	16 300 000	7.2%
Textiles	Gauteng, 2 Eastern Cape	18 149 969	8%
Tourism	Gauteng, Limpopo, Eastern Cape, Mpumalanga, KwaZulu Natal, Northern Cape	22 759 153	10%
Transport (Freight)	Limpopo, KwaZulu Natal	2 750 000	1.2%
Wood & Paper	Western Cape, Limpopo	1 700 000	0.8%
Wood products (coffins)	2 KwaZulu Natal, Western Cape	1 870 000	0.8%
		226 216 556	**100%**

Source: RCF 1 Portfolio Data

Thirty five per cent of the RCF 1 funding in value terms was in the priority sectors of tourism and agriculture. Figure 5 shows that in terms of the geographic spread, 58% of the investees were in the more developed provinces of Gauteng and the Western Cape.

Figure 5: RCF 1 Geographical Spread



Source: RCF 1 Portfolio Data

3. <u>Technical, financial and management skills transferred to members of HDP communities</u>
Among the active SMEs, only 2 investees received BSS support amounting to ZAR 3 661 561. One of the investees was in the electronics sector and in the expansion phase while the other was a start-up in agro-processing.

Lessons Learnt

Based on the experience gathered during management of the RCF 1 portfolio, a number of key lessons have been learnt so far, the lessons can be divided into the following categories:

Pre investment due diligence

A number of failures can be attributed to weak management of the investees, it is therefore important that during the pre-investment due diligence, IDC should adequately assess the management team based on the complexities of the business. For example, there was no thorough assessment of the management team's experience or knowledge on the new area of business in the case of V VAC Cleaning Machines which ventured into a new area of business where management lacked knowledge. In such cases, BSS should have been a key component of the intervention. Sensitivity analysis should be undertaken especially for investments that are linked to foreign exchange earnings, for example, Motswedi Flowers and Breathetex Investments collapsed due to the strengthening of the Rand and this could have been foreseen during the pre-investment due diligence if a currency sensitivity analysis had been conducted. Such sensitivity analysis should be extended to other variables including production costs and pricing that might impact negatively on the business.

Access to Markets

While access to markets is an important consideration, this should normally be assessed during the pre-investment due diligence process. Some of the projects that failed were relying on a single market, for example, Marble Gold/AW Timber lost a contract with Mondi and could not find sustainable alternative clients, Rustmin was also highly dependent on contracts from Anglo while Chrisvencia relied on a single market that failed and a result the company struggled to continue operations. A diversified market is always a good condition precedent for successful investments.

Management/Business Support

The importance of appropriate management skills to deal with critical areas of the business such as production, sales, project management, financial management etc. cannot be underestimated. Good corporate governance is very important especially the relationships between shareholders and management, for example in the case of NDC Kamfersdam, shareholders had poor working relationships with management, this affected the business operations. Afripath Medical failed due to the fact that they were dealing with questionable suppliers and did not have solid corporate governance structures in place. RCF should consider appointing independent directors in transactions where it is prudent to do so. For new entrants into a sector, with no prior experience, involvement of Business Support should be considered during the implementation of the project. In the event that investees change their business model, IDC should ensure that there is strong management with appropriate skills to manage the transition. In sectors that require continuous product development, ensure that investees are supported with product development specialists. In cases where IDC is financing new manufacturing facilities, investees should be supported by experienced project management experts. Lack of project management skills results in severe delays and consequent delayed start up. New technologies are often a high risk area and therefore require special attention.

Post Investment Monitoring

This area is closely linked to the one above, the difference is that monitoring is an external undertaking by IDC whose objective is to check on deviations from the original plans and trigger an early warning in case of any problems. Therefore stringent monitoring of clients is needed at all times. There are a number of lessons that have been learnt related to post investment monitoring which include the following:

Project promoters to provide security to ensure commitment, legal recourse to be in place to prevent promoters from developing second series without discussion with IDC.

- IDC should aim to take action if the client is in arrears for three months. During the "breathing period", if a restructuring appears unfeasible, the IDC could then negotiate with other companies to take over the contracts and assets.
- Check with Insurance Companies if policy still in place and need to have insurance policies ceded to IDC.

7.5 Annexe: Medium Term evaluation and ROM monitoring recommendations and comments

- MTR recommendations

Recommendations to the EC	**Comments**
In view of the satisfactory implementation of RCF 2, despite a number of implementation features can be improved, the evaluators recommend that the Programme be extended for a further two years so as to allow time to invest the third tranche.	Done
While extending the Programme, it should be recommended that RCF 1 re-flows be utilised first to fund new Direct Channel and Niche Fund Channel investments, before using RCF 2 funds, so as to insure that RCF 1 is revolving;	RCF 1 reflows were transferred to support another IDC fund called Technology Venture Capital (TVC) Fund. RCF 2 reflows have not been reinvested. Plans are to use them for TVC funding.
The Increase Investment and Employment in Africa result should be abandoned, as being out of focus for the RCF programme.	This covenant has been made optional. In 2010, the EC adopted the MTR recommendation not to consider RCF's contribution to increased South African SME investments in other African countries.
Recommendations to the dti	
The dti should define the PSC responsibilities through a precise Charter. The present definition of the PSC tasks based on the FA: "*The PSC will provide the project management with guidance and policy direction*" is insufficient.	Terms of reference for the PSC have been formalised in May 2011. The description of the PSC duties is still very succinct.
The number of PSC members should be reduced to a maximum of eight members to achieve an effective support to the RCF management through efficient debates over the raised issues.	Number of PSC statutory members is limited to 13, one of them, the EU, having observer status.
Consider waiving the year on year limitation for the payment of the 10% of the reflows management fee to IDC, or even consider granting a higher yearly percentage fee on the funds under management, provided the IDC takes a minimal percentage share in the RCF risks (to increase the incentive on IDC to propose quality risks) and/or take charge of the due diligence and post monitoring costs implied by third party loans.	No change made
Recommendations to the EIB	
It is recommended the EIB gets more involved with the various IDC SBUs, and more particularly the Risk Management SBU which seems very powerful in determining the financial instrument to be used as well as the pricing of the investments.	Limited involvement has continued as before
The EIB should be more involved to find ways to unlock the Third Party Channel operations and	EIB did not try to get the Third Party channel off the

develop third party financing.	ground after the Mid-term Review through high ranking follow up. A decision was taken not to pursue the TCP further as it had failed. The funds were to be used either for the Niche Fund or the Direct Channels.
Recommendations to the IDC/RCF	
➢ Mission and task definition	
To empower the RCF SBU and its account officers, the evaluators recommend to precisely define the responsibilities of the RCF SBU, especially i) related to the “equity” investor responsibilities to the clients, ii) responsibilities vis a vis the other IDC SBUs and iii) establish proper job descriptions, more comprehensive than the existing implied ones described in the procedures.	Responsibilities of RCF staff vis a vis clients remain back stage behind IDC officers
The responsibilities of the RCF account officers shall be clarified and confirmed vis a vis the other IDC SBUs to enhance their responsibilities in a number of area, such as their involvement in the direct marketing of the RCF Facility, in the SMEs financing needs identification, in the due diligence process, in determining the terms and conditions of the RCF facilities, in the client follow up as a minority shareholder and partner, in the post monitoring and in the potential restructuring processes.	Relationship between RCF and other IDC SBUs is not formalised in a specific document
The evaluators recommend that the IDC as fund manager of the RCF EU funds shall be implicated in the potential risks taken by RCF on its own funds, up to a minimum percentage, as is the practice on the market.	Not done
➢ Client target	
IDC/RCF seems to be more at ease with the larger segment of the SME market and should gradually move up market provided that Khula which is supposed to fill the gap for smaller enterprises comes of age. It is our recommendation to use two third of the Third Party Channel available funds to check each institution capacity to support the financing needs of the smaller SME	Negotiations with Khula and SEFA have been going on for couple of years without tangible results in view of the profound reorganisation of these entities
The evaluators recommend dropping the required result number 6: Increased investment and employment in Africa, in view of the difficulty for an HDP SME to engage in international operations, except in unusual instances.	See above This indicator was completely relaxed through a letter from the EU. It was decided that it would not be practical to issue another rider.
➢ Equity finance instruments	

Use proper equity finance, so as to avoid a financial drain on RCF client cash flow, especially after a few years from granting the financing facility, when the working capital requirements of the client are increasing;	Efforts to make subordinated loans resemble more equity have been pursued through lengthened grace period and increased up side compared to fix rate.
Avoid a facility having similar repayment schedule as the commercial term lender (IDC or third party), which will drain the company's financial resources concurrently (loan repayment as well as "quasi equity" repayment), discouraging any commercial lender to relay the IDC financing;	Same as above
Avoid heavy interest/upside not linked to the companies' cash flow or to the enterprise valuation increase;	Same as above
Avoid having subordinated loans only subordinated to the IDC loan which shall discourage other commercial lenders to support the company;	Since there were usually no commercial lenders involved, this recommendation did not apply. IDC was of the view that the main issue was not about equity, preference shares or subordinated loans and decided to review on a case by case basis and apply the appropriate financing instrument depending on the need.
Consider taking systematically a minimum equity participation of 26%, even for a nominal amount, to accompany the term finance granted, possibly as a shareholder's loan, so as to ensure that RCF officers and clients really act as shareholders partners in the SME management;	No minimum limit has been set up
Depending on the possibility to cover the Third Party Channel costs for RCF to conduct due diligence by itself plus monitoring the socio economic indicators, and depending on the volume of expected operations to be sourced from each third party, consider embedding one of RCF account officer with the third party to participate in the due diligence and risk committees involved with the proposed co-investment;	Implementation of Third party channel has not progressed
Have a legal counsel to assess the risk of a lender giving management advice to its borrower, be construed as "de fait" management and put the lender at risk from the borrower's creditors on its own assets, in case of the borrower being in financial difficulty.	Done
➢ Business Services Support	
A representative of the BS Department should be systematically invited to attend the RCF weekly management meetings;	Not done. No systematic management meetings by RCF
BSS should be involved "ex ante" if a proposed operation needs to be verified as far as its business plan or its feasibility study are concerned. The budget authorised for such investigation should not be too small (Cf. Box 4: The case of the feasibility study). The RCF unit shall be responsible to	Done, it is now a condition for an assessment of BS needs be attached to investment application

approach the BSP Unit with such request within an approved budget. It should be up to the BSP Unit to organise the required expertise within the authorised budget in due course.	
Regarding “ex post” BSS, it is recommended that each and every authorised commitment shall be informed to the BSP Unit, it being provided with a copy of the due diligence exercise, with a request to have an analysis of the strengths and weaknesses of the company’s management conducted within an authorised budget and within a precise time frame. Such review shall provide recommendations for the support of the investees in the most effective manner.	Done
Based on this review, the RCF shall agree to finance support to the investee over a one to three year period; such support to be organised by the BS Department within an approved budget.	Business Support was delivered for some investees over a one to three year period
Finally, it is recommended that if the RCF account officers are not empowered to get closely involved with the support of the investees management, “a referent” (an expert in charge of a precise investee) be appointed by the BS unit in accordance with the RCF, to support investees through regular 3 months visits and reporting.	This does not seem to be the case
➢ Third party channel	
Our first recommendation would be maintaining the Third Party Channel, up to 1/3rd of the initial amount to serve investments proposed by third parties, below ZAR 1 million, provided the RCF/IDC is confident on being able to deliver an answer on individual proposals within one month, including securing the EIB green light. This would most probably entail to devise a simpler due diligence process for smaller risks/companies and require the IDC to take an important Policy Decision: to waive its present policy to apply the full due diligence process to even the smaller investments/companies. It would also imply to gear up the RCF team to be able to assume the proposed new responsibilities and estimate the costs/fees of such increased responsibilities. Finally, due incentives should be built up in the form of fees or new prospective clients discovery for IDC and increased responsibilities and empowerment for RCF account officers. A minimal risk sharing by the third party in the RCF facility should be considered.	Not done
Our second recommendation would be to liaise with the Khula Enterprise Finance (Khula) and work out an agreement with them to harness their small enterprises direct financing capacity (due to be authorised in the coming months). The co-operation with Khula could be in a form similar to the support granted by RCF to the niche funds, i.e. subject to the RCF conditionalities, to the RCF funds being leveraged up to a minimum of 100%, subject to a satisfactory due diligence on the capacity and ability of Khula. The evaluators understand that Khula at present is not yet authorised to grant direct financing to the small enterprises, but that its Charter is in the process of being reviewed in this respect. Such scheme up to 1/3rd of the Third Party Channel funds would be subject to Khula gearing up its ability/capacity to IDC/RCF satisfaction, IDC possibly providing Khula with strong Business	Not done

Support Services. The advantage of this solution would be on the one hand to support the capacity development of Khula as well as achieving financial support to the lower segment of the SME market. To ensure success of this sub channel, due consideration shall be given to provide incentive for its success not only to Khula, but also to IDC and RCF.	
Our third recommendation would be to entrust the remaining 1/3rd of the funds to the Direct Channel, with a recommendation/conditionality to target the smaller end of the market.	Not done
➢ Performance indicators	
Consider benchmarking the performance indicators against the national scorecard indicators to facilitate the assessment of the RCF results;	Not done
The evaluators recommend simplifying the performance indicators by focusing on the FA seven[37] key indicators, leaving the "auxiliary" indicators defined by the EIB to be appreciated flexibly by RCF and EIB on a case per case basis.	Not done
➢ Post monitoring	
It is recommended that the RCF SBY 2009/10 Business Planning be translated into a more detailed RCF EU Fund Annual Work Plan against which the activities and results described in the quarterly reports could be benchmarked. Cf. paragraph 3.3.4 Post monitoring issue.	This has not been done
It is recommended that a yearly post monitoring of the effective socio-economic indicators achieved should be organised for RCF 1 as well as RCF 2, and its conclusions analysed to draw lessons for the future.	Follow up is done at the DFD level through analysis of the investees' reports in this regard.
Similarly, it is recommended that a study be made or commissioned to assess the impact of the environment programmes as well as the HIV Health programmes on the HDP population involved with the investees.	One survey was conducted which pointed to some inefficiencies in the HIV and environment plans. However, the survey was not an impact analysis.
It is recommended that the financial analysis of the portfolio of clients be conducted more deeply in the quarterly reports, including the evaluation and appreciation of the due and delayed IRR and principal repayments, its composition, its importance compared to the principal repayments still due, it repartition among the various type of clients (on track, under supervision, being restructured and legal action), so as to understand the likely consequences regarding sustainability and to draw lessons for the future pricing structure.	Not done
Conduct a precise analysis of the interest and principal amounts postponed under RCF 1 and 2, and plan specific guidelines to provide an exit strategy for RCF, including the possibility to transform the	This was not done and is still highly recommended.

[37] . Suggested to be reduced to six by suppressing the out of South Africa related investments

accumulated unpaid loan principal into equity.	

- ROM recommendations

To all Niche funds: the additionality of RCF should be impressed i.e. sub-investees should be riskier investments promoting HDP share ownership and employment especially for women and with an emphasis on HIV and environment.	Done, but not always taken into account, the balance between Development objectives and financial returns weighting more towards the financial returns. The Niche Funds have fully understood and embraced the importance of the developmental indicators and are all doing their best to comply. However, at this stage there are seven investments that are not RCF compliant.
It should be ensured that all investees have HIV/AIDs and environmental plans and adhere to them as field visits indicate this is not occurring in 100% of the cases as reported.	No systematic control of clients' reporting in this regard has been organised
Partnerships with Business Partners and NEF should be explored and developed. In the case of BP, the possibility of EIB undertaking the due diligence should be assessed.	Contacts were originated but not conclusive
The annual client monitoring exercise that is being undertaken should look at satisfaction of investees with the IDC process and issues which are appearing from initial enquiry to receipt of funds; the quality of jobs being created; if BSS support is needed by Workers Trusts; whether HIV/AIDS and environmental plans actually exist and are being implemented. The report should do a breakdown of SMEs according to their size to give an informed opinion on whether smaller SMEs are being focussed upon or marginalised. It should also study a sample of rejected applicants to assess what factors led to a negative outcome.	No systematic review of the portfolio is conducted by RCF
The condition of 12 months to reach 25%+1 HDP ownership should be flexibility applied if genuine constrains exist which are flagged by the investee in time and if progress towards increased HDP ownership is evident.	Done
Success stories, good practices and lessons being learnt should be routinely documented by IDC for its own and others' learning.	IDC has created a Knowledge Management Department which collects lessons learnt from the various IDC departments/units, including ECF, especially from the IDC Franchise unit RCF investments.

7.6 Annexe: Conditions for the release of the tranches as per the Financial Agreement, modified by rider 1 and 2

Event	Amount available for support to RCF	Date of request for tranche release from NAO	Date of tranche release by the EC	Conditions for tranche release
First Fixed Tranche	EUR 20.0 million		December 2006	(i) General conditions as set out in Table A3.2 (ii) Specific conditions as set out in Table
Second Fixed Tranche	EUR 13.5 million		December 2008	(i) General conditions as set out in Table A3.2 (ii) Specific conditions as set out in Table A3
Third Fixed Tranche	EUR 13.73 million	December 2009	March 2010	(i) General conditions as set out in Table A3.2 (ii) Specific conditions as set out in Table A3.3(a)

Table A3.2: General Conditions for Tranche Release

Conditions	**Verification**	**Comments by the final evaluation mission**
A sound national macroeconomic environment remains in place or does not unduly put at risk the achievement of the objectives of the EC support [1]	Opinion of the Ambassador of the EC Delegation in South Africa based on, for example: - Article IV consultations with IMF - Annual Budget review and budget tabled in parliament - Government plan of action programme and report on implementation monitoring and evaluation briefings of economic, social and governance clusters. - Quarterly financial stability review of SA Reserve Bank.	No comment - IMF Article IV review have been produced regularly - Government budgets have been duly voted - A special monitoring scheme has been established: The Government Wide Monitoring and Evaluating System (GWMES) - Reserve Bank did publish their quarterly reporting

IDC Remains solvent[1] RCF continues to meet substantially its development and financial targets, viz: (1) Development outcomes: [3] • Some six thousand jobs for HDPs created as a result of the investments and the BSS at an average cost to the fund of around ZAR 60 000. The approximate indicative targets in time are: First Year: zero new HDP jobs Second Year: 1,879 new HDP jobs Third Year: 1,142 new HDP jobs Fourth Year: 960 new HDP jobs Fifth Year: 1,020 new HDP jobs Sixth Year: 999 new HDP jobs • Around 30% are held by women are created • Approximately 70 SME BEE enterprises have been funded • Investments outside Gauteng and Western Cape should preferably exceed 65% measured in number or in value • RCF participation on average leveraged 100% by IDC or other investors. • As a result of RCF investment in a company it should achieve 25% HDP ownership within one year from investment (2) Financial outcomes: • For RCF II, the programme management will aim towards a re-flow of 100% of the after deductions of IDC management fee and expected and/or actual delinquencies. • The fund should target IRRs that are market related in order to be able to achieve its portfolio return goal. An acceptable strategic framework for the dti: ., The sector programme (i.e.: the dti's Medium Term Strategic Plan as it relates to the provision of support to	• Latest annual report • Annual Audit reports from the IDC external auditors • Quarterly RCF progress reports on implementation • Progress reports for actions to be taken to address findings of the audits • Minutes of steering committee meetings • Annual EIB report on Fund performance • Annual IDC report on implementation of RCF	• Confirmed from latest annual report • Clean audit report • Reports produced • Not required since audits were usually clean • Minutes produced • EIB reports produced • IDC reports produced • Development and financial outcomes were usually met, even if subject to evolution in time.

[1] Disbursement may proceed if, in the opinion of the EC, an unfavourable status does not unduly put at risk the achievements of the programme.

[2] Not necessarily, due to timing, for the financial year prior to the year of request

[3] These conditions will apply to the second and third tranche. As they are directly related to past performance, they cannot apply to the first tranche. Unfavourable reports will require the development of a strategy to address the issues raised

SPECIAL CONDITIONS FOR RELEASE OF TRANCHES:

Table A3.3 (a): First Tranche – 2005/2006

Special Conditions: Release of Tranche 1				Comments by final evaluation mission
Portion	Indicative request	Indicative Payment	Conditions	
Fixed	02/2006	03/2006	Satisfactory outcome of the audit of RCF1	Done
€			Agreement in place with EIB for monitoring of RCF operations	Done
20,000,000			Confirmation of availability of funds for the provision of business support services.	Done
			Formal Agreement between the dti and IDC concerning the management of the Fund	Done
			Presentation of the annual business plan of the IDC's RCF business unit	Annual business plans were not specifically produced; the FA yearly targets were considered as the yearly objectives
			Agreement on the set-up of the performance monitoring system	Done
			Agreement on targets to be achieved	Done
			Agreement on the annual performance review	Done
			Monitoring system in place	Done
			Submission of request for release of the first tranche.	Done
Special Conditions: Release of Tranche 2				
Portion	Indicative request	Indicative Payment	Conditions	
Fixed	01/2006	03/2006	Annual performance review meeting conducted based on IDC's annual implementation report and EIB performance report.	Done
€ 13,150,000			Satisfactory progress achieved in terms of performance indicators	Acceptable despite delays

			80% commitment rate achieved on funds transferred in the previous tranche.	Commitments stand at ZAR 291 million prior to disbursement of the third tranche, i.e. representing about 86% of funds made available.
			Formal Agreement between the dti and IDC concerning the management of the Fund	Done
			Annual audit conducted	Done
			Performance monitoring system operational	Done

The special conditions for release of tranche 3 are modified to read as follows (with the modified sections highlighted in bold):

Special Conditions: Release of Tranche 3				
Portion	Indicative request time	Indicative payment date	Conditions	
Fixed EUR 13,730,000	12/2009	03/2010	Annual performance review meeting conducted based on IDC's annual implementation report and EIB performance report. Satisfactory performance as detailed for the release of tranche 2.	Done
			Satisfactory progress achieved in terms of performance indicators.	Satisfactory progress
			80% commitment rate achieved on funds transferred in the first tranche and second tranche.	Done
			Satisfactory outcomes of mid-term review.	Done
			Annual audit conducted.	Done

<u>Enclosure No 3 to Addendum No 2 to Financing Agreement No SA/21.031700-05-01</u>

MODIFICATION TO EACH BUDGET ITEM

(All amounts in EUR)

	Budget after Addendum No l	Modification of Addendum No2	Budget after Addendum No2
Budget Support	47,000,000	+230,000	47,230,000
Complementary Support:			
Technical Assistance (EIB)	2,500,000		2,500,000

Evaluation and Reviews	500,000	-230,000	270,000
Audits	0		0
Contingencies	0		0
TOTAL	50,000,000		50,000,000

7.7 Annexe: Investments guidelines

The primary focus of the Fund is on investments in the sector comprised of SMEs, designed to enhance Black Economic Empowerment and to create jobs. In this context, specific investment proposals will be considered against the following guidelines. Subject to the consent of the EIB and IDC, these Investment Guidelines can be revised, within the framework of the Financing Agreement governing the Fund, in accordance with a decision of the PSC and upon an endorsement of such revision by the EC and the DTI.

For the purposes of this Agreement:
"SME" means a company that, at a time either before any investment by the Fund or at the end of the first year of full production in the case of companies that are new projects or start-ups, complies with any one of the following criteria:

- it has less than 100 employees;
- it has an annual turnover of less than ZAR50 million•;
- it has total assets of less than ZAR30 million•;

"Black Economic Empowerment" means funding provided to enterprises in which historically disadvantaged persons (namely those persons who were disenfranchised politically prior to 1994) will hold at least 25% of the issued share capital or the members' interests and will have significant operational involvement in the business of such enterprise.

1. Direct Finance

Sectors – all sectors of the economy are eligible, primary sectors (including agriculture and mining), as well as the industrial, commercial and service sectors. However projects in the armaments field will be excluded, as will projects primarily focused on tobacco production and on gambling. Projects to be financed must be located in South Africa.

Size – 50% of investments by value made from the facility should be less than ZAR 5m each. The maximum investment size for a single investment will be ZAR 15million• although exceptions to this can be considered should there be compelling reasons for this related to the primary purposes of the fund. Minimum investment size will be ZAR 500 000.

Instruments – the fund will be used primarily for equity and quasi-equity investments although conditional loans or convertible loans could also be considered.

Stakes in Investee Companies – Stakes should normally be minority stakes (maximum 45% of voting shares) yet large enough to enable the IDC, through the fund, to be an active partner in each investment. Under certain conditions (e.g. to facilitate a structured buyout) a majority stake could be considered.

• Increased by South African inflation

Exit mechanisms – mechanisms, such as repurchase of shares by project promoters, sales to strategic investors or listings, should be assessed as part of the project evaluation process, with a target of an exit from equity investments by 8-10 years after the initial investment. Longer periods will be allowed for long gestation projects in sectors such as the commercial agriculture and tourism.
Environmental provisions – Investments should comply with South African legislation and environmental issues, including appropriate mitigating measures, should be reviewed by relevant IDC staff.

Evaluation criteria – projects to be financed should be demonstrated to be financially viable, technically feasible, environmentally sound and economically desirable. Empowerment aspects and/or job creation features should be highlighted. The use of the risk capital facility should demonstrate additionality.

IDC is expected to provide co-financing for projects funded through the direct finance facility. Co-financing opportunities with commercial lenders and EU DFIs will be actively sought.

2. Niche Funds[♦]
Sectors – all sectors of the economy are eligible, primary sectors (including agriculture and mining), as well as the industrial, commercial and service sectors. However investments in the armaments field will be excluded, as will investments primarily focused on tobacco production and on gambling. Projects to be financed must be located in South Africa. These restrictions will need to be acknowledged by the niche fund managers. To help ensure continuity, the "200%" principle will apply – in other words if the facility comprises 20% of the niche fund by value then 40% by value of the niche fund investments will need to go into risk capital eligible sectors.

Criteria – investments in niche funds will need to: meet the overall objectives of the risk capital fund; to show a comparative advantage in the meeting of these objectives;

Fund managers will need to: demonstrate a sound track record and/or competence in the field; have sound due diligence procedures (including an assessment of environmental issues).
Size no single investment can account for more than 33% of the maximum allowable funds available for niche investments.

Instruments – the risk capital fund will be an equity investor in the niche fund. The niche fund itself can make available equity, quasi-equity, loans and guarantee products.

Share – the risk capital fund will always be a minority investor in a niche fund; it is intended as a general principle that the IDC will be represented on the relevant investment committee of the niche fund but other means of ensuring appropriate representation will also be considered.

Exit mechanisms - exit from investments under niche funds will be expected within 8-10 years after the initial investment. Longer periods will be allowed for long gestation projects in sectors such as the commercial agriculture and tourism.

[♦] The foreseen continuation of EU support for the Land Reform Credit Facility will mean that it will be evaluated under separate size/instrument/share criteria to those outlined here.

3- Business Support Grants

It is intended as a general rule that Business Support grants will only be made in conjunction with direct investments and/or niche fund investments.

Sectors – refer to allowable sectors under section 1 above.
Exclusions – refer to allowable sectors under section 1 above.
Size –Need for and size of business support grants will be assessed on case by case basis as part of the investment appraisal and decision making process, and can also be assessed and made at a later time, depending on the prevailing circumstances and if deemed necessary by the parties.

Other Criteria – comprehensive empowerment plan in place on project/niche fund level; cost sharing desirable.

Procurement – business support services will be procured from the IDC database in compliance with EC procurement procedures.

4. General provision

Limitation on investments – no investments shall be made, whether through direct finance or niche funds, and no grants shall be made in or to companies or any business entities in which any employee, director or officer of the IDC, the EIB or the EC or any relative or spouse of such a person has an interest, whether direct or indirect, regardless of the nature or size of that interest.

7.8 Annexe: RCF 2 log-frame with evaluators comments and results

Annex: Logical Framework Matrix (including rider 1 and rider 2 modifications)

	Intervention logic	Objectively Verifiable Indicators	Source of verification	Assumptions	Final evaluation mission comments and recommendations
ACTIVITIES					
Overall Objective	To contribute to economic growth of South Africa and to promote the participation of historically disadvantaged people (HDP) in its economy.			The legal framework supporting social stability is in place.	The programme has made a direct contribution to economic growth, although the impact might appear small based on the number of SMEs supported and the jobs created, the catalytic contribution is much more significant especially in terms of the funds that have been put in place as well as the new skills that IDC now possesses which has given the organisation additional ability to make a significant contribution to the economic growth of the country. Through the programme, participation of HDP has increased as is evidenced by the statistics provided by the investees that have been supported.
Project Purpose	Job-creation, SME support and Black Economic Empowerment.	Six thousand sustainable jobs for HDPs created as a result of the investments and the BSS.	IDC / RCF records, independently audited.	SA economy continues to grow at steady and stable rate IDC and other financiers will leverage the EC funds by 100% on average.	RCF has so far supported 5,840 jobs and 63 SMEs. Inclusion of Niche Funds investees that are not fully RCF compliant will exceed the targets set. The indicators defined at the project purpose level have to a large extent been achieved and should be exceeded in a few years in the future even with impairments or cancellations.

Results	1. SMEs access to development funding increased.	Approximately 70 SME BEE enterprises have been funded and EC grant leveraged 100% by IDC and other investors. Possibly a further €20m contributed by other investors. The funding can take place either through 1) the direct channel with IDC as co-investor or 2) with a co-investor in the form of a Niche Fund or 3) direct investment with a 3rd party.	IDC / RCF investment record	IDC and or a third party co-investor will leverage EC funds by 100%. The deal flow provides sufficient adequate investments in terms of profitability and job creation.	The IDC files show that the facility supported 73 clients overall. Currently there are 63 active clients (53 under the Direct Channel and 10 in the Niche Funds) The funds were leveraged at an average of 286% over the course of the 7 years. RCF 2 funds were used by the Niche Funds to attract other investors and there were investments from organisations such as IFC – USD$20 million, AfDB – USD$10 million in the Evolution One Niche Fund.
	2. Increased numbers of <u>new</u> jobs created for HDPs in particular for women.	Six thousand new jobs of which around 30% are held by women are created as a result of the investments and the BSS as follows: Investments outside Gauteng and Western Cape should preferably exceed 65% measured in number or in value.	RCF Quarterly Reports showing actual job creation against planned	Sufficient deal flow can be generated.	RCF has facilitated the creation of 5,840 jobs in the active 63 SMEs that it has supported. The IDC Portfolio data on the facility indicates that the target of at least 30% newly created jobs are held by women. However, as observed during the MTR, IDC is not systematically tracking their investees annually and it is possible that the figures might have changed over the passage of time from the time when they last did a comprehensive survey 2010/11. The geographical spread target was not achieved with the current nominal and value at 59% and 45%

					respectively. Part of the reason why this target has not been met is due to failure to generate sufficient deal flow, an assumption made in the logframe. It is acknowledged that it is not easy to generate deals outside Gauteng and the Western Cape provinces. The fact that about 50% of employment depends on five investees should warrants a specific follow up of these five investees with regard employment creation over time.
	3. A revolving self-sustainable RCF has been established.	For RCF11, the programme management will aim towards a reflow of 100% of the funds after deductions of IDC management fee and expected or actual delinquencies (*replaced through rider 2*: (which is consistent with an ex ante required return on investments of 10% in real terms and a “death rate” of 30%).	IDC / RCF Cash flow records	The market can accept the necessary internal rate of return required.	It is still too early to say whether the fund will revolve and remain sustainable as there have only been 3 exits and reflows to the value of ZAR 30, 295, 705. The set IRR is competitive in the market given the high risk nature of the fund.
	4. Increased BEE though shareholding and possibilities for HDPs to hold managerial positions.	As a result of RCF investment in a company it should achieve 25% HDP ownership within one year from investment.	IDC / RCF records	Sufficient deal flow can be generated.	The IDC has not been able to provide the updated BEE shareholding statistics in all the investees due to limited visits. However, the approved investees either had a 25.1% shareholding or were on course to fulfil it within the stipulated one year. There were 7 applications with a Worker’s Trust component intended to

					improve the BEE shareholding. It is important for RCF to follow up the shareholding positions annually to see whether or not there are any changes.
	5. Access to and use of BSS.	The BSS included in approved allocation requests has been delivered and the total amount available is on target to be used during the life of RCF2. In addition to RCF2 clients, the RCF1 clients who need BSS are also eligible for it. It is recognized that BSS clients may no longer qualify as SMEs at the time they receive the business support.	Audit of BSS services to investees	Up to € 5M will be made available from RCF1 backflows and Government resources The Investees will accept either grant funding, interest bearing loans or non-interest bearing loans.	Only 27 out of the 63 active investees received BSS at a cost of ZAR 20, 247, 155. Of this figure, only ZAR 4, 384, 210 has been disbursed. Access to and use of BSS has improved immensely from the time of the MTR. In fact, through RCF, IDC now undertakes ex-ante a BSS needs survey on all its project applications. BSS is now a major feature in the organisation. The evaluators were not able to obtain from the IDC the ZAR equivalent of the amount set aside for BSS. However, the approved amount is less than half of the estimated total allocation and to make matters worse, the disbursed amount is less than 10%. It might not be possible for the entire amount to be utilised during the life of the fund. One of the Niche Funds has made a request that IDC considers providing the BSS as a loan for their investees.
	6. Increased South African investment in other African countries.	Funding of about 15 South African SMEs investing in other African countries to provide around 500 new jobs.	IDC / RCF investment records		This target was relaxed as the project main geographic result is expected in South Africa and besides the present IDC infrastructure is not yet ready to tackle SME's abroad.

	7. The socio cultural and environmental aspects of Investee businesses have been strengthened.	Every Investee business has HIV/AIDS prevention (*replaced through Rider 2*: socio cultural) and environmental protection plans. The progress against plans is to be monitored and measured yearly.	EIB Monitoring Reports		The investees do not have formal policies but have activities around environmental/HIV awareness. The logframe indicator was that progress against plans would be measured yearly, this has not been done.
Activity 1.1	IDC will promote the RCF facility to increase potential deal flow and achieve a steady flow of high quality deal potential.	Potential deal flow (to be recorded and monitored) should reach at least 400 realistic opportunities for the **six years** implementation period to ensure that RCF participates in the best quality projects. This deal flow target to be modified according to quality investments being presented for approval.	IDC record of promotion activities and deal flow.	IDC will actively promote and continuously search the market for the best opportunities for high quality deals.	The unit in charge of RCF 2 has marketed the facility with input from EIB and other stakeholders. IDC developed an RCF marketing brochure. Some of the marketing activities were ad-hoc.
Activity 1.2	RCF will invest €47.23M over **six years** through the three channels open to it. RCF will provide flexible equity / quasi equity products to SMEs through IDC channels ensuring adequate profit potential and fulfilment of Black Economic Empowerment goals.	Deal making / contracting: First year (Dec 06): 0% Second year (Dec 07): about 21% Third year about (Dec 08) : about 22% Fourth year (Dec 09): about 24% Fifth year (Dec 10): about 19% Sixth year (Dec 11): about 14% Disbursements: First year (Dec 06): 0% Second year (Dec 07): about 2%	RCF/IDC records	IDC's mandate for small business investment continues to apply.	Both Direct and Niche Fund Channels are in line with their target while no deal has been made through the Third Party Channel.

		Third year (Dec 08): about 11% Fourth year (Dec 09): about 14 % Fifth year (Dec 10): about 16% Sixth year (Dec 11): about 28% Seventh year (Dec 12): about 23% Eighth year (Dec 13): about 6%			
Activity 1.3	IDC or other co-investors will leverage all funds made available from the EC by 100%.	EC financing of RCF investment fund €47M leveraged to €94M.	IDC/RCF records	IDC is willing to leverage 100%.	The funds were leveraged at an average of 286%.
Activity 2.1	RCF / IDC will invest in SMEs with high HDP job creation potential, especially for women.	The approximate goals are: First Year: 0 new HDP jobs Second Year: 1879 new HDP jobs Third Year: 1142 new HDP jobs Fourth year: 960 new HDP jobs Fifth year: 1020 new HDP jobs Sixth year: 999 new HDP jobs Women will occupy at least 30% of the jobs as a voluntary target.	Quarterly reporting by Investee measured against their stated goal.		Jobs created: - 2007 – 1797 - 2008 – 931 - 2009 – 932 - 2010 – 472 - 2011 – 863 - 2012 – 1190 - 2013 – (-345) (adjustment due to cancellations) In the above years, women occupied over 30% of the created jobs.
Activity 2.2	Target sectors with high employment / empowerment / environmental	High quality promotional material and promotion campaigns produced and implemented.	Promotional material and campaigns.	IDC will pay for the promotions. It is possible to find enough high quality investments.	The investments are spread across 11 sectors with the exception of three (Tourism, Mining and Mineral Beneficiation as well as

	enhancement impact (tourism, food production and textiles, recycling etc.) through active promotion to obtain a high quality deal flow.				Healthcare)
Activity 2.3	Target geographical areas outside Gauteng and Western Cape through local promotion to obtain a significant deal flow from less favoured provinces.	Promote the RCF outside Gauteng and Western Cape to ensure investment in those areas exceeds 65% either in value or in numbers.		IDC will pay for the promotions. It is possible to find enough high quality investments.	The regional offices do not promote RCF 2 per se but merely promote the funds available to the IDC. The investments outside of Gauteng and the Western Cape are 59% and 45% numbers and value respectively.
Activity 3.1	Pricing of funding instruments including expected long term equity returns to be set cautiously in order to obtain a self-sustainable revolving fund.	The RCFII fund should target IRRs that are market related in order to be able to achieve its portfolio return goal, while at the same time taking into consideration the developmental returns achieved through the investment.	IDC and EIB monitoring of cash flows for the RCF2 portfolio.	The South African economy continues to stay on the positive side.	The facility's IRRs are competitive while serving a developmental purpose.
Activity 3.2	Set-up a system for monitoring of RCF clients. The funding facility will be set-up within the RCF organizational unit. IDC will fund this facility.	The system must be in place no later than 2 months after the start of implementation.	The Financing Agreement and the subsequent statutes of the sub-fund.	IDC is willing to set up and fund the funding facility for RCF to operate.	PIMD has the mandate of monitoring IDC clients on the whole. As a result, there were limited monitoring activities of the RCF 2 investees.
Activity 3.3	IDC will agree monitoring rules	The MOU will be signed within the first three months	The MOU.	A mutual agreement on future division of roles can be reached.	This was done through the EIB IDC Memorandum of Agreement

	with the European Investment Bank (EIB).	of the start of the RCF2.			
Activity 4.1	Funding dependent on investee companies fulfilling the BEE requirement for 25% HDP ownership.	No SME should be funded unless they fulfil the requirement for 25% black ownership or alternatively follow a plan to fulfil such condition within one year from the investment date.	Company shareholder registry.	It is possible for RCF / IDC to avoid **counterfeit** deals	Not all the investees have been followed up to ensure the fulfilment of the 25% black ownership stipulation. Twenty two out of the sixty three approved investments are 100% HDP owned with fifteen being more than 50% HDP owned. The expected average HDP holding for the portfolio is 57% with minimum HDP shareholding of 25%. Special follow up of investees with important Workers' Trust shareholding should be organised
Activity 4.2	RCF will actively seek to invest in enterprise managed by well-educated HDPs or alternatively educate the HDP managers or make sure good ones are hired.	A precondition for investment would be that management of potential clients is adequately trained or is trainable to a sufficient proficiency within one year using the BSS component.	RCF record of client managers' level of education and experience.	It is possible to find enough HDPs with the right qualifications from the start of an investment.	The recommended compulsory BSS (especially the diagnosis of the SME's and its management) to be enforced before any investment is committed should provide the necessary information and result in a support programme for the investee.
Activity 4.3	Training has been provided to the following relevant persons: - HDP Managers/ Owners; - HDPs with the	Over the life of RCF2 (i.e. up to 31 December 2018) the training needs of relevant persons (as defined) in all funded clients have been identified, courses	Training certificates awarded	The relevant persons are willing and available to be trained.	These socio-cultural data could also be collected and checked in the future by an appointed "mentor" for a 5 year period. If information collected is showing any weakness which might put in difficulty the investee,

	potential to become managers; - HDP Executive and Non-Executive Directors - HDP Trustees; and - HDP persons identified below Managerial level who are employed in technical areas which are of strategic value to the organisation. - HDP women managers' training has been emphasized.	designed to meet those needs and training has been provided if and requested by the client. In excess of 30% of the number of HDP persons trained will be female HDP managers.			the mentor attached to the investee should recommend the provision of the necessary BSS.
Activity 5.1	RCF-SBU will set up a voucher/loan system for SME clients to buy management training organizations.	Voucher accounting must be reconciled with the evidence of participation in training courses by company. The loans for vouchers should be 5-10 years, no-interest or low interest instruments.	Voucher accounting system.	The voucher system would be controllable and acceptable to investees.	During the MTR it was suggested that the programme should not follow any systematic training but should rather consider internships with other companies. IDC has not closely followed this recommendation.
Activity 5.2	RCF-SBU will make an agreement with BSS providers for them to supply accredited private consultants for	The agreement should be signed before the launch of the RCF2 fund.	The agreement.	Availability of good quality private consultants and willingness by IDC to pay the going market rate for consultants.	This has been done by the BSS team and about 170 consultants have been selected through a tender.

	monitoring of RCF clients.				
Activity 5.3	The BSS provider will assist with identification of training needs and recommendation of training institutions.	As a pre-condition for investment, a training needs' analysis must be carried out and a report written specifying who needs what training and a general indication are given as to when this training will take place. This will form part of the allocation request.	Training needs analysis reports.	Availability of good quality private consultants and willingness by IDC to pay the going market rate for consultants.	IDC now conducts an ex-ante training needs analysis on all its project applications.
Activity 5.4	RCF SBU will ensure adequate monitoring of investee companies.	Each client is visited and monitored annually (instead of every half year). The output will be a monitoring report covering the performance in all relevant areas.	Annual Monitoring reports.	Availability of good quality private consultants and willingness by IDC to pay the going market rate for consultants.	As IDC is co-investing its own funds with RCF normally taking a smaller part, clients are managed by PIMD post investment. Due to the workload of this Department they do not visit all the RCF clients annually and therefore there is no sufficient monitoring of the investee companies as long as they are repaying their obligations. This is an issue that must be urgently addressed so that lessons are continuously being learnt throughout the life cycle of the investments.
Activity 6.1	Promote the funding for investment support in other African countries so as to get the best quality clients for this test phase.	High quality promotional material and promotion campaigns produced and implemented. Up to fifteen investments in other African countries, in support of South African SMEs.	Promotional material and evidence of promotion campaigns.	Deal flow of high quality investments can be found.	This activity was completely abandoned.

Activity 6.2	BSS providers will assist the Investees in other African countries with TA and training.	Assistance rate would be dependent on client need.		Private consultants can be identified who have the capacity and capability to operate in other African countries.	This is no longer required.
Activity 7.1	Ensure that Investee businesses produce and follow plans for HIV/AIDS prevention	The existence of plans and implementation of the plans. The staffs' knowledge and use of HIV/AIDS prevention measures.	Annual (instead of EIB) Monitoring Reports testing the staffs' knowledge about and actual prevention of HIV/AIDS.	Availability of good quality private consultants and willingness by IDC to pay the going market rate for consultants.	Investees do not usually have plans on HIV/AIDS prevention but instead have been conducting awareness activities. This activity has not been followed up, apart from the 2011 survey.
Activity 7.2	Ensure that Investees follow the laws for environmental protection and that there are plans for rectifying problems.	The existence of environmental protection plans. Staff knowledge about the environmental protection plans.	Annual (instead of EIB) Monitoring Reports testing the staffs' knowledge about and actual prevention of HIV/AIDS.	Availability of good quality private consultants and willingness by IDC to pay the going market rate for consultants.	Investees visited were not following or even aware of environmental laws unless their projects were directly related to environmental protection. It is not clear why this was included as an important activity for SMEs.

7.9 Annexe: Final evaluation terms of reference

LOT N° 10: Trade, Standards and Private Sector

REQUEST N° AFS / 2013 2009 ***/ 323-036***

Specific Terms of Reference for the Final Evaluation of the Private Sector Support Programme titled, 'Support to the Risk Capital Facility 2', Republic of South Africa – Agreement SA/21.031700-05-01

1. Background

The European Commission ("the EC") and the Government of South Africa ("the Government") entered into a Financing Agreement (SA/21.031700-05-01) on 28 February 2006 ("the Financing Agreement") in terms of which the EC made a grant of an amount of Euros ("EUR) 50,000,000.00 to the Government, for support to the Risk Capital Facility (RCF) set up by the Government and managed by the Industrial Development Corporation of South Africa ("the IDC"). The programme is formally entitled the 'Private Sector Support Programme – Risk Capital Facility 2' ("RCF2", "the Programme") and it is the second phase of the Risk Capital Facility 1 (RCF1), which commenced in 2002 and was closed in 2005.

The grant is comprised, in the first part, of a grant of EUR 47,230,000[38] in the form of Sector Budget Support, which was to be utilised for investments in small and medium enterprises ("SMEs") owned by entrepreneurs with a historically disadvantaged background (such first part being "the Fund").

A second part is a grant of EUR 2,770,000 to be utilised for implementation and policy support in the form of technical assistance and evaluations. A third part of EUR 5,000,000 is incorporated in the Programme for the provision of Business Support Services (BSS) to SMEs. This third part is made available by the IDC from its own resources.

RCF2 was set up as a revolving investment Fund which may be invested through a wide range of instruments, including equity and quasi-equity. The Financing Agreement foresaw three possible funding channels through which investments could be made:

- Direct channel: investment through the IDC's own direct project investment routes (direct investments);
- Niche Fund channel: by investment in niche investment vehicles or funds (niche investments);
- Third Party channel: by co-investment with other financial institutions (third party investments).

In terms of the Financing Agreement, the Government, acting through the Department of Trade and Industry (which is the responsible department of the Government) ("the dti") mandated the IDC to manage the Fund on behalf of the Government. Under the Financing Agreement, the EC appointed the European Investment Bank ("the EIB") to provide the EC, the Government and the IDC with independent advisory services with regard to investment decisions and portfolio management of the Fund, and furthermore to oversee, review and

[38] The initial amount allocated to budget support in the original Financing Agreement was EUR 46,300,000, but subject to some reallocations through Riders 1 and 2 to the Financing Agreement, the budget support component increased to EUR 47,230,000.

monitor the management of the Fund. The EIB was appointed to play this role during the implementation period of the Programme. A Programme Steering Committee (PSC), comprising representatives of key institutions, is in place and provides strategic direction to the Programme. The PSC meets on a quarterly basis.

The **overall objective** of the programme is to contribute to economic growth in South Africa and to promote the participation of HDPs in its economy.

More specifically, the **programme purpose** aims at job-creation, through the provision of financial assistance in the form of equity and quasi-equity to SMEs. SMEs are supported with grants and/or low or interest-free loans to enable them acquire Business Support Services (BSS) such as technical assistance and training.

The programme was designed to support the dti in developing and strengthening its policies for empowerment of HDPs. In order to achieve its purpose, **seven (7) key result areas** were identified in the design of the programme (as detailed in the Financing Agreement and its Riders 1 and 2):

1. **Result 1:** SMEs access to development funding increased, resulting in 70 enterprises having been funded through the programme during the six years of operational implementation period.
2. **Result 2:** Increased numbers of new jobs created for HDPs in particular for women, resulting in some six thousand new jobs.
3. **Result 3:** A revolving self-sustainable RCF2 has been established, which is on target to achieve the financial goals established by the dti and to meet the agreed expectations of other investors.
4. **Result 4:** Increased HDP empowerment through shareholding and possibilities for HDPs to hold managerial positions. As a result of RCF investment in a company, it will achieve 25% HDP ownership within one year from investment.
5. **Result 5:** Access to and use of BSS has been improved through effective assistance to SMEs. As a result the Investees have received adequate BSS in the form of relevant training, technical assistance and monitoring over the project lifetime.
6. **Result 6:** Increased South African SME investments in other African countries, targeting 500 jobs, either for HDPs in South Africa or residents in those countries.
7. **Result 7:** Environmental enhancement activities will be actively encouraged. The health and environmental aspects of investee businesses have been strengthened. As a result every investee business has HIV/AIDS and environmental protection plans. The progress against plans will be monitored and measured yearly.

The RCF2 is being executed over eight years, which officially commenced on 28 February 2006 at the entry into of the Financing Agreement *(following signature by the South African government)* and ends on 31 December 2013. The execution period comprises two phases: (i) an operational implementation phase, which commenced on the entry into force of the Financing Agreement and ended on 31 December 2011; and (ii) a closure phase, which commenced on 1 January 2012 and expires on 31 December 2013.

Two riders (amendments) to the Financing Agreement were introduced during the implementation of the programme. Rider 1 was introduced in February 2008 and its main objective was to extend the operational implementation period by one year until 31 December 2009 and the closure period up to 31st December 2011. It also introduced other minor

modifications to the programme including a reallocation of the budget, changes to Result 6, and also changes to the audit provision.
Rider 2 was introduced in December 2009. Its main objective was to extend the operational implementation period by two years until 31 December 2011 and the closure period up to 31 December 2013, as is currently the case. It also made minor changes to the technical and administrative provisions (TAPs) including a minor reallocation of the budget and minor changes to results 1, 5 and 7.

The Sector Budget Component (EUR 47,230,000) of the programme has been fully disbursed through three tranches based on fulfilment of conditions as stipulated in the Financing Agreement. The first tranche of EUR 20,000,000.00 was disbursed in December 2006, a second tranche of EUR 13,500,000 in December 2008, and the final tranche of EUR 13,730,000 in December 2010 and February 2011 *(the payment was made in two parts).* It should be noted that the actual operational implementation of the programme started in early 2007 after receipt of the first tranche payment of EUR 20,000,000.00 in December 2006.

The programme has been **monitored twice** (in 2007 and 2010) as part of EC Result Oriented Monitoring (ROM) exercise. A **mid-term review** was also conducted in 2009 and provided a positive assessment of the programme and made some recommendations for the remaining implementation period, which have been taken into account by the programme management. The programme is also being evaluated as part of an important on going exercise of the **EC's evaluation of budget support in South Africa** which commenced in 2012 and will end in 2013. This evaluation is assessing the EC's overall portfolio of budget support in South Africa and it comprises three in-depth sector case studies, including private sector (RCF). The main objective of the evaluation is “to assess to what extent Budget Support in South Africa contributed to achieve sustainable results on employment creation and poverty reduction with particular regard to inclusive and sustainable growth and the provision of social services. Indicators of success include the extent to which the support enabled the SA Government to implement its sector strategies and to enhance the efficiency and effectiveness of its policies, strategies and spending actions."

2. Description of the assignment

2.1 Global Objective

The overall objective of the final evaluation of the RCF2 Programme is to provide decision-makers in the South African Government and the EC with a detailed assessment of the performance of the programme to date in terms of its relevance, efficiency and effectiveness, and with special attention to its impacts and prospects for sustainability.

The expected results and indicators defined in the Financing Agreement (and its Riders 1 and 2) should form the basis of measurement. However, important developments that have taken place during implementation will need to be taken into account. This will include the findings and recommendations of the mid-term review.

2.2 Specific Objective

The specific objectives of the final evaluation are:

- Based on the design and evolution of the programme, to assess the relevance, efficiency, effectiveness and impact of programme implementation;
- To assess the sustainability of the programme;

- Provide clear key recommendations on potential future activities in the Private Sector in South Africa, especially in terms of improving access to finance for small, micro and medium enterprises (SMMEs), where there are market constraints and for which development funding could add value.

2.3 Guiding documentation

The experts will be expected to examine in detail and report upon the progress and performance of the programme implementation. This assessment should be made taking into account the following key documents:

- The Financing Agreement including its Riders 1 and 2,
- The Memorandum of understanding between the IDC and the dti,
- The Agreement between the EIB and the IDC,
- The Memorandum of Understanding between the EC and the EIB,
- Key Performance Indicators contained in the above documents,
- RCF Annual Business Plans prepared by the IDC,
- Quarterly and annual progress reports of the RCF prepared by the IDC (from 2007 to date),
- EIB and IDC presentations at PSC meetings,
- Annual Performance Reviews by the EIB (for years 2007 to 2011)
- RCF audit reports (prepared by IDC independent auditors)
- Independent EC ROM reports for 2007 and 2010,
- The dti's Medium Term Expenditure Framework and its relevant parts of the Vote pertaining to SME support.

The experts should also review other relevant documentation such as relevant legislation, the IDC Strategy, relevant dti strategies and policy documents, Agenda / Minutes of PSC Meetings, investment and business support proposals and the draft reports of the EC Evaluation of Budget Support in South Africa.

2.4 Requested services

The services should be rendered in accordance with internationally accepted practices on evaluations including the OECD DAC evaluation methodology. The services to be provided include:

1) An assessment of the extent to which the programme remained consistent with, and supportive of the strategic priorities and policies of South Africa;
2) A thorough assessment of key stakeholder participation in the management and implementation of the programme, and the level of ownership at institutional level. This should include an assessment of EIB's contribution in its role of technical assistance to RCF2;
3) A critical assessment of the efficiency of the programme (in terms of input delivery, cost control and activity management, programme management and overall coordination arrangements) and effectiveness (actual and potential delivery of outputs and progress towards achieving the purpose). In terms of effectiveness, performance should be measured against performance targets detailed in the Financing Agreement and changes as adopted following the mid-term review. The evaluation should however also identify shortcomings, if any, on the selected performance targets of the Financing Agreement and if possible provide recommendations on how a future RCF programme could be measured;

4) An assessment of the effectiveness and success in aligning the outcomes and activities of the programme with other EU-, government- and donor funded programmes;
5) An assessment of the prospects for sustainability of the Programme including the systems and institutional capabilities developed during the Programme;
6) Provide clear recommendations on potential future activities in the Private Sector in South Africa, especially in terms of improving access to finance for small, micro and medium enterprises (SMMEs), where there are market constraints and for which development funding could add value.

In assessing the issues of relevance, efficiency, effectiveness, impact and sustainability, the final evaluation shall specifically:

(i) Assess the general management of the Fund by the IDC;
(ii) Assess the communication between the EIB and the IDC;
(iii) Identify any obstacles to the implementation of the Fund;
(iv) Measure the performance of the Fund and the management by the IDC of the Fund against the key indicators and performance targets detailed in the Logical Framework of the Financing Agreement and further stipulated in Article 5.01 and Annex C of the EIB/IDC Agreement, namely:
    a) Number and investment value of small and medium enterprises (SMEs) financed (for specified investments approved, committed and disbursed) through each of the various channels, their status against the SME parameters defined in Annex A of the same Agreement, and their location within South Africa and elsewhere in Africa;
    b) Amount of the Fund that has been approved by the IDC in respect of the specified Investments and Grants;
    c) Number of new jobs created by investments, and in particular the number of these jobs held by women;
    d) Number of new managers who are historically disadvantaged persons, and in particular the number of female HDP managers;
    e) Number of SME's owned by HDPs and the level of ownership (current and planned within 12 months);
    f) Number of HDP employees (and specifically HDP women) trained through business support services;
    g) Number of days of training received per person (and especially women), for specified investments;
    h) Existence of HIV/AIDS prevention and environmental protection plans of investees and progress against such plans;
    i) Progress with regard to the achievement of the programme's financial goals which include the establishment of a revolving self-sustainable RCF2;
    j) Deal flow (number, potential value and channel type of realistic investment opportunities) examined;
    k) All reflows, including but not limited to capital, dividends, coupon and interest payments, in respect of the investments;
    l) IDC's promotional activities for the RCF (marketing materials, campaigns).

(v) Detail number of investments that were proposed but which were not approved, not undertaken or which failed and analyse the underlying causes.

(vi) Other specific items to be reviewed in detail are:

a) Third Party Investment Channel (TPC): evaluate the evolution of the TPC following the recommendations made in the mid-term review[39];
b) Africa Investments: evaluate the relevance, effectiveness and efficiency of the "Africa Investment" channel for RCF2, including the efforts undertaken by IDC thus far; identify key obstacles and provide recommendations on how a such a regional component could be better taken into account in a future programme;
c) Business Support Services: evaluate the relevance, effectiveness and efficiency of Business Support Services to SMEs, including the efforts undertaken by IDC thus far, and progress made since the mid-term review.
d) Additionality: evaluate the extent to which RCF2 funding can be considered additional, i.e. catalytic in enabling investments that would otherwise not be "bankable" according to the criteria of the IDC and/or commercial lenders.
e) Evaluate the degree of adherence to the Investment Guidelines on the one hand, and the relevance, effectiveness and efficiency of the Investment Guidelines themselves in achieving programme objectives on the other hand.
f) Evaluate the Key Performance indicators applied to the Programme, identify shortcomings, if any, and provide detailed recommendations, if necessary,

(vii) RCF1: evaluate the relevance of lessons learned from RCF1 as stated in the Financing Agreement and assess the degree to which they are effectively applied and/or applicable to RCF2. Furthermore, review the status of the current portfolio of RCF1 and identify further lessons applicable to RCF2.

The services will include site visits to a representative sample of SMEs and niche funds, key institutional stakeholders involved in the implementation programme, development partners and others as appropriate.

2.4 Required Outputs

The following outputs are required:

- Inception Report, detailing the organisation and methodology to be adopted for the assignment;
- Debriefing Report, indicating the critical findings and recommendations. This report could take on the form of a PowerPoint presentation;
- Draft Final Report, documenting all aspects of the review; and
- Final Report, incorporating comments on Draft Final Report.

3. Experts profile

The evaluation team will be composed of two (2) experts with the following profiles and qualifications:

- **Expert 1 (Team Leader – Senior expert):** this expert will have an education equivalent to a Master's Degree in Finance (Development Finance and Corporate), Business Administration or other appropriate qualification, with 10 years general experience relevant to the assignment. He/she must be an excellent communicator in spoken and written English and should demonstrate extensive experience in leading and coordinating working teams together with the ability to co-ordinate joint research/evaluation processes and produce a consolidated report.

[39] It should be noted that the TPC was found not to be feasible during implementation, and recommendations were made during the mid-term review on how to restructure this channel.

- **Expert 2 (Senior expert)**: this expert will have an education equivalent to a Master's Degree, with 10 years general experience relevant to the assignment. In addition, the expert will have extensive experience in SME development preferably in emerging markets, with exposure to the financing, auditing and diffusion to SMEs, SME capacity building, as well as understanding of benefit flows to clients and impact thereof.

Collectively, the team of experts should demonstrate the following:

- Extensive knowledge and experience of EC programme implementation by means of the Sector Budget Support delivery modality;
- Sound knowledge and experience of conducting reviews and evaluations of donor-funded projects *(the Team Leader should have participated in at least two reviews and/or evaluations and have led at least a third in the past five years, and Expert 2 should have participated in at least one review or evaluation in the past three years)*;
- Thorough understanding of Private Sector Development Programmes;
- Significant Expertise in Development Finance;
- Project cycle management processes;
- Sound understanding of the South African policy context in so far as it relates to Broad-Based Black Economic Empowerment (BBBEE) will be an advantage.

The **working language** for the assignment is **English**. Both experts should be fluent in spoken and written English, and should have excellent writing skills.
The Framework Contractor must ensure that the experts have adequate administrative support, so that their time and expertise can be used optimally for achieving the objectives of the assignment.

4. Location and duration

4.1 Starting and finishing date of the assignment

The assignment has to be executed during a period of ten (10) weeks, indicatively starting on 16 September 2013, with the mobilisation and briefing meeting, and ending on 30 November 2013, with the submission of the Final Report.
The mobilisation and briefing meeting with the EU Delegation will be held in Pretoria on 16 September 2013 from 1000hrs. This will be confirmed once the contract has been awarded.

4.2 Schedule and number of days for the assignment per expert

A total of 57 working days have been provided for each of the experts (a total of 79 calendar days and 114 person days in total). NB: the working days include a provision of 4 travel days per expert (for the international days of travel).

The experts will be expected to interview all key stakeholders and to make site visits to a representative sample of Investees (SMEs and niche funds) located in various provinces in the country. The site visits will require air and/or road travel. The experts will exercise the right to determine which clients they wish to visit and the names of the selected clients should be indicated in the inception report. This said, the experts must liaise with the IDC regarding client visitations and the list of clients to be visited may have to be revised taking into consideration the availability of these clients and/or other constraints.

It is also a requirement of this assignment that the experts should meet with the EIB officials in Luxembourg, for one day, to take into consideration the EIB's views on the programme's performance and to develop a detailed understanding of the role and contribution of the EIB in the programme, including but not limited to the EIB's role in (a) providing macro-monitoring of the portfolio, and (b) evaluating and approving individual investments. This visit should be undertaken after completion of the interviews with the Investees and other stakeholders. The visit will necessitate one international return flight (South Africa – Luxembourg – South Africa) for each of the experts.

It is a further requirement of the assignment that the experts should do a debriefing presentation on the critical findings and recommendations to the key stakeholders of the programme (the dti, IDC, National Treasury, EU and other PSC members) possibly on the occasion a PSC meeting. According to the current planning for PSC meetings, the third quarter PSC meeting will take place on 13 November 2013 and this meeting could be extended to incorporate the above-mentioned presentation. The draft final report will need to be submitted with stakeholders sufficiently in advance of this meeting.

The table below presents an indicative scheduling of the assignment, which could be revised as deemed appropriate by the experts and with the agreement of the IDC and the EU Delegation:-

	Phase of Activity	**Indicative Dates**
1.	Mobilisation and Briefing Meeting, EU Delegation offices	16 September
2.	Data Review in Pretoria	17 to 20 September
3.	Submission of Inception Report	23 September
4.	Interviews with IDC, the dti and other Gauteng-based stakeholders	24 September to 30 October
5.	Interviews with Investees and other Stakeholders	
6.	Visit to EIB (Luxembourg offices)	1 November
7.	Debriefing to the EU, IDC and dti of critical findings and corresponding recommendations	4 November
8.	Production and submission of Draft Final Report	5 to 8 November
9.	Presentation at Project Steering Committee (at IDC offices) of key findings and recommendations	13 November
10.	Submission of comments on the Draft Final Report by the EU, the dti, the IDC	By 25 November
11.	Production and Submission of Final Report, for approval by the EU and the dti	25 to 30 November

Both experts will be expected to work full-time in-country from 16 September to 13 November, but they may work from their home base after the debriefing workshop if preferred.

For the purpose of this contract, experts have the permission to work during weekends and public holidays, as required for delivering the requested services.

4.3 Location of the assignment

The assignment will be executed mainly in the Gauteng Province, South Africa, where the following are located:

- EC Delegation to South Africa – in Pretoria;
- The Department of Trade and Industry (the dti) – in Pretoria;
- The Industrial Development Corporation (the IDC) – in Johannesburg.

In addition, visits to the afore-mentioned Investee clients (in various Provinces) and to the EIB (Luxembourg) will also take place.

4.4 Budget

The maximum budget available for this assignment is **€ 152,902.00.** The contractor will cover the travel costs and subsistence allowance of the consultants from the overall budget value. The budget should make provision for:

- Professional fees;
- International travel depending on the home base of the experts proposed; NB:- provision should be made for two international return flights per expert due to the additional trip to EIB offices in Luxembourg:
- Per diems;
- Local travel (including inter-city travel); NB – a maximum of 6 inter-city flights for both experts (3 trips per expert);
- Printing costs for the presentations that will be made at the debriefing workshop and any other meeting.

5. Reporting

All reports as indicated in Section 2.4 of this ToR should be presented in an agreed format. The Inception Report should be between 5 and 10 pages, excluding annexes. The Draft Final and Final Reports should be a maximum of 50 pages, excluding annexes. All reports should be drafted in English, and prepared with MS Office software. Each report should be presented to the parties involved.

The indicative time schedule for the delivery of and comment on the outputs indicated in Section 2.4 is as follows:

Report	**Delivery & presentation date**	**Date for comments**
Inception Report	23 September 2013	27 September 2013
Draft Final Report	8 November 2013	25 November 2013
Final Report	30 November 2013	15 December 2013°

º If the Final Report is acceptable, this will be the date of approval.

The following information should be noted on the **final reporting**:

FINAL REPORT	
Title	Support to the Risk Capital Facility Phase 2 (SA/21.031700-05-01) Final Evaluation
Language	English
Recipient	European Union Delegation to South Africa
Responsible	Ms Milly Chesire, Project Officer
Copies to submit	Inception Report: electronic copy Debriefing document/presentation: electronic copy Draft final report: electronic copy Final report: 5 hard copies + 1 electronic copy

The cover page of the final report shall carry the following text:
" This evaluation is supported and guided by the European Commission and presented by (name of consulting firm). The report does not necessarily reflect the view and opinions of the European Commission".

6. Administrative information

6.1 This contract will be a **global price** contract.

6.2 The **contact details** for the relevant institutions are as follows:

EU Delegation:
Ms Milly Chesire
Project Officer
Tel: + 27 12 452 5224
E-mail: **milly.chesire@ec.europa.eu**

The dti:
Mr Sipho Zikode
Deputy Director General, Enterprise Industry Development Division
Tel: +27 12 394 1396
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The dti:
Mr Mojalefa Mohoto
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IDC: Head, Risk Capital Facility
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IDC: Account Manager, Risk Capital Facility
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EIB: Investment Officer
Mr Francois-Xavier Parant
Tel: +352 (43) 79 85 312
Email: f.parant@eib.org

7.10 Annexe: List of persons met

Name	Surname	Institution	Email address	Tel
Meryl	Mamathuba	IDC	merylm@idc.co.za	011 269 3038
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Billy	Cobbinah	IDC	billyc@idc.co.za	011 269 3663
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Thandie	Mashego	IDC	Thandiem@idc.co.za	011 269 3027
Matsobane	Khwinana	IDC	matsobanek@idc.co.za	011 269 3395
Samantha	Mohanlal	IDC	samantham@idc.co.za	011 269 3028
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Enriko	Fourie	IDC: Western Cape	enrikof@idc.co.za	021 421 4794
Lizo	Ntloko	IDC: Western Cape	lizon@idc.co.za	021 421 4794
Pat	Moodley	IDC KZN Regional Office	patm@idc.co.za	027 31 337 4455
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Emmanuel	Ramathuba	National Treasury	Emmanuel.Ramathuba@treasury.gov.za	012 315 5528
Seema	Naran	National Treasury	Seema.Naran@treasury.gov.za	012 315 5528
Mojalefa	Mohoto	The dti	mmohoto@thedti.gov.za	012 394 1619
Mahomed	Vawda	Economic Development Department	MVawda@economic.gov.za	012 394 5606
Milly	Chesire	European Union Delegation	Milly.CHESIRE@eeas.europa.eu	012 452 5242
Bart van	Uythem	European Union Delegation	Bart.Van-Uthem@eeas.europa.eu	0124525242
Richard	Young	European Union Delegation	Richard.Young@eeas.europa.eu	0124525242
Chabir	Hassam	International Finance Corporation	Chassam@ifc.org	0117313071
Busso	Von Alvensleben	KFW	Busso.alvensleben@kfw.de	012 423 6357
Marc	Leistner	EIB	leistner@eib.org	012425 0466
Carmelo	Cocuzza	EIB	cocuzza@eib.org	012425 0460
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Christophe	Blanchot	Proparco	blanchotc@afd.fr	011 540 7100
Brandon	Morgenrood	Standard Bank	brandon.morgenrood@standardbank.co.za	011 721 7027
Sisa	Ntshona	Barclays/ ABSA Bank	Sisa.ntshona@absa.co.za	(0)11 846 4079
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	Manila	Pick and Pay, Kokstad		0820 6304 85
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Ryan	Davies	Amathole Berries	Ryan@amathileberries.co.za	043 782 0610
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Sereshen	Moodley	MX Metal Shop		0114742602
Warren	Bam	Lushof Fruit		0232400925
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Guy	Baxter	Inspired Evolution Investment Management	guy@inspiredevolution.co.za	021 702 1290
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Avril	Stassen	Agri-vie	avrils@agrivie.com	021 913 5662
Hermann	Marais	Agri-vie	hermanm@agrivie.com	021 913 5662
Roberto	Vasconcelos	Primolitos	Roberto@primolitos.com	0861 123 321

7.11 Annexe: List of documents and web sites consulted

7.11.1 List of documents

- Provided by the EU:

- The Financing Agreement including its Riders 1 and 2,
- The Memorandum of understanding between the IDC and the dti,
- The Agreement between the EIB and the IDC,
- The Memorandum of Understanding between the EC and the EIB,
- Key Performance Indicators contained in the above documents,
- RCF Annual Business Plans prepared by the IDC,
- Quarterly and annual progress reports of the RCF prepared by the IDC (from 2007 to date),
- EIB and IDC presentations at PSC meetings,
- Annual Performance Reviews by the EIB (for years 2007 to 2011)
- RCF audit reports (prepared by IDC independent auditors)
- Independent EC ROM reports for 2007 and 2010,
- The dti's Medium Term Expenditure Framework and its relevant parts of the Vote pertaining to SME support.

- Others:

- IDC Annual report: http://www.idc.co.za/images/publications/IDC_ir_2013.pdf
- IDC Development Funds Department documents
- dti Medium term strategic plan 2011 – 2014: http://www.info.gov.za/view/DownloadFileAction?id=144930
- dti Annual report 2011 – 2012: http://www.thedti.gov.za/DownloadFileAction?id=793
- dti Rethinking Small Business Support in South Africa, report on the review of Government support for small business, by Osiba research, 2011
- EDD The new growth path framework: http://www.thedti.gov.za/DownloadFileAction?id=793
- National Treasury Strategic Plan 2013 – 2017: http://www.treasury.gov.za/publications/strategic%20plan/Strat%20Plan%202013-2017.pdf
- IMF Article IV, South Africa 2012: http://www.imf.org/external/pubs/ft/scr/2012/cr12247.pdf
- National Development Plan 2030: http://www.info.gov.za/issues/national-development-plan/
- The Small and Medium Enterprise (SME) Sector — Catalyst for Growth in South Africa by JP Morgan: http://www.jpmorgan.com/cm/BlobServer/JPM_Dalberg_SME-Catalyst-for-Growth.pdf?blobkey=id&blobwhere=1320545178691&blobheader=application%2Fpdf&blobheadername1=Cache-Control&blobheadervalue1=private&blobcol=urldata&blobtable=MungoBlobs

7.11.2 List of web sites

- National Treasury	http://www.treasury.gov.za/divisions/info.aspx#EP
- dti	http://www.thedti.gov.za/sme_development/sme_development.jsp
- IDC	http://idc.co.za/
- EDD	http://www.economic.gov.za/
- NEDLAC	http://www.nedlac.org.za/
- WDB Investment Holdings	http://wdb.co.za/about/
- Banking' association	http://www.banking.org.za/
- SAVCA	http://www.savca.co.za/
- ABSA group	http://www.absa.co.za
- SEFA	http://www.sefa.org.za/
- Business Partners	http://www.businesspartners.co.za/
- NEF	http://www.nefcorp.co.za/
- IFC	http://www.ifc.org
- USAID	http://sa.usaid.gov/south_africa/node/68
- ADB	http://www.afdb.org
- DFID	https://www.gov.uk/government/world/organisations/dfid-south-africa
- AFD/Proparco	http://www.proparco.fr
- EIB	http://www.eib.org

- KFW	https://www.kfw-entwicklungsbank.de
- StatsSA	http://www.statsa.gov.za/publications/populationstats.asp
- City Press	http://www.citypress.co.za/news/study-finds
- Wikipedia	en.wikipedia.org/wiki/Corruption-Perceptions Index
- Financial Mail	http://www.financialmail.co.za/economy/2012/10/04/working-but-still-poor
- IMF	http://www.imf.org/external/pubs/ft/scr/2012/cr12247.pdf
- Finscope Study	www.btrust.org.za/..../o-nsbs-finance-small-business-survey
- PWC	www.pwc.co.za/en/assets/.../pwc-banking-industry-survey-june2009.
- BEE Codes	http://www.southafrica.info/business/trends/empowerment/BEE- codes.htm
- EPWP	http://www.epwp.gov.za/
- The Presidency	http://www.thepresidency.gov.za/dpme/docs/guideline.pdf
- CWP	http://www.tips.org.za/community-work-programme
- Jobs Fund	http://www.jobsfund.org.za/
- ECF	http://www.thedti.gov.za/financial_assistance/financial_incentive.jsp?id=58&subthemeid=8

7.12 Annexe: Characteristics of investees'/rejected applicants visited and/or reviewed.

INVESTEES ASSESSED AND VISITED							
Client's name, region, status	Business sector, start up or new development	IDC/other commitments & RCF Amounts committed	Type of RCF financial instrument & Pricing	Purpose of financing	Duration, grace and repayment period for IDC and RCF	Training/ BSS received Impact	B-BBEE commitments/shareholding B-BBEE effective impact at visit date compared to initial plan
Gauteng province							
Primolitos Limited (PRIMOPCO) On track	Established business in food manufacturing sector	IDC: ZAR 35 million MT ZAR 3.9 million WC Secured by 2nd mortgages on Pties RCF ZAR 11.2 million Pref shares to Workers trust to control 32% holding company (off properties)	Preference shares, price at 5% pa gross plus upside provided by value of shares, estimated at gross 5% pa	Funding plant expansion while RCF would fund Workers trust 32% shareholding	Not described in credit application	115 new employees planned, significantly females at cost of about ZAR 100,000	Workers trust funding means BEE finance, increasing BEE shareholding.
Pharox Lumens Africa (Pty) Ltd On track	Green energy, reducing electricity consumption related to public lighting	IDC: ZAR 21 million MT + 6 months capitalised interest – repayment over 2.5 years RCF: 7 million MT loan + 6 months capitalised interest – repayment over 2.5 years	Prime less 2% for IDC loan 5% interest + 1.63% of turnover ~ 10% pa, not capped	Replacing traditional electric bulbs with low energy consumption one for ESKOM	See column 1 RCF loan has the same terms and conditions as IDC. Personal guarantee from the shareholders	BSS has been planned for ZAR 454,000 + 345 280 BSS loan	BEE controlled business 40 seasonal jobs over 3 years 70 temporary jobs over 6 months
Power 98.9 FM (Pty) Ltd On track	Start-up radio station	IDC: 13, 500, 000 IDC Capitalised Interest: 1, 350, 000 RCF: 20, 000, 000	Subordinated Loan Min 5% RBTIRR plus upside based on 10% PAT, targeting RBTIRR of 10%	IDC: Build station studios, acquisition of studio equipment and other assets RCF: Fund operational expenses	IDC: 6 years from drawing date. 20 equal monthly instalments of R137, 000, there after 29 equal monthly instalments of R385, 000 and R935, 000 prorated to begin 18 months after 1st drawdown.	None (Turned Down)	Not informed

					RCF: 10 years duration 70% of free cash flow paid pro rata semi-annually on 31 August and 28 February. Any shortfall or over payment is taken into account in the subsequent payment		
MX Metal Shoppe CC (Gridfast cc) On track	Emerging engineering and structural steel fabrication shop for construction	IDC: 10, 200, 000 (Portion A – 8, 200, 000) (Portion B - 2, 000, 000) RCF: 3, 000, 000	Subordinated Loan Min 3% RBTIRR plus a bullet payment in 2017 to achieve 7% RBTIRR	IDC: Plant & Equipment and Working Capital RCF: Working Capital	IDC Portion A: 72 months (including 12 months moratorium) 59 monthly instalments of R136,670 a final R136, 470 commencing 12 months after first draw IDC Portion B: 60 months (including 12 months moratorium) 47 monthly instalments of R41, 670 and a final R41,510 commencing 12 months after first draw RCF: 60 months commencing immediately Bullet payment (s) on the 5th anniversary from first drawdown date to achieve a minimum RBTIRR of 5% plus an upside participation equivalent to 10% of grid fast	None	Not informed
Name Plate Centre Signs (Pty) Ltd On track	Commercial and industrial signage manufacturing	IDC: ZAR 3.1 MT 3 years ZAR 1 WC RCF: ZAR 3.25 5 years MT	IDC : 6% fixed, then Prime - 0.7% RCF : 5% BTIRR + 1.8% turnover if profitable not capped	IDC	IDC: 2 years after 1 year grace RCF: Bullet repayment	Grant 159,600 + 184 600 grant loan	BEE shareholding reached 33% HDP employment confirmed

Client's name, region, status	Business sector, start up or new development	IDC/other commitments & RCF Amounts committed	Type of RCF financial instrument & Pricing	Purpose of financing	Duration, grace and repayment period for IDC and RCF	Training/ BSS received Impact	B-BBEE commitments/shareholding B-BBEE effective impact at visit date compared to initial plan
Western Cape province							
Lushof Fruit (Pty) Ltd On track	Expansion of the blueberry farm	IDC: 45, 500, 000 IDC Capitalised Interest: 4, 300, 000	Subordinated Loan RCF: Min 5% RBTIRR plus upside of 1% based on turnover targeting 8%	IDC: Plant & Equipment and Working Capital RCF: Working Capital	IDC: 10 years (5 year capital moratorium plus 3 year capitalised interest) Principle: 5 equal annual repayments of R9, 100, 000 starting 5 years from first drawdown Capitalised interest: 5 equal annual repayments of R860, 000 starting 5 years from first drawdown. RCF: 9 years No fixed terms of repayment	Due to receive BSS Support in 2014. Delays due to clashes with planting and harvesting season.	Not informed
Micawber 803 (Pty) Ltd t/a Noodle Factory Under supervision	Start-up, Agro industries	IDC: 3, 146, 489 RCF: 1, 586, 297	Subordinated Loan Minimum Real before tax IRR of 5% plus upside from year 5 at 2.145% of turnover to achieve an uncapped RBTIRR of 10%.	Capital Expenditure and Working Capital	Redemption date: 04 March 2018	None	Not informed
Eastern Cape province							
SPLJ - Amathola Berries Pty (Ltd) Work out and restructuring dept.	Plantation of blue berries: IDC 40% equity ECDC: 10% SPLJ: 40% Yummy berries:	IDC Shareholders loan: ZAR 18 million + 17 million 8 year new loan IDC Pref shares: ZAR 14 million RCF ZAR 18 million	3 year grace Loan priced at After tax of 6.7% Share hurdle rate expected: ATIRR 8%	Financing the planting and equipment of the farm plus working capital	Despite three year grace period, the enterprise is facing difficulties at only 50% maximum of expected income. Work out and restructuring has taken control.	BSS	230 staff, minus 60 due to difficulties with potential up to 816 permanent staff

	10%						
Client's name, region, status	Business sector, start up or new development	IDC/other commitments & RCF Amounts committed	Type of RCF financial instrument & Pricing	Purpose of financing	Duration, grace and repayment period for IDC and RCF	Training/ BSS received Impact	B-BBEE commitments/ shareholding B-BBEE effective impact at visit date compared to initial plan
Pick and Pay (Shelfzone 109) On track	Retail franchise	IDC: ZAR 9.7 + 11.3 + 39 + 105 million w 1 year grace RCF: ZAR 1.3 + 0.6 + 19.5 + 15 million IDC Gtee: ZAR 1.2 + 2.4 + 6 + 9 million	Pricing and loan duration not mentioned in documents supplied	Financing franchises store opening, with very high gear (9% equity only at beginning)	Pricing and repayment period are not mentioned in the documents entrusted to the mission	???	About 160 HDP employed for the Shelfzone store, mostly female at ZAR 150,000 per job BEE 51% controlled and managed
Aristopix (Pty) Ltd On track	New development in vehicle fleet provision & maintenance	IDC/UIF: ZAR 12.4 million 5 year + 2.5 million VAT loan 0.1 year + 1 million 5 year RCF: ZAR 5.5 million subordinated loan, 5 year NEF: ZAR 21.6 million	UIF: Fixed 6.6% until 2015 then prime – 0.7% RCF gross 5% + upside 1.5% of turnover, not capped NEF: prime	Financing new 66 vehicles + managing 48 existing for KSDM Municipality Secured on vehicles for RCF as well???	Job creation should reach 90, including 80 at KSDM Gearing very high at 12% equity at beginning	BSS needs assessment conducted: 0.4 million grant and 0.256 RCF loan no interest	100% BEE shareholding and management Cost per job for RCF is only 50.000.
Limpopo							
Astradeals 220 CC Legal action	Oxygen production start-up	IDC: 1, 000, 000 RCF: 2, 000, 000	Subordinated Loan 5% RBTIRR plus upside of 1% based on turnover targeting 10%	IDC: 6 years (5 years + 1 year capital moratorium) 59 equal monthly instalments of R16, 700 and a final payment of R14, 700 RCF: 6 years (3 years + 3 year capital moratorium) 35 equal monthly instalments of R55, 500 and a final payment of R57, 500	Purchase of Plant and Equipment (Oxygen cylinders and delivery vehicles) – Both RCF and IDC	R125, 000 funded on a 50-50 basis between IDC and Astradeals.	51% BEE shareholding. Plant not yet operational. Due to start in November 2013.

Client's name, region, status	Business sector, start up or new development	IDC/other commitments & RCF Amounts committed	Type of RCF financial instrument & Pricing	Purpose of financing	Duration, grace and repayment period for IDC and RCF	Training/ BSS received Impact	B-BBEE commitments /shareholding B-BBEE effective impact at visit date compared to initial plan
KwaZulu Natal							
Cyclocor (KZN) 2 On track	Start-up manufacturing polymer-bonded fire-resistant 'green' roof tiles	UIF fund ZAR 8 million RCF ZAR 4.6 million subordinated term loan NEF ZAR 7.1 million WC + 0.7 million senior TL + 3.2 million BEE (Batuka) shareholder finance + 1.1 million stand by	UIF and NEF pari passu and similar pricing: 6% gross then prime -0.7% RCF: 5% gross IRR + bullet to achieve gross 8% IRR, if profitable after payment upside.	Financing equipment, working capital, replacing one commercial lender and providing share capital on behalf of BEE.	NEF and UIF Term senior debt: 6 years - 1 year grace RCF: 7 years – 1 year grace Effective equity will represent 29% and increase after 2015 Security on equipment, and other assets and shares		107 BEE job at ZAR 179,000 cost 49% BEE ownership Green production

REJECTED APPLICANTS, ASSESSED							
Client's name	Business sector, start up or new development	IDC commitments & RCF Amounts required	Type of RCF financial instrument required	Duration, grace and repayment period for IDC and RCF	Purpose of financing	B-BBEE status B-BBEE impact	Reason for refusal
Agro Tractor House	Client information no longer available.	Client information no longer available.	Client information no longer available.	Client information no longer available.	Client information no longer available.	Client information no longer available.	Client information no longer available.
Amadwala Trading 851CC,	Client information no longer available.	Client information no longer available.	Client information no longer available.	Client information no longer available.	Client information no longer available.	Client information no longer available.	Client information no longer available.
MAZWE	MFI	IDC: ZAR 15 million RCF: ZAR 10 million	MT wholesale loan Equity	N/A	Strengthening the MFI financial structure to fund expansion	100% BEE status	No direct job creation while MFI lending targeted both consumer and development purpose
Client's name,	Business	IDC commitments & RCF	Type of RCF	Duration, grace and	Purpose of financing	B-BBEE status	Reason for refusal

	sector, start up or new development	Amounts required	financial instrument required	repayment period for IDC and RCF		B-BBEE impact	
AGNI/AFRO Asia	Processing scrap metal	IDC: MT loans + 12 month guarantee to commercial bank Working capital facility + 10% of the equity; Rest of equity: Workers trust: 10%; BEE partners 40%; Indian foreign partner: 40%	RCF was to bring equity ; finally, foreign partner with process know how was required and replaced RCF	NA	Purpose was to fund processing of scrap metal Good point about the project was: - Small workers trust shareholding - Know how supplied by foreign partner - Gtee ifo commercial bank to induce it to support project after 12 months trial period - Real involvement of BEE shareholders cum managers - BSS to support BEE managers in their relationship with powerful foreign partner	50% BEE shareholding 100% BEE employment + significant scrap metal suppliers + production value adding + FDI	Equity was finally provided by foreign partner bringing in process know how as well as equity on a 50/50 basis

NICHE FUNDS INVESTMENTS							
	Amount invested % total fund	**Expected after tax IRR**	**Investment period**	**Disinvestment period**	**Estimated net IRR at end June 2013**	**HDP S/holding**	**HDP employed**
AGRI-VIE Fund	45, 000, 000	Min nominal IRR of 18%	10 years				
Agri-vie client's name, region, status	**Business sector, start up or new development**	**IDC commitments & RCF Amounts committed**	**Type of RCF financial instrument**	**Pricing**	**Duration, grace and repayment period for IDC and RCF**	**Purpose of financing**	**B-BBEE status** **B-BBEE impact**
AfricaJUICE, Ethiopia, on track	Agro Industries	RCF: 1, 234, 680		IRR hurdle of 31%		Early stage	HDP New jobs: 1 250
New Forest Company, Uganda, on track	Forestry and Wood Products	RCF: 3, 369, 218		IRR hurdle of 25%		Replacement and expansion capital	HDP New jobs: 794

Asilia, Tanzania, on track	Eco-Tourism	RCF: 2, 023, 087		IRR hurdle of 30%		Replacement and expansion capital	HDP New jobs: 160
Dew Crisp, Gauteng, on track	Agro Industries	RCF: 3, 285, 474		IRR hurdle of 25%		Replacement and expansion capital	None
Hygrotech, Gauteng, on track	Agro Industries	RCF: 2, 325, 748		IRR hurdle of 27.5%		Replacement and expansion capital	HDP Shareholding: 0.01% HDP SH: 4 Female HDP SH: 1% HDP Managers: 3 HDP New jobs: 153 New Female HDP Jobs: 33
Fairfield Dairies. Kwa Zulu Natal, on track	Agro Industries	RCF: 1, 620, 796		IRR hurdle of 31.6%		Replacement of Shareholders	HDP Managers: 19 Female HDP Managers: 3 HDP New jobs: 55 New Female HDP Jobs: 7
EVOLUTION ONE-	**Amount invested % total fund**	**Expected after tax IRR**	**Investment period**	**Disinvestment period**	**Estimated net IRR at end June 2013**	**HDP S/holding**	**HDP employed**
Evolution One Fund	65%	24.6%	6 years (2008 – end 2013)	4 years (2014 – end 2017)	25%	25%	2 HDP males. 1 HDP female has recently resigned to pursue new opportunities.
Evolution One client's name, region, status	**Business sector, start up or new**	**IDC commitments & RCF Amounts committed**	**Type of RCF financial instrument**	**Pricing**	**Duration, grace and repayment period for IDC and RCF**	**Purpose of financing**	**B-BBEE status** **B-BBEE impact**

	development						
Red Cap,Eastern Cape, on track	Wind renewable energy, new development	RCF: R4.72m, IDC: R581.6m	Ordinary shares	N/A (equity instrument)	RCF: EV1 exit investment by 2018. IDC: 15 year senior debt no grace period; 15 year mezz debt with no grace period; Equity funding with 17 year vesting period @ 7% RATIRR	Develop and build grid scale wind renewable energy assets	26% Community Trust, for social & critical infrastructure
Slimsun, Western Cape, on track	Solar renewable energy, new development	RCF: R1.21m, IDC: R102.48m	Ordinary shares	N/A (equity instrument)	RCF: EV1 exit investment by 2018. IDC: 15 year senior debt no grace period; 15 year mezz debt with 6 month grace period; Equity funding with 12.7 year vesting period @ 7% RATIRR	Develop and build a grid scale solar renewable energy asset	20% Community Trust, for social & critical infrastructure
RustM01 - Momentous Energy, North West, on track	Solar renewable energy, new development	RCF: R1.67m, IDC: R101.3m	Ordinary shares	N/A (equity instrument)	RCF: EV1 exit investment by 2018. IDC: 15 year senior debt no grace period; Equity funding with 15.1 year vesting period @ 7% RATIRR	Develop and build a grid scale solar renewable energy asset	17% Community Trust, for social & critical infrastructure
Acapulco, KwaZulu Natal, on track	Waste management, new development	RCF: R131 418, IDC: no further commitments	Ordinary shares & shareholder loan	Interest free shareholders loan	RCF: EV1 exit investment by 2018.	Develop and build a fertilizer production plant	No B-BBEE
Slimsun Too, Western Cape, on track	Solar renewable energy, new development	RCF: R42 000, IDC: no further commitments	Ordinary shares & shareholder loan	Interest free shareholders loan	RCF: EV1 exit investment by 2018.	Develop and build a grid scale solar renewable energy asset	No B-BBEE. 30% B-BBEE equity will be brought in at Financial Close.

UTHO INFRA-STRUCTURE SME FUND	**Amount invested % total fund**	**Expected after tax IRR**	**Investment period**	**Disinvestment period**	**Estimated net IRR at end June 2013**	**HDP S/holding**	**HDP employed**
Utho Infrastructure SME Fund	48.8%	20%	5 years	4 years	Nil	100%	50%
Utho Infrastructure SME Fund client's name, region, status	**Business sector, start up or new development**	**IDC commitments & RCF Amounts committed**	**Type of RCF financial instrument**	**Pricing**	**Duration, grace and repayment period for IDC and RCF**	**Purpose of financing**	**B-BBEE status B-BBEE impact**
West Coast Power Solutions (Pty) Ltd, Western Cape, on track	Green Industries Start-up	RCF: 3, 185, 000	Equity and SHL	IRR of at least 50%	Nil	Capex & W/Cap	86% HDI Shareholding 2 HDI Shareholders 0 % Female HDP SH 1 HDP Managers 0 FEMALE HDP Managers 1 HDP New Job 50% HDP jobs of total: 0 New HDP Female Jobs
Richards Family Investment Properties, Northern Cape, on track	2010 & Construction Start-up	RCF: 1, 901, 658	Equity	IRR of 42%	NIl	Capex	100% HDP Shareholding: 2 of HDP Shareholders 50% Female HDP SH: 2 HDP Managers: 1 Female HDP Managers: 50 % Female HDP managers of all Managers: No New Jobs

Bantsho Homes and Maintenance, Gauteng, on track	2010 & Construction Expansion	RCF: 2, 440, 000	Quasi Equity Loan	Prime plus 4%	NIl	Working Capital	100% HDP Shareholding: 1HDP Shareholding 0% Female HDP SH: 3 HDP Managers: 1 Female HDP Managers: 33% Female HDP managers of all Managers: 52 HDP New jobs: 100 % HDP jobs of total: 4 New Female HDP Jobs.
WHTP Construction, Eastern Cape, on track	2010 & Construction Growth Capital	RCF: 2, 439, 024	Loan/Profit Share	IRR of 51%	Nil	Working Capital	50% HDP Shareholding: 1 HDP Shareholder: 0% Female HDP SH: 1 HDP Managers: 0 Female HDP Managers: 0% Female HDP managers of all Managers: 90 HDP New jobs: 98% HDP jobs of total: 0 New Female HDP Jobs.

7.13 Annexe: Reports of visits to RCF clients

Visit report to: The Utho Capital Infrastructure SME Fund

Date: 30th September

Persons attending:

Modula Molofo
Stephen Pearce
Philippe Guitard
Daniel Chiwandamira

- Based on RCF Credit Application and riders and visit to the fund
- EIB Assessment document was not supplied
- Annual business review was not supplied

➢ **General Information**

Fund is managed by Utho Capital Fund Managers Ltd, controlled by a 100% BEE Financial Consulting Company called Utho Capital Ltd.

EIB approval was received in September 2010.

➢ **Investment project**

The Utho Capital Infrastructure SME Fund is a 9 year private equity fund with a target size of ZAR 300 million to 500 million. First closing should take ZAR69 million. Targeting 3 to 5 year equity and quasi equity investments for business expansion (70%) or start-ups (10%) or property development (20%).

Focus is to support BEE SMEs in infrastructure development, construction related industries and property development.

➢ **Financing framework**

First closing planned at about ZAR 69 million made up of RCF 30 million + BSS, Khula 30 million* (participation from Khula will take the form of a loan to a SPV due to Khula internal regulation not to invest in equity; loan will be on soft terms and conditions) + BSS, Musa capital 5 to 6.5 million (finally not paid in due to some trust issues) + Fund manager 1.3 million; finally the first closing was at ZAR 61 million.

Management fees are indicated from 3% down to 2% depending on the size of the fund.
A second closing bringing up the amount to ZAR 500 million was anticipated 18 months after the first closing. This unrealistic expectation proved that the fund manager lacked experience.
Board of Trustees will act as Investment Committee. It was planned to have 2 members of IDC, 1 or 2 from Khula, and 1 from Utho Capital. It seems dangerous to rely so much on IDC and Khula; experienced professionals from the targeted sector should have been involved significantly.

Main issue is to give 20% allocation to property investments which is usually speculative and outside IDC outreach normally.

The cost per job, based on potential investments in the pipeline is ZAR 131000, based on RCF investments. Targets are BEE SMEs while commitment is secured to support female employment.

RCF will also supply a grant envelop of ZAR 1.5 million, consultants being designed by IDC BSS Department.

- **Meeting investment guidelines**

Guidelines appear to be met by this investment at the Niche Fund level, such as Regional spread of investments outside Gauteng, BEE shareholding, BEE management, maximum ZAR 30 million and maximum 12 years duration while commitment to adhere by the guidelines at the investees' level is secured.

- **Results**

Expected gross IRR is 11% pa after a loss default rate of 10%; profit above hurdle rate to be split 20/80 between fund manager and investors.

Fund has invested in four projects so far:

- two of them were financing of property development; they are facing some difficulties;
- One is the financing of a start-up to provide bio gas. The project is at a turning point when important end buyers' contract should be signed. However, once this is achieved, further financing has it be organised to build the plant, implying a technical risk on the ability to produce the gaz.
- The last project funded was a property development which provided a satisfactory financial return and is nearly fully exited.
- Projects financed were geographically spread.

The socio economic criteria in terms of BEE shareholding and BEE employment were met, however with the time limit characteristic of property development.
Main issue rests with the slow disbursement of the funds at about ZAR20 million out of ZAR60 million.

- **Issues and lessons learnt**

- It was a first for this Fund Manager and it probably lacks professional support, especially linked to its very specific area of interest;
- Only SEFA (ex Khula) and IDC/RCF are investors in the fund, except for the small amount by the fund manager. This does not provide a wide range of expertise, guidance and support to the Fund manager; furthermore, it does not act as a catalyst to leverage the public investments;
- Members of the credit committee are not professionals with very specific abilities regarding the targeted sector.

For the future, should not a revision of the Investment Committee membership be considered? Should the fund manager not benefit from specific business support through BSS, further to a more thorough business need appreciation?

Nameplate

Date: 1st October
Persons attending: Hans Tilleman, Director
Gerry Geel, Director
Job Moraka, Director
Philippe Guitard
Daniel Chiwandamira

- Based on RCF Credit Application and visit to the client
- EIB Assessment document was not supplied
- Annual business review was not supplied (recent investment)

➢ **General Information**

Nameplate is a start-up business established by three former executives from 3M. Business plan is to address the "visibility" market, i) for the mining industry (about 50% of activity) and ii) Public visibility at all levels, national down to local.

Support from IDC/RCF is welcome while it is regretted that delays took about 18 months before funding could be secured due to a few modifications along the process.

It is however recognised that commercial banks would not have supported this start-up.

➢ **Investment project**

IDC/RCF to fund the start of the business, including the purchase of the machinery, the recruitment and training of the staff and the development of the contracts.

At present most equipment has been received. A machine is still due from Germany soon.
Commercial business is starting with the company looking at a number of tenders.

➢ **Financing framework**

Financing is based on an IDC term loan for 5 years with one year grace period, supported by ZAR 2 million equity from the three partners plus one equipment supplier 10% of equity shall be given to the Workers Trust.

RCF subordinated loan is for the same duration, however bullet to allow time for the cash flow to grow. Interest is fixed at 5% gross IRR plus a percentage of the turnover to achieve 10% gross IRR over the life of the project.

The bullet repayment shall probably have to be negotiated when due, if the company does not have the means to pay the full amount at once.

BSS needs assessment has been conducted. Training shall be organised in the near future.

- **Meeting investment guidelines**

Investment guidelines are met in terms of enterprise size, BEE ownership, management and employment. Female HDP minimum number should be met when activities and recruitment increases.

- **Results**

It is too early to assess results in as much as the enterprise started operation in June 2013. Staff number 12 at the moment and should grow when business develops.

There is plan to establish a HIV/AIDS awareness plan and an environment plan.

- **Issues and lessons learnt**

Main lesson learnt concerns the support granted by RCF as a bullet loan which shall effectively support the enterprise during its initial years.

It is duly noted that equity support would not have added much to the company financial structure, however, support in the form of real equity could be envisaged when the loan falls due, if business shows good prospects then.

The evaluators are of the opinion that RCF involvement with Nameplate fully meets its development agenda.

It is too early to know if business will be coming as expected. It is recommended that the BEE shareholder takes an active part in securing proper contracts. Impression is that it is not a BEE led project and based on our experience with other investees, this usually appear like a significant factor of success.

Pharox Lumens

Date: 1st October

Persons attending: Brian Ndoo
Philippe Guitard

- Based on RCF Credit Application and visit to the client
- EIB Assessment document was not supplied
- Annual business review was not supplied

- **General Information**

Pharox Lumens belongs to a larger group of which was not effectively assessed in the credit application. Pharox together with a JV partner has secured a contract from ESKOM to upgrade the lightning energy efficiency in a number of areas nationwide.

Pharox was established in 2009, its activities are limited to the establishment of a JV with a Dutch partner and the delivery of the ESKOM contract.

Plans for the future are for the company i) to try and obtain a second similar contract from ESKOM, ii) to develop consulting and support activities to corporates to improve their green efficiency, linked to the energy consumption and iii) develop manufacturing of some green energy products.

- **Investment project**

The project funded by IDC and RCF is tantamount to project finance, most of the financing and repayment being based on the ESKOM contract.

RCF facility was subordinated to the IDC financing. Both had similar duration and grace period, while the interest was different for each one, reflecting as far as RCF is concerned the expected 10% gross IRR, with 5% upside based on turnover percentage.

At this stage, the installation of the new bulbs is completed and performance is above the expected energy saving so far. Payments are due quarterly based on the sustainability of the LED lamps supplied which again is above expected performance.

The company is therefore able to meet the repayment schedule and should gather good profit further to the above expected performance.

- **Financing framework**

The RCF financing being of similar duration like the IDC did not provide real equity or quasi equity support. Its subordinated feature was limited to IDC loan and therefore was not attractive to commercial banks.

This financing framework had the characteristics of project finance and not of equity support.

However, the benefit to the company was that if it had not received the IDC/RCF support, it could not have raised the required financing from the commercial banks.

- **Meeting investment guidelines**

Guidelines appear to be met by this investment, such as BEE shareholding (100%), BEE management (100%), maximum ZAR 30 million and maximum 12 years duration.

At the employment level, the company now has 9 permanent staff and its implementation phase led to the employment of 200 temporary staff for 6 months.

One could check on the female employment ratio, and the company does not have a HIV/AIDS awareness plan.

- **Results**

Results were good as far as the project is progressing satisfactorily, that a number of HDP were employed, while only temporarily and the company tries to build on this successful first contract.

BSS needs assessment has been conducted with some area for support identified. Company is in the process of getting the support organised.

- **Issues and lessons learnt**

Main lesson is that this successful support was not granted as equity support to a new company but rather as limited project finance, with the benefit that a new company could prove its capability with the business;

Limit to the financing so far is that it did not allow the company to be financially strong and secure commercial lending.

However, it may be a necessary first step to prove its capabilities through a limited and risk secured project finance before entering into long term equity support to ensure a more sustainable activity development.

Success shall be confirmed if the company manages to secure additional contracts, but more importantly if it can develop ancillary business as planned which do not require such important financing up front.

Power 98.9 FM (Pty) Ltd (Power FM)

Date: 1st October 2013

Persons attending: Given Mkhari
Philippe Guitard
Daniel Chiwandamira

General Information

Power FM was licensed in December 2011 but only began operations in June 2013.[40] It is an English medium, talk-led commercial radio station which broadcasts in Gauteng Province.

The station is owned by MSG Afrika Media, Ndalo Media, Zico and other investors. The overall emphasis of Power FM will be on talk, with between 60% and 70% of air-time being speech-based programming.

The radio station saw an opportunity to be a **catalyst** and open up frank debate among its target audience on pertinent issues in the country. As such it uses a dual approach in order to achieve its aims which are:

i. Transforming the media's role in society with a view to facilitate a safe space for every South African to hold authentic conversations and express themselves on what is happening in the country rather than in a closed environment between individuals. These discussions could be on the direction of the economy or the country's past but people do not openly discuss them in public for fear of being judged as being anti or pro-apartheid or "sucking up to the current administration". Another example could be black South Africans who sacrificed their lives fighting for the liberation of the country who think this is not the country I fought for. There are also young people who are thankful for the liberation heroes but do not feel they are the ones who will take the country forward and
ii. Ensuring that the business is sustainable

Entry into the market

Several opportunities exist in the radio talk show market and Power FM aims at filling these gaps: These gaps are briefly explained below:

i. There is currently only one independently owned talk radio station in Gauteng(702) and one in Cape Town(Cape Talk);
ii. There is a need for a radio station that has a split between talk and music, however with a higher percentage of programming being aimed at talk;
i. Current radio stations are white dominated and its generational
ii. There is no radio station that caters explicitly for the needs and interests of the black audience; and
iii. There have not been any post 1994 media businesses and a lot of the current businesses are second to fourth generation businesses.

[40] The reason for the delay was the process of seeking capital on a loan basis and not getting funding from an Investment fund because of a "selfish view" that the work put in was worth the wait and did not want to give the value away. However, had it not been for IDC and NEF funding, MSG would have had to settle for an equity investment in Power FM because they had already had many approaches from potential investors.

The primary target audience will be black males and females between the ages 25 and 49. Given the history of the media, there is no platform to facilitate such a conversation with.

Shareholding

The major shareholder in Power 98.9 FM (Pty) Ltd ("Power FM") is MSG Afrika Media (MSG). MSG has a positive track record in radio start-up and operations and will be responsible for the management of the radio station. MSG would use its relationships institutions in the advertising and media buying industry.

A capital injection of R34.8 million to fund the radio station's start-up capex and operational costs was requested from the IDC. The investment is as follows: IDC – R13.5 million and RCF - R20 million. The RCF investment is in a form of a subordinated loan.

The shareholding structure of Power FM is shown below:

Table1: Shareholding Structure

Shareholder	% Shareholding
MSG Afrika Media (Pty) Ltd (MSG)	50.1
Zungu Investment Company (Pty) Limited (Zico)	20.0
MIB Radio & Media Investments (Pty) Ltd (MIB)	7.0
Friedshelf 1136 (Pty) Ltd (Ndalo Media)	9.0
AIH Media (Pty) Ltd (AIH)	3.4
Friedshelf 1125 (Pty) Ltd (Kgalagadi Media)	4.0
Friedshelf 1135 (Pty) Ltd (TT Media)	2.5
Friedshelf 1134 (Pty) Ltd (Thonga Media)	2.0
Friedshelf 1122 (Pty) Ltd (Jacobs the 4th)	2.0
Total	**100.0**

Investment project

The RCF subordinated loan facility will receive a minimum of 5% IRR before tax and a target 10% before tax is expected by achieving 10% net profit after from the year 2019. IDC's term loan was priced at prime plus 1%.

Financing framework

The company required a total of R79.3 million in order to reach breakeven and the proposed funding structure of Power FM was as follows:

Funder	Instrument	Amount	%
Shareholders	**Ordinary Shares/Loans**	**22 000 000**	**27.7**
	RCF subordinated Loan	20 000 000	25.3
	Team Loan	13 500 000	17.0
	Capitalised Interest	1 340 000	1.7
Subtotal IDC		**34 840 000**	**44.0**
NEF	Term Loan	4 500 000	5.6
	Mezzanine Loan	18 000 000	22.7
Subtotal NEF		**22 500 000**	**28.3**
Total		**79 340 000**	**100.0**

The IDC put up an RCF subordinated loan of R20 million over a period of 10 years with the final disbursement date due for the 31st December 2014. The amounts will be disbursed in two tranches at 50% each after the achievement of each of the 2 milestones.

Results

The investment is expected to facilitate a lot of positive growth in the sector as shown by the various researches that have been conducted.

- **Jobs:** The station is expected to create 67 permanent jobs
- **Black Empowerment:** The investment facilitated industrial capacity through support of up and coming talented young black entrepreneurs and the development of talk radio and support of broad-based black economic empowerment company. The station expects to create 67 permanent jobs.
- **Audience:**
    - **Listenership:** The listenership number surveys are conducted through a research by the South African Audience Research Foundation (SARF) which uses the Radio Audience Measurement Survey (RAMS) on a quarterly basis. The first results for Power FM are due in November and these will give an indication of the station's listenership. The estimated broadcast area footprint population (as at July 2011) is approximately 9.83 million with an audience projection for 2011 which is 788,840.
    - **Internet:** Power FM is only 105 days old but is the second most clicked radio station on the web with an average of 73 000 unique page visitors per month after Power FM which is a national radio station that has been around for about 40 years with an average of 100 000 unique page visitors.
    - **Social Media:** In social media, Khaya FM, a major competitor, is 15 years old and has just below 15000 twitter followers, whereas Power FM is at 25000.
    - **Influence:** After only 48 days on the air the station was ranked the second most powerful media platform in the country after the Mail and Guardian. In a list including international media entities Power FM was ranked fifth after Reuters, Financial, Bloomberg and Mail and Guardian respectively. This has put Power FM ahead of all the radio and television stations in that short space of time

Revenue Inflows

The most encouraging feature in all this the quality of the advertisers that include banks and cellular operators (Cell C, MTN and Vodacom).

Currently, month on month, the station is performing at 400% ahead of the budget on revenue. The revenue figures are as follows:

- Month 1 = R1 Million
- Month 2 = R1.7 Million
- Month 3 = +R2 Million
- Month 4 = R3.4 million projected

The focus of the investment was in capex and infrastructure while pushing down the opex costs. This is because image in the industry is very important especially when attracting potential clients.

Issues and lessons learnt

- A start up business needs a strong market research base
- There is space for a black only audience in radio in the market
- Partnering with shareholding entities such as Ndalo Media is a positive step because they have experience in the media space
- There is space for black businesses in white dominated entities as long as there is a thorough business analysis that has been undertaken

Astradeals 220 CC

Date: 3rd October 2013

Persons attending: Jaco Kritzinger
Zeph Kolobe
Daniel Chiwandamira

General Information

Astradeals is a start-up SME located in Polokwane, Limpopo Province. It was established by entrepreneurs, Joe Chuene and Jaco Kritzinger for the initial purpose of providing oxygen gas to the welding industry and later to the medical and other industries.

Motivation for the business

The market is monopolised by three multinational companies, Air Liquid, Air Products and Afrox. The Astra Deals plant is the only South African owned in the country. If this succeeds, there are plans to franchise it and IDC will be asked to support that process.

IDC through RCF 2 provided R2 million in subordinated loans at 6% interest rate for capital expenditure as well as start-up costs. The loan was sought from the IDC because other financial institutions such as commercial banks were concerned with the risk.

Business Support from the IDC

Astradeals benefited a great deal from the IDC's BSS because it assisted the SME with the meeting the requirements to operate in the industry. The main support received was in the following areas:

i. Obtaining the required paperwork to operate in the industry
ii. BEE Certification

The expectation is that this will be a continuous process. The BSS was valued at ZAR125, 000 funded on a 50-50 basis between IDC and Astradeals.

The shareholding structure of Astradeals is shown below:

Shareholder	% Shareholding
Joe Chuene	51.0
Jaco Kritzinger	49.0
TOTAL	**100.0**

Investment project

The RCF subordinated loan facility will receive a minimum of 5% IRR before tax. DFD will participate in the upside based on 1% of turnover payable annually from 2 years after 1st drawdown provide the company is profitable and remains profitable after payment of sweetener. The upside will continue until a minimum of RBTIRR of 10% is achieved. If the minimum RBTIRR of 10% is achieved prior to exit, the upside will end on exit.

Financing framework

The company required a total of ZAR3million and the proposed funding structure was as follows: IDC plant and equipment loan (UIF) ZAR1million and RCF subordinated loan ZAR2million.

Results

The project has not yet started and as such there are no results to be discussed at this stage.

Issues and lessons learnt

Provision of BSS is very important is start-ups especially involving technology intensive industries as is evidenced by the experiences in this project. According to the project promoters, without the consultant who is regarded as a mentor, it would not have been possible to get the project to take off. The mentor must be highly knowledgeable of the industry in order to be respected by the project promoters.

There is potential for other SMEs to participate in the value chain around this investment if it succeeds.

Visit report to Cyclocor

Date: 7th October

Persons attending: Vezokuhle Msibi
Philippe Guitard

- Based on RCF Credit Application and visit to the client
- EIB Assessment document was not supplied
- Annual business review was not supplied despite situation not favourable and investment already 2 year old.

- **General Information**

Cyclocor KZN (Pty) Ltd ('CKZN') is a start-up entity that will manufacture recycled polymer-bonded fire-resistant 'green' roof tiles with low-weight/high-strength capabilities based on technology licensed from 51% shareholder Cyclocor (Pty) Ltd ('Cyclocor'). 49% of CKZN will be owned by 100% BEE entity Batuka Investments (Pty) Ltd ('Batuka'). CKZN will take over an off take agreement originally signed by related company Cyclocor Manhole Covers (Pty) Ltd ('CMC') to supply 1.2 million roof tiles per year (ca R8 million pa) to Group Five Motlekar (Pty) Ltd ('G5 Motlekar').

CKZN's initial market focus is contract based. CKZN has eased their market penetration by obtaining interest from two major players in the industry, Imbani Projects and G5 Motlekar, who constitute approximately 80% of the forecasted budget.

- **Investment project**

The project is to fund the start of the business, including the purchase of the machinery, the recruitment and training of the staff and the development of the contracts.

Risk rests on only 2 big clients; however, it seems that the company managed to secure an important contract from the fourth largest house building company for 1500 houses in the area.

Risk on securing plastic waste supply materialized in the sense that competition from China arose driving the prices up, while the inconsistencies of the supply proved challenging for the manufacturing process.

After two years' experience, the issue is not so much on the marketing side where success has been met, but on the manufacturing process and securing the proper waste.

Machines have to be improved after experience and BSS technical support, with a further ZAR 3 million, while the shareholders do not have the means to follow up.

Recent developments have seen two new plants being developed by BEE entrepreneurs with NEF support, and Cyclocor minority shareholding, one in Cape Town, one in Johannesburg. The Cape Town one is already operating, having benefited from lessons learnt from the Durban plant.

At the company level, competition is not real an issue, since the tiles cannot travel such a long way, issue might concern the waste supply, however, here again, distance protect the Ladysmith plant. Main issue is that these three plants should have cooperated more under NEF guidance and Cyclocor involvement, and the NEF could have waited to confirm the Cyclocor process and results before committing to these new projects. IDC/RCF are not involved in these other plants.

Good point is that this IDC/RCF plant seems to be a success as far catalysing development (two further plants) through example, provided the process can be profitable.

Finally, with hindsight, one can regret that the pilot phase has not been longer to ensure proper fabrication performance.

- **Financing framework**

Financing is based on term loan from UIC and NEF plus subordinated loan from RCF.
NEF also financed working capital requirements as well as BEE share capital!

High leverage at only 29% shareholding funds, out of which some is NEF refinanced.
RCF pricing does not include an upside in case of successful investment. Upside is capped at 10% gross in case of success, bullet!!!

BSS needs assessment was conducted three months after start of business. The main issue concerned the production process. TA was received which proved positive.

- **Meeting investment guidelines**

Investment guidelines are met in terms of enterprise size, BEE ownership, management and employment. Female minimum number should be met when activities and recruitment increases.

152 permanent employment has been created, including female employment. An HIV plan exists with two conferences having been organised so far.

- **Results**

Results are not there whereby production reached about 70,000 tiles per month for about ZAR 800,000, i.e. only 50% of the budget.

A further investment of about ZAR 3 million would allow for the purchase of improved equipment to meet the challenges, allowing for the production to reach about 250,000 tiles per month.

It is suggested that one of the major housing construction projects should support the further financial needs, to ensure not only necessary financing but consolidate some of the up take risks.

- **Issues and lessons learnt**

Client appreciates the upside being payable only at the end of the loan, provided that the cash flow is positive;

Client appreciated the professionalism of IDC/RCF compared to NEF.

Client would have agreed to a RCF equity investment possibly up to 25%, provided the price would have been acceptable, so has to provide financial strength. However the client was not aware that the RCF facility was designed for such equity or quasi equity support.

Last let's mention that with such new development and new processes, the pilot phase should be given more importance, and further development should await confirmation that the development is viable.

Partnering with a larger group to provide some security for the future would have limited the financial risks as well as providing an outlay to the production.

Lushof Fruit (Pty) Ltd

Date: 7th October 2013

Persons attending: Warren Bam
Enriko Fourie
Daniel Chiwandamira

General Information

Dreammaker Fruits Group is in the business of growing and selling berries and grapes to the United Kingdom and South African markets. The Dreammaker group carries out the farming of Northern Highbush and Southern Highbush types of Blueberries, table grapes, Raspberries, Blackberries on three farms in the Western Cape namely, Teeland and Zuurvlakte which are managed as one unit. The third and only organic farm in the group is Lushof Fruit located 15km to the South of Porterville at Sharon.

Lushof Fruit is a broad based black empowered company that currently produces blueberries (30 hectares) and grapes (30 hectares) using organically certified production methods. In addition to supplying Lushof with plant material, Eurafruit, through licensing agreements also markets the fruits locally and abroad. Lushof's products are sold to retailers in Europe and the USA.

Lushof's maintenance of market share throughout the European winter season is based on the fact that they have the advantage of being the first to market for Southern Hemisphere countries. The farm is able to start planting in early October with the right varieties and growing techniques and finishes by early December with the SHB types. As the only organic farm in the group, it is important to have continuity after Christmas for its customers, so the farm has smaller area where it grows the later "Rabbit Eye" types. With a combination of the right varieties and growing techniques, it is possible to continue production at least until the end of January. These types also store very well which further extends the season for the Organic fruit, which obtains a healthy premium over the conventional production.

Shareholding

Lushof Fruit (Pty) Ltd is 74% owned by Dreammaker Fruits (Pty) Ltd and the Lushof Workers Trust the remaining 26%.

The shareholding structure of Lushof Fruit is shown below:
Table1: Shareholding Structure

Shareholder	% Shareholding
Dreammaker Fruits (Pty) Ltd	74.0
Lushof Workers Trust	26.0
Total	**100.0**

Investment project

Lushof required funding for the establishment of an additional 70 hectares of organic blueberries to use for development and production capital.

The RCF subordinated loan facility had return requirements budgeted at 8% RBTIRR based on a hurdle of 5% with an up-side of 1% of turnover as from 2018.

Financing framework

The company required a total loan of R60.5 million for the development of 70 hectares of blueberry orchards, upgrade and construction of workers' accommodation as well as working capital and operating expenses. The proposed funding structure for Lushof Fruit was as follows:

Funder	Instrument	Amount (ZAR)	%
IDC	Developmental Loan	45 500 000	75%
	Capitalised Interest	4 300 000	
RCF	RCF subordinated Loan	15 000 000	25%
Total		**60 500 000**	**100%**

Results

There have been several developments with regards to the implementation of the fund requirements. These developments are briefly explained below:

Workers Trust

There is still need to relook at the Workers Trust Empowerment Scheme. Currently the level of shareholding is at 26%. The Trust was meant to benefit from the company not the IDC fund. Currently the Trust is not generating any extra funds on its own but is waiting for the company to pay out dividends. It is suggested that the Trust sets up a business that will offer a service to Lushof Fruits so as to earn regular income. It also emerged that some of the farm workers are not beneficiaries of the trust and there is need urgent need to relook at the trust and find ways to ensure all workers are represented.

Accommodation

Part of the agreement with the IDC was that accommodation be made available to farm workers. Lushof is in the process of building houses as well as hostel facilities and the building of the hostels will begin in February 2014 after harvesting. The other reason for the delay was that certifications from the local government came late.

Business Support

Business Support logistics have reached advanced stages and arrangements with the consultants have been made. The proposed dates for the capacity building intervention have been set for March.

HIV/Environmental Issues

There are no HIV programmes or awareness initiatives that have been conducted by the company. There is however, contact with the local clinic who conduct HIV programmes.

Number of HDP in management

The company still needs to meet its targets with regards to HDP representation. With regards to this, the trustees requested to be involved in management, and as a result, the company has advertised for internally for candidates to fill in some positions if there are qualified individuals. Further the identified individuals will be trained by the company in preparation for these positions.

Other Issues

There are plans to build a crèche for the employees' children. The crèche will be funded from the Waitrose Foundation and the company's internal funds.

Visit report to Aristopix

Date: 8th October

Persons attending: Andiswa Mkrola
Vuyiswa Mfaka
Philippe Guitard

- Based on RCF Credit Application dated March 2011 and visit to the client
- Enterprise business plan was not supplied
- EIB Assessment document was not supplied
- Annual business review was not supplied

- **General Information**

Aristopix is a start-up created by two professionals with a good experience of the sector, to purchase, lease and manage for 5 years the King Sabatha Dalindyebo Municipality (KSDM based at Umthata) 66 new vehicles fleet on top of the existing 48 that Aristopix managed since 2010.

The business was started just providing fleet management support to KSDM existing vehicle fleet in 2010. They then won a municipality tender to supply and manage a further 66 vehicles.

- **Investment project**

Plan was to buy the 66 vehicles plus maintenance contract plus a tracking system to monitor the fleet as well as the drivers' performance on time.

It was planned that the project would create 90 permanent jobs, 10 with Aristopix and 80 with the Municipality.

Gearing is high (10% equity at most), based on asset finance plus assignment of contract.

In practice, the founders were not able to provide equity and the tracking part of the deal was sub contracted to their informal partner Freight Dynamics.

Overall the project represented about ZAR 42 million which was financed as project finance, based on the strength of the Municipality.

- **Financing framework**

Funding was supplied by IDC as a 5 year term loan ZAR 12.4 million, plus 6 month VAT advance plus RCF 5 year ZAR 5.5 million subordinated loan both with 3 month grace period.

NEF covered the balance with a ZAR22 million 5 year loan.

RCF repayment of principal is subject to cash flow availability; pricing at gross 5% plus upside at 1.5% of turnover after year 2, not capped.

BSS support loan of ZAR256, 000 at zero interest rate is also made available alongside the grant.

- **Meeting investment guidelines**

Investment guidelines are met in term of size, employment, BEE shareholding and management, environment plan. The cost per job created seems on the high side at about ZAR 450,000.

- **Results**

After 2.5 years, the company is on track with all loan repayments and interest up to date. Enterprise is very grateful to NEF, IDC and RCF support since the banks were not interested to fund the project. Business just breaks even with no real profit to show for. The profit will only come at the end, incorporated in the remaining value of the depreciated vehicles which will continue to have a useful life.

Today the main challenge is to find other contracts, to improve the economies of scale under their management. The enterprise is responding to tenders, but it seems that municipalities are on the hold pending the elections due in 2014.

Not to be too dependent on these contracts, the enterprise is trying to sell more services to various users such as fleet tracking, pure maintenance or other services not requiring important capital which they do not have. This should be the real future of this enterprise.

They have been told by IDC that it would not consider financing another contract if they were to get one, due to a change of policy. The mission is surprised, more so that the job creation element has been met in excess of the initial plan since the company employs about 30 staff, 7 of them women, that it is 100% BEE controlled, and that the Municipality has employed more than 50 persons further to the fleet expansion.

Also the enterprise has a HIV awareness plan as required.

Finally, the enterprise benefited from BSS which was well appreciated. It regrets that the full amount was consumed and not increased and that they now have to pay with their own resources 100% of the support and training that they continue to source from the same supplier.

- **Issues and lessons learnt**

Main lesson learnt is that supporting a new investment in the form of project finance seems to be working, provided the management/shareholders are real professional in their sector.

That IDC together with RCF but also with the support of NEF has managed to start a business which would not have had a chance otherwise with the commercial sector in view of its risk profile.

Enterprise regrets that IDC would not consider financing another contract if one was secured. It is doubtful that the banks would finance a second contract of a similar nature.

Enterprise regrets that no visibility sign is provided to inform the enterprise partners that it is funded by IDC and RCF/EU.

Pick and Pay

Date: 8th October
Persons attending: Manila
Philippe Guitard

- Based on RCF Credit Application and visit to the client
- EIB Assessment document was not supplied
- Annual business review was not supplied

- **General Information**

Pick and Pay, a large retailer chain sought to expand its network of stores through franchisees, especially in the poorer areas of the country.

It relied on BEE shareholder/managers who usually do not have the funds nor the collateral to supply the required financing in such places like Kokstad on the border of Kwazulu-Natal and Eastern Cape, a poor area of the country.

P&P has therefore approached IDC to finance a number of its new BEE franchisees.

- **Investment project**

Initially, the plan was for four franchisees to be funded, which ended up with three being funded. Significant employment was envisaged for each store, including female staff, at a cost estimated at ZAR 150,000 per job created.

Stores would end up being 51% controlled by the BEE managers.

The P&P Kokstad franchisee was developed by Mr Manila, a Regional Manager with P&P who had very limited self-financing available. Thanks to IDC/RCF plus P&P finance and another P&P franchisee, the deal materialised in 2011.

- **Financing framework**

Funding is supplied by IDC as a term loan, maxim ZAR3.6 million, plus RCF subordinated loan maximum ZAR.8 million plus a guarantee maximum ZAR 0.6 million.

Pricing of neither the facilities nor their term is indicated in the credit application given to the mission.

In the later years, the new stores have been increasingly financed by the Commercial banks, based on the good example provided by the initial IDC/RCF operations.

As far as the P&P Kokstad franchisee is concerned, it is mentioned that such development could not have happened with only bank support, not only because the banks would not have taken the risks, but also because they would have been too expensive compared to the business cash flows.

The interest rate structure, including the RCF upside is appreciated, as not too heavy for the enterprise, compared to its available cash flow. It must be said however, that the business just breaks even and treasury is tight. This should improve significantly once the loans are fully repaid. The fact however that the promoter is able to buy out his partner while the loans are still outstanding proves the profitability of the operation.

Mr Manila has started another P&P franchise with support from the banks only and the operation is suffering.

- **Meeting investment guidelines**

Investment guidelines were met in terms of size, employment, BEE shareholding and management, environment plan.

The franchisee has an HIV awareness plan, in line with IDC/RCF requirement, but also in line with P&P policy.

- **Results**

Initially three stores funded have performed very well one of them having paid back the facility three years in advance.

The Kokstad franchisee is on track with all payments. The franchisee is in the process of buying out its partner, thereby becoming a 100% BEE investment.

76 new jobs have been created, 70% female plus jobs created at the enterprise suppliers' level.

- **Issues and lessons learnt**

Very positive operation with regard the number of stores successfully financed, including the Kokstad franchisee, thanks to the careful selection of the franchisee as being a professional of the retail sector, with good management expertise and significant involvement in the business.

It seems that the commercial banks are now prepared to finance new franchisees, however at a higher cost than IDC and probably requesting a lower gearing.

The success of this operation was the result of good cooperation between IDC/RCF and Pick and Pay which was very supportive of its franchisees, a must in this kind of competitive operations.

Micawber 803 (Pty) Ltd Noodle Factory in the Western Cape

Date: 8th October 2013

Persons attending:

Mohamed Shakiel Parker
Daniel Chiwandamira

Background

Micawber 803(Pty) t/a Factory Noodle (Factory Noodle) is a 60 000 unit Greenfield manufacturing concern situated in Philippi-Western Cape. Factory Noodle has acquired the rights to manufacture the Alhami brand under the licence from Macro Ocean (Malaysian Company). Shakiel Parker, who started the business by acquiring the sole agency to sell and distribute "Alhami" instant Noodle in 2000, is the sole shareholder of the company.

Funding from the IDC

The application to IDC was made in 2009 and approved in 2010. The plant was commissioned in February 2012. It took the firm 10 months (from February 2012 to December 2012) to master local noodle production. There was no local skill and the skills of a noodle master needed to be acquired abroad. The noodle master will work with the company for the next three years and transfer skills to the locals.

Micawber received two funding facilities, from RCF and IDC. The bulk of the funding has been used for working capital. However, the company has requested IDC for a further cash injection of 5 million for working capital. It was revealed that the company is currently operating at half capacity and ideally the company should operate for 24 hours with three 8 hourly shifts consisting of 30 employees. Currently this is not happening. In future the company would like to employ more workers. The IDC has been lauded for having payment terms that were better than the banks though there was a high IRR tax. It was concerning to note that there was no knowledge of the RCF fund.

It was also noted that some of the logistics such as the reports that are requested also tend to frustrate management.

There was a concern from the investee that the IDC about the time lag between the approval and the disbursement of the funds. In addition, the business is also restricted by the IDC concerning borrowing from other institutions. It is also difficult to secure funding because the capacity is not utilised hence no profitability. Funds are required to increase capacity so as to enjoy the economies of scale and then profits could be expected.

BSS Funding

With regards to BSS it was noted that the RCF had offered BSS to the company but it had been turned down because the owner already has acquired in-house knowledge on how to run a business.

Opportunities for Down-streaming
It was pointed out that there were big opportunities for down streaming industries e.g. packing spices and making cups.

Markets
It was noted that the company was the first to produce noodles though there were some companies such as Maggie who were also venturing into that area. Competition is stiff since big companies such as Macro import noodles directly from China. The company is in talks with some of the country's top retailers such as Game and Shoprite regarding supplying them. The problem is that Micawber cannot produce enough to meet the demand in the market which is supplemented by imports from China.

The company is also strategically positioning itself for the regional, East and West African markets when it has increased its capacity.

Investment Project
IDC Credit Committee of the 27th August 2010 approved R4.7 million to Micawber. The required return is 10% RRTIRR.

Results
The company is employing HDIs and has also trained unskilled workers. In addition the company is set to pioneer noodle production in South Africa and the region.

Lessons Learnt
The IDC might need to have more innovative uses of the BSS fund in cases where owners are knowledgeable about business and might not need the money.

Agri-Vie Investment Fund

Date: 8th October 2013

Persons attending: Lynette Thomas
Avril Stassen
Hermann Marais
Daniel Chiwandamira

1.0 Background

The Agri-Vie Fund operates in the Agri-business Sector. The Fund comprises two portfolios one of which is focused on South Africa (SA portion of the Fund) and the other Sub-Saharan Africa (SSA portion of the Fund) including South Africa (but investment in South Africa will be on a discretionary basis. The Niche Fund is structured as the South African Agri-Vie partnership which is a parallel structure in the overall fund and offshore structure which is in Mauritius.

The following are the drivers that warrant the establishment of a dedicated Private Equity Fund for the Agri-Business sector. These are:

- There is a need for sustainable BBBEE in agribusiness;
- The far reaching multiplier effects of the sector in SA;
- Limited supply of risk capital in agribusiness;
- The need to stimulate Socially Responsible Investment ;and
- The Positive knock on effects agribusiness has on other sectors.

Entry into market

The agro-processing sector turnover amounts to some R165 billion per annum (2006) in South Africa. There are good prospects for the agricultural industry and growth prospects for the industry are positive due to good overall economic and consumption expenditure growth and increases in households. A number of factors will also influence the prospects of the food and beverage processing industry over the coming years. These mainly include the following:

- Ensuring food security (sustainable supply) in South Africa and in the region;
- The expected growth in the production of bio fuels which could have a negative impact on food and beverage availability and specifically affect certain product groups such as soybeans, maize and sugar;
- Continuing changes in consumer markets especially a growing middle class, changes in tastes and preferences, on-going opportunities in value adding and changes in marketing;
- A continuation and probably an acceleration in the demand shift towards technologically more advanced processed foods; and
- Continued strong growth in the tourism sector presenting on-going demand in the hospitality and food service industries.

2.0 Financing Agreement

The investors are shown in Table 1 below. Investors are both local and foreign. In total there are 9 funders. Other funders include IFC (World Bank) and AFDB.

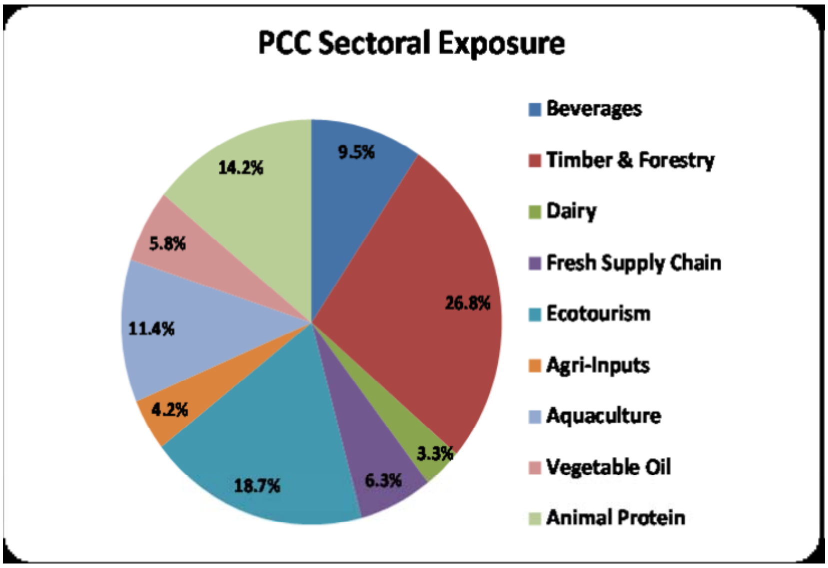
Investor	Commitment	Description
Sanlam Life Insurance	R140 million	For the SA portion only where R100 million is available for investment immediately. The remaining R40 is dependent on the value of the Fund by the second close. If the fund value reaches R700m by second close then the additional R40m would be available for investment
DBSA	Maximum R100 million	Will invest an amount equalling 25% of the size SA portion
Kellog Foundation	R140 million	For the SSA portion of the fund
RCF	R45 million	For the SA portion of the Fund. The RCF guidelines as per the EIB/IDC MOA stipulates that R30m is the maximum value that may be invested in any one Niche Fund, however a derogation of this clause (conditional upon a satisfactory overall assessment by the EIB has been discussed with EIB for RCF to invest R45 million in the fund
Know Fund	R75 million	

3.0 Investment Project

This is a 10 year fund. Agri-vie looks at a 6 to 7 year investment period with slightly longer periods for the earlier investments and lesser for the later transactions. On average, the investment period is 5 to 7 years. Agri-Vie is targeting a net return to investors of 20% in IRR terms (nominal before tax). The hurdle rate is 12% IRR. If the fund achieves the 20% then the 8% difference will be split 20/80 to the fund manager and the investors respectively. On this basis RCF could receive 18% nominal IRR which could be within RCF targeted returns for the RCF fund as a whole of ca. 17% before tax nominal IRR(RCF reflows are tax exempt. IDC as fund manager of RCF will be entitled to 10% of the total reflows (capital and returns) from this niche fund investment.

4.0 Results

The SA portion of the fund‘s focus on star-ups has created new jobs and entrepreneurs. The fund has also ensured that investee clients have BBEEE credentials thereby transforming the current SA Agri-businesses into BEE companies. On the South African side the fund has made 6 transactions in food, agriculture and agricultural inputs to date. As of 2008 the Agrie Vie Fund had the following geographic and sectoral diversification.



Several companies have benefitted from the fund and are deemed as successful. These investments were assessed in line with the RCF Criteria and other full range of developmental arrange. Through the narrow lense of the RCF mandate, there are two deals that tick all the boxes i.e. Vida oils in Kwa Zulu Natal and the Cape olive transaction. The Cape Olive is currently at 14% shareholding but there are plans to increase it to 25%. In Vida Oils, this has not been achieved bit the plans are in place. These two investments have by and large achieved the deployment target on the quantity side.

5.0 Lessons Learnt

Several lessons have been learnt from the Agri-Vie Fund. These are briefly explained below:

- If there is a primary agricultural component in the business the investments tend to be longer;
- Equity investments in a 10 year funds have a better chance of succeeding if invested in a vertically integrated fund rather than in a stand-alone farming venture;
- Need to maintain a balance between matrix and impacts especially when looking at BEE
- There is a risk to drive the full BEE benchmark in a short period of one year might not be realistic;
- There has been contact but no business has been done together. There is a scope for a formal community of practice engagement to share experiences. This is happening informally or during some private equity gatherings;
- They look at the platforms with an existing track record and a business model that lends itself to higher volume transactions and less effort required;
- Away from the financial support, interventions could focus more on mentoring, skills transfer at a larger scale for emerging entrepreneurs;
- Support for the venture capitalist structure in South Africa to pick up businesses and give them the required support;
- Establishment of a guarantee system to banks to allow them to offer debt lending to SMEs. The challenge is not the equity component but debt; and

- There is a stakeholder supply chain programme in Mexico where there a national programme that creates a pool of funding to address the issue of late payments and fund the supply chain. This could be established in SA with the support of big business;
- Agri-Vie has an active model thus it is represented on the board and in the audit and remuneration committees on the boards. On the informal side there is a regular engagement directly with either the CEO of CFO on a face to face basis
- In future there might be need to partner with other investors in the agribusiness sector. These are shown below:

Fund	**Description**
Emerging Capital Partners	Is an international fund which has been investing in Africa since 2000 and recently closed its fifth fund bringing the total capital raised for Africa investments to US 1 billion. It holds 35 investments in 30 Sub SAHARAN Africa(SSA) countries of which some 20% are in the agribusiness sector
Actis Africa	Has a long standing involvement in SSA Agribusiness and launched a $100 million fund in 2006 targeting an estimated 15% return for investors
Zeder Investments(PSG) Controlled	Is a listed agribusiness vehicle and in 2006 its call to KWV, Kaap Agri and Senwes amongst others

Despite these participants being competitors there appears to be limited supply of risk capital and or excessive demand for risk capital and AGRI-Vie intends to pursue these investors as co-investors rather than to view them as competitors

Amathole Berries

Date: 9th October

Persons attending: Ryan Davies
Philippe Guitard

- Based on RCF Credit Application, Amathole business plan and visit to the client
- EIB Assessment document was not supplied
- Annual business review was not supplied

- **General Information**

Project was promoted by Philip Howes who had some experience of the fruit business, but was not a farmer. Philip Howes did not have any funds to put in the project, his share of about 15% of the equity was to be recognised against under-priced blueberry plants supplied from his nursery.

IDC was to take 40% of the equity, Eastern Cape Development Corporation 10%, a SPV including Philip Howes (PH) plus the Workers Trust plus two BEE shareholders and one last shareholder with agriculture background 40% and PH another 10%.

Finally, the two BEE shareholders did not pursue the matter nor the agricultural technician.
So, the promoter PH had a minimal shareholding, paid through the supply of nursery plant, while there was no real BEE shareholder, with a real involvement in the management, not counting the Workers Trust.

Plan was to purchase about 350 ha of land, and to plant 225 ha of blue berries, all financed from borrowing or financed by shareholders. Business plan was very optimistic especially regarding the potential production per ha, bordering on fraudulent presentation, as can be seen with hindsight.

After 3 years, only 41 ha have been planted. Fruits are of low quality, production lost after harvesting and in transport, prices are lower than expected and production way below business plan. Due to a number of reasons, trust in the promoter has disappeared and the project has obtained his resignation.

File has been handed out to Work out and Restructuring unit.

Plan is to find a professional major investor to buy back the project at a loss to the financiers.

- **Investment project**

Project was heavily funded by IDC and RCF on behalf of the Workers Trust. Main issue was that the initial promoter of the project and GM had a conflict of interest being shareholder, MD and unique supplier of the blueberry plants.

Furthermore, at the financial level:

- Very high financial gearing, due to the whole land having to be purchased;

- Promoter did not commit his own funds, thereby having very limited risks, and significant upside should the project perform;
- The Workers Trust share was entirely funded by RCF, so no risk for the workers but very limited say in the management due to lack of management expertise

At the operational level:
Negative side:
- Nobody in the management with experience of blueberry cultivation,
- Terrible logistics to transport the harvest, neither the port of East London, nor Durban are equipped to handle cold storage chain, while the East London Airport flights cannot handle heavy loads (small aircrafts), so berries have to be transported by refrigerated truck either to Cape Town or Johannesburg at high costs;
- The access road to the farm is not passable during the rainy season;
- The manpower is far away, labourers have about ZAR 700 transport cost per month out of a salary of about ZAR 2000;
- Project could not plant well established and known blueberry varieties because the license for such plants is in the hands of Eurofruit (a large fruit marketing operation in SA) which would only grant access to the plants against a 10 year exclusive take off contract at low conditions.

Positive side:
- Access to water is secured or nearly secured for the whole plantation
- Project has a high employment impact in a very poor region and could have a pulling effect towards the out growers if it proves successful
- Higher future value processing of the crop, providing increased employment is also possible on site.

➢ **Meeting investment guidelines**

Guidelines were met; in as such it was a new development, with BEE employment in Eastern Cape. The BEE aspect was covered through the funding of the Workers trust by BEE, repayment coming out of the dividends!!!

Main issue was that there was no real BEE shareholder cum senior manager.

➢ **Results**
- Only 42 ha have been planted;
- Crop is way below budget;
- Things are starting to improve with a number of lessons learnt on the production and logistics side;
- Workers have benefited from training improving their education and skills;
- However, the present financial situation of the project is very bad.

➢ **Issues and lessons learnt**

Main issues, with hindsight are the following:
- Workers Trust while BEE should not be counted as effective BEE shareholders; a real effective BEE shareholder with management responsibilities should be part of all projects; (mission has noted that over a few sample investees met, those without BEE shareholder cum manager

seem to be performing less well); Probably, the reason the BEE shareholders in the above project finally declined to let go of a good job to get involved with Amathole Berries, it may be that they were not confident in the future of this project.

- Promoter should be somebody with experience in the sector he wants to develop;
- An agricultural project especially shall not be financed nearly 100% through borrowing, even in the guise of preference shares;
- A pilot phase should be organised before moving to the full blown out project, especially for new processes or new industries;
- A big player should have been associated with the project, being attracted by the soft finance, if not at the shareholders' level, at least in some sort of technical support agreement.
- It is a real challenge to find BEE with good management ability, minimum investment capacity, willing to take the risk of business development in such poor regions like Eastern Cape, to run a business in the wild.

Future of this project seems to all depend on the possibility to get one of the big players in the blueberry sector to take over the project with some incentive from development funding. It is understood that project is considering such issue with Agro Heaven, a large group in this sector. We recommend that Chilean groups involved in the industry (Chili is a world large producer of berries) should also be approached so as not to be too dependent on one solution which would dictate unacceptable terms.

The fact that no effective shareholder is involved in the management explains for example that nobody has seriously tried to contact Chilean or other investors… One understand that IDC has tried to identify some Argentinian parties through the Argentinian commercial attaché… but it seems that such a challenge should be taken more professionally by persons in the industry.

Evolution One

Date: 9th October 2013

Persons attending:

Guy Baxter
Steven Faure
Daniel Chiwandamira

The Evolution One Fund (the fund) is a 10 year private equity sustainability fund with a target size of R1 billion. The Founders of the Fund are Consensus Business Group (CBG), Pan African Capital Holdings (PACH), Capital Evolution (Pty) Ltd (CE) and Alluvia Group (PTY) Ltd (AG). The founders started working towards the establishment of the Fund in June 2007. The mandate of the Fund is to finance investments in South Africa and the SADC regional countries that advance the innovation and deployment of clean technology (clean-tech) in-order to greatly reduce or eliminate negative environmental impacts and hence improve the quality of life.

The Fund comprises two independent legal structures that will co-invest on a pro-rata basis. These structures comprise a limited partnership established in the British Virgin Islands(BVI) for the offshore investors called Evolution One (BVI) Limited Partnership(''BVI Partnership") and En Commandite (limited liability) partnership established in South Africa for investors wanting to participate in the local fund called Evolution One En Commandite Partnership.

The fund focuses on funding investments aimed at accelerating the adoption and deployment of tried and tested clean technologies across environmental goods and services markets in South Africa and SADC region countries. The Fund's investment strategy is premised on long term equity and quasi equity investments that are predominantly at expansion stage with some early stage and start-up investments only made in projects with proven technologies at commercial level and to a lesser extent a focus on later stage buyouts

The Fund will target eight sectors or industry focus areas as follows:

- Clean energy such as wind, solar, biomass, hydro wave ,geo thermal and energy efficiency(up to 50% of its investments)
- Efficient and clean manufacturing processes and technologies(cleaner production)
- Air Pollution Control
- Waste Management and recovery
- Water Quality and management
- Agribusiness, organics and natural products
- Forestry and certified value-added forest products and
- Eco-tourism and green real estate

Entry into Market

Climate Change and environmental degradation strongly support the development and introduction of new clean technologies that cuts across a variety of industries. The use of clean technologies such as wind and solar power to supplement energy sources for both domestic and heavy industry usage is thus a priority for future developmental efforts.

At present there are no competing or complementary clean technology funds in South Africa and Africa and the Fund will be the first private equity fund to offer South African and SADC regional entrepreneurs access to funding for environmentally sustainable businesses.
Key drivers that warrant the establishment of a dedicated private equity fund for the clean tech investment sector are:

- The need to stimulate Socially Responsible Investment (SRI) in this industry and the positive knock on effects clean tech has on other sectors;
- The limited supply of risk capital in clean tech sector;
- The far reaching multiplier effects of the sector in South Africa;
- Enabling government policy and incentives;
- An opportunity for sustainable BBBEE and PDI participation in clean tech;
- Potential for social equity and shared growth transformation through innovative deal structuring and SME participation;
- The need to ensure resource security due to depletion of natural resources; and
- Global climate change.

Shareholding

Still to be requested

Financing Agreement
Castleway Properties is the major investor in the project though there are other DFIs who have committed to funding the project. The World Bank (IFC) and the African Development Bank are major funders of the project.

List of Funders and Commitments

Investor	**Capital(R Million)**	**Commitments(USD Million)**	**Comments**
Castleway Properties Limited	267.0	26.7	
IFC(World Bank)	200.0	20.0	IFC capped at 20% of the total commitments
SIFEM	80.0	8.0	
FinnFund	80.0	8.0	
Total Commitments	627.0	62.7	
Actual First Closing	540.0	54.0	IFC commitment may not exceed 20% of total commitments
South African Portion			
African Development Bank(AFDB)	100		
Norfund	80.0		

Global Energy Efficiency and Renewable Energy Fund	120		
Risk Capital Facility 2(RCF2)	33.0		R30 million for investments and R 3 million for Business Support

Investment Criteria
The RCF SBU co-invests through the IDC direct channel with Wood SBU, however through this proposed Niche Fund channel, RCF funding will have a far broader reach in this sector creating a further avenue for business entities to access funding. The RBTIRR IS 19%.

Results
There are positive outcomes that are expected to be generated by the Fund. These are briefly explained below:

- The commitment of the investment Fund to technology sectors which mitigate climate change, carbon footprints efficiency, clean transport and recovery, water sectors, is strong enough to suggest the inherent environmental element safety consideration of the equity fund;
- The fund's strong focus towards investing in expansions early stage companies and start-ups (i.e. 85% of the fund will promote the creation of new jobs and entrepreneurs;
- The fund will also ensure that investee clients have BEE and BBBEE credentials;
- The fund will also target SMEs and will involve the development of clean energy and technologies for previously disadvantaged individuals (PDIs) and rural communities. The fund will invest in environmental goods and services with sustainable impact thereby creating a broader societal impact with net positive societal and ecological returns; and
- The Fund will be investing in start-up and expansion phase businesses. Such businesses from time to time, face non-financial challenges that could be resolved through business support interventions

MX Metal Shoppe CC (MXM)

Date: 10th October 2013

Persons attending: Sereshen Moodley
Daniel Chiwandamira

General Information

MX Metal Shoppe CC (MXM) was setup in 2006 with the purpose of manufacturing, supply and installation of mild and stainless steel balustrades & light to medium structural steelworks mainly to the construction industry. MXM's current product offering is mild and stainless steel balustrades, specialising in architectural design and light to medium structural steel works, and secondary steel works (cast in angles, gratings, cat ladders, mezzanine platforms.). Initially there were challenges especially with established competitors who charged very low prices in an effort to force the BEE competitors out of the market. This worked and they forced the company to go back to its forte.

MXM initially commenced business manufacturing, supplying and installing steel fixtures and shop fittings to the Edcon group. Subsequently MXM completed projects in low cost housing projects in Alexandra Township. To date MXM has completed projects for the 2010 Soccer World Cup stadiums such as Mbombela, FNB Soccer City with a total project value of R46 million. The company is also involved with clients in the Health, Beverage and telecommunications industry. Some of these projects that the company has undertaken include:

- Silver Star Casino;
- Gautrain Park;
- Rosebank and Marlboro Stations;
- Nedbank Phase 2 in Sandton;
- Heineken Brewery Phase; and
- Cresta Parkade.

Current major projects include:

- Brits Hospital;
- Nestle Babelegi;
- Isando Entyce Beverages; and
- MTN 14th Avenue.

The company has also successfully extended its product lines through the formation of Gridfast. Through extensive Research and Development exercise a prototype was developed in preparation for an SABS ISO9001 standard grating for industrial applications. Part of this developmental process involved undertaking overseas visits to China with a view to procuring the appropriate machinery and benchmarking his grating product to international standards. MXM now boasts a final product which is now fully compliant to the SABS ISO9001:2008 standard. Word of mouth is also extending the company's customer Gridfast customers are also highly impressed with the service to such an extent that they have referred the company to other customers.

The total staff compliment is 32 and the company has a loyal workforce which has been trained and up skilled. The respective staff members have been trained over time in the following key areas of work: boiler making, welding, grinding, measuring, cutting, spray painting, sandblasting, site installation and erection. Many have been tested by the relevant authorities and progressed from unskilled labour and semi-skilled to skilled labour. The staff turnover is nil.

Entry into Market
There is a large market for MXM products. The South African market is approximately R500 million per annum. The market for MXM's initial product offering was mainly in construction. The industry experienced a large boom with the 2010 Soccer World Cup but has since been in decline leading to the company experiencing negative growth.

There are two suppliers in the primary market, namely Andrew Mentis and Vital Engineering. The two companies control 90% with an equal split of 45%. Supergrid accounts for the other 10%. Currently these three companies are not coping with local demand and consumers are considering acquiring their products from foreign companies despite the perception in the market that South African products are superior. There is also a possibility that the current major players might also concentrate their efforts on the foreign market leaving a gap in the local market. Gridfast will initially target the neglected local market and has already started winning business from Andrew Mentis and Vital Engineering as a direct result of this.

The market for the new product i.e. grating is vast and consists of various primary consumers, namely: mining, civil construction, petrochemical, power and plant generation and shipping. The secondary consumers are mainly in housing construction. Mining companies are the biggest buyers of the new product. Furthermore, Gridfast will be the first fully fledged BEE grating company in South Africa.

Shareholding
The shareholding structure of MXM is shown below

Shareholder	% Shareholding
Ashokgan Perumal Moodley	30%
Manohari Moodley	30%
Sereshen Moodley	40%
Total	100%

Investment project
The RCF subordinated loan will receive a 3% RBTIRR plus a bullet payment in 2017 to achieve 7% RBTIRR. The Risk Premium is 1.54% and the Development Premium is 1.00%

Financing framework
MXM approached IDC because they offered a better deal than the banks since they did not require any collateral
The financing framework is shown below:

Source of Funding	**R'000**	**%**
Retained Income	**805**	
Member's Loans	**0**	
Depreciation	2,001	
Member's Contribution	2,807	19%
	9,200	
IDC Proposed Normal Loan-Port A	**8,200**	**55%**
IDC-Proposed Normal Loan-Port B	1,000	7%
RCF –Proposed Subordinated Loan	**3,000**	**20%**
	15,007	**100%**

Issues and lessons learnt

The Industry is still white dominated and there is a need to open up the space for smaller SMMEs. Going forward the government should prioritise empowerment in the steel manufacturing industry. The government also needs to encourage and empower Research and Development. Other government parastatal such as Transnet and Eskom could also come in through offering various opportunities for newly formed steel manufacturing industries and also offer market opportunities for newly developed products.

MXM should be commended for its effective worker retention strategies. The company has a 100% retention rate. For example the production manager at Grid Fast was trained on the job but is successfully running the department.

IDC needs to carry out a publicity drive to ensure that companies are aware of their products. In the case of MXM the organisation was not informed upfront that RCF2 was funding the business.

Primolitos

Date: 11th October 2013

Persons attending: Roberto Vasconcelos
Daniel Chiwandamira

General Information
The Primolitos Group (Primolitos) was established in 1994. Primolitos is currently an established supplier of a wide variety of food products including sauces, baking products, spices, convenience foods and sachets as well as a limited range of beverages. The Primolitos Operating Group (Primo) consists of the following groups:

- Primolitos Limited(Primopco)-A public unlisted company that is being registered(currently) Primolitos CC-the primary manufacturing and holding entity;
- Portion Control Packers (PTY) Limited –A manufacturing entity producing small food portions(dry and liquid) in sachets or tubs; and
- The Primolitos Property Group-Consists of various companies.

The company currently supplies the local Food Services Sector (FSS) segment which accounts for 90% of the company's turnover. They have a wide range of clientele which includes the following:

- Catering entities;
- Large Institutions;
- Bakeries;
- Leisure Market;
- Cash and Carry Segments; and
- Retail Segment.

Between 2006 and 2007, Makro asked Primolitos to expand its facility to comply with the new health standards. The expansion was a major leap for the organisation and proponents such as Massmart (now a subsidiary of Walmart) required the company to build premises which were compliant to international standards. However since the expansion, the company has encountered several difficulties. These are listed below:

- There has been a dip in profits post 2010 World Cup and the company has struggled to pay back the IDC loan;
- Primolitos competitors offer a lower price scale and do not adhere to many regulations which keeps their prices lower;
- Expected business has not materialised as quickly thought. The traditional focus of the business has been food services and some of the clients have either reduced their capacity or shut down. In 2012 the company thus had ZAR 10.5 million in debts. Primolitos has been put into a risk containment unit but they have not been harsh though there is a court date in MAY 2014;and
- The company has an experienced management team and has a strong record technical and marketing department. The company also employs Previously Disadvantaged Individuals (PDIs). However the company has an urgent need for financial skills. The Employees through the Grey Shares Trust have a share of 32% in the organisation. The company's shareholding is as follows:

Entry in market

The Food and Beverage market is diverse and is segmented into the following: Cash and Carry, Food Services and the Retail. The size of the market is estimated at R16 billion in 2008 and the market is expected to grow at not less than 3% per annum. Currently Primotilos occupies a relatively small market share in the target segments.

Investment

IDC co-investment is through Preference shares. The RCF subordinated loan will receive a minimum IRR of 5% IRR +upside based on 5% of increase in market value.

Financing

The company will be financed as follows;

Description	Lender	Borrower	R50 200 000
Plant and Equipment	IDC	Primopco	R35 040 000
Working Capital	IDC	Primopco	R 3 960 000
Preference Shares	RCF	PET	R 11 200 000
Total Exposure			R 50 200 00
Related Party			
Exposure			
Business Partner			R0

Lessons Learnt

There are several lessons that could be gleaned. These are briefly explained below: The envisaged expansion should be thoroughly and critically assessed during due diligence process.

- Teams should endeavour to attach realistic values to companies by ensuring that conservative assumptions are made when valuations are completed. In many instances overpayment for shareholding has led to inability to repay IDC funding
- There is a need to ensure that Workers Empowerment Trusts are solid and the perceived benefits are clearly articulated to the intended beneficiaries. With the case of Primolitos the workers are supposed to be empowered through rising through the ranks in the business based on performance. Despite workers owning 32% of the business the workers still go on strike;
- There is a real need for the government to relook at the issue of subsidies. With regards to Primolitos the subsidies did not seem to achieve the desired results; and
- Bigger firms are comparatively at a better advantage in terms of dictating supplier prices and this puts SMEs at a disadvantage. An option is for the SMEs to buy at factory shops at discount prices so as to lower their producer prices.

Expected Results

Primolitos is expected to generate 115 new permanent employment opportunities at an average capital cost of R403 512 per employee. In addition Primolitos acquires its raw materials locally thus boosting the local agricultural industry.

Final Evaluation of the EC-funded Private Sector Support Programme titled "Support to the Risk Capital Facility 2" – SA/21.031700-05-01

December 2013

ANSWERS TO COMMENTS ON THE DRAFT FINAL REPORT

Executive Summary

Page No.	Comment	Action taken
11	Seven categories of results were expected, in terms of enterprises supported, in terms of job created, with at least 30 % female employment, with a regional bias towards the poorer regions, a sector wide dispersion, at an interest rate of return (IRR), which allowed for the maintenance of the nominal value of the Facility over the duration of the programme. **EU Comment** Please also include the result relating to HDP empowerment.	The section has been revised to include reference to HDP empowerment.
12	Since its inception, RCF has supported a total of 82 investees including 13 write offs and two (2) exitsin the direct channel. This total figure also includes the 3 active niche funds as well as the one that was exited. Over and above this, the Niche Funds have invested in 10 SMEs that are RCF compliant. **IDC Comment** This figure includes 7 full cancellations	Figures have been revised according to the following breakdown: Active -63 Exits-3(2 Direct Channel and 1 Niche Fund Write Offs-13
	Since its inception, RCF has supported a total of 82 investees including 13 write offs and two (2) exitsin the direct channel. This total figure also includes the 3 active niche funds as well as the one that was exited. Over	Removed the Niche Funds from the grand total.

	and above this, the Niche Funds have invested in 10 SMEs that are RCF compliant. **IDC Comment** The 82 does not include Niche Funds since they are not counted as SMEs. Also, there is not Niche Fund that has ever been exited. One Niche Fund was cancelled.	
	Since its inception, RCF has supported a total of 82 investees including 13 write offs and two (2) exitsin the direct channel. This total figure also includes the 3 active niche funds as well as the one that was exited. Over and above this, the Niche Funds have invested in 10 SMEs that are RCF compliant. **IDC Comment** These 10 SMEs are already included in the 82. 82 comprises 72 SMEs through the DIC and 10 through the NFC.	Comment noted.
	Since its inception, RCF has supported a total of 82 investees including 13 write offs and two (2) exitsin the direct channel. This total figure also includes the 3 active niche funds as well as the one that was exited. Over and above this, the Niche Funds have invested in 10 SMEs that are RCF compliant. **IDC Comment** These are jobs facilitated only through the DIC (net of cancellations). Kindly note that for consistency, if you include cancelled SMEs above, then the total jobs would have to include cancelled jobs. Otherwise all figures should be net of cancellations, which I think is more appropriate. Including the RCF compliant transactions through the NFC the total number is 6 369 (net of cancellations)	The report has not included cancellations in any of the calculations. Total number of jobs created has been amended in the report and the figure supplied by IDC of 6369 (net of cancellations) jobs has been used throughout in the final report.
	Since its inception, RCF has supported a total of 82 investees including 13 write offs and two (2) exitsin the direct channel. This total figure also includes the 3 active niche funds as well as the one that was exited. Over and above this, the Niche Funds have invested in 10 SMEs that are RCF compliant. **IDC Comment** Cleardata and Massiv TV have struggled to achieve this requirement was post the 12 months.	This information has been included in the main text.

12	It is important for RCF to follow up the HDP empowerment annually to see whether or not there are any changes. **EIB comment** Please note that in the specific cases where EIB provided its approval on the condition that there is an acceptable plan in place for the proposed investee to achieve 25.1% HDP ownership within one year from investment (as per the provisions of the Investment Guidelines), EIB followed-up with IDC on the satisfaction of this condition.	Noted.
13	The evaluators were not able to obtain from the IDC the ZAR equivalent of the amount set aside for BSS. **EIB comment** For information purpose, BSS presentation made during Feb 2012 PSC may be helpful in this regard (see PSC minutes, item 11- revised KPIs)	Text has been revised based on the 2nd amendment to the RCF2 IDC EIB MOA which stated that an exchange rate of Euro1=ZAR9 would be used.
13	**EU Comment** **Result 6** (Table 1) - Propose to include a comment here regarding the investment that was made by RCF in an SME in Angola, despite the fact that the SME is currently facing challenges. For accuracy, please include the issue in this section.	Comment about the SME that had operations in Angola has been added to the table.
13	The log frame states that progress against plans would be measured yearly, however, this has not been done. **EIB comment** See minutes of Feb 2012 PSC, item 5.1. The decision was taken that PIMD will develop a template, thus solving the two key issues identified by IDC-EIB, namely: - who is in charge of monitoring HIV plans? and on which basis?	Still the mission noted that this was not done annually for all investees and a comment has been added to acknowledge the decision of the Feb 2012 PSC meeting on this point.
14	It seems that the opportunity to entrust the management of the RCF to a private party was not considered at the time. With hindsight, it seems that a private party could also have managed such a facility efficiently; however, this would not have resulted in the indirect impact capacity building at IDC level described thereafter. **EU Comment**	This point has been noted and text revised accordingly.

	(IDC as the Implementing Agency): Please note that RCF2 being a budget support entity, its management could only be entrusted to a public entity according to EU procedures.	
15	The limited numbers of investees (however within target) supported is mostly due to the unsuccessful Third Party channel process which did not meet the private financial sector's requirements for an effective cooperation, mostly linked to the burdensome investees' assessment process, IDC perception as a competitor, as well as some lack of interest on the part of the large banks for the limited amount of the Facility (this last argument would not apply to the smaller financial institutions which could have been approached further to the mid-term review recommendations). **IDC Comment** But the MTR's recommendation was to abandon the TPC and utilise its allocation between the NFC and DIC. Actually the revision of the allocations as evidenced in the addendum to the IDC/EIB MOA was informed by the MTR's recommendation.	Disagree with the comments. It was suggested in the MTR that IDC targets smaller SMEs in the Direct channel, that Khula would be used as a channel and some smaller financial institutions be approached for cooperation.
	Because of this slow deal flow, the Facility amount is still not fully committed (78% committed as of end of June 2013) and the reflows have not been reinvested; neither RCF 1 nor RCF 2 are yet revolving. **IDC Comment** Might need to elaborate that the 78% is based on the increased Fund size as compared to the 93% when considering the original fund size estimate of R423 million.	Suggested text added as a footnote.
	The funds have been leveraged up to about 300%, much in excess of the initially expected 100%. In that respect, RCF was effectively catalytic towards the financial support granted by IDCs to the investees as well as towards the niche funds developments through an increased visibility to raise other parties' investments. **IDC Comment** In excess of	Correction done.
15	It is regretted that it was not able despite its efforts i) to help improve the Third Party channel process, to make it acceptable to commercial financial	Efforts by the EIB to help in this regard have been noted and this is what the evaluators were referring to previously. The EIB effort in

	institutions and ii) that it could not ensure, that a global portfolio review be conducted yearly to monitor more clearly and accurately the financial and socio economic results of the Facility. **EIB comment** For record purpose, EIB respective efforts are summarised below. - *Third Party Channel* During Q1/Q2 of 2008 the RCF SBU was actively involved in negotiating framework contracts with potential Third Party Channel (TPC) intermediaries. There, the EIB regularly provided its review, assessment and recommendations on the status of the discussions. The Bank has in the past promoted a deal-by-deal approach and has particularly encouraged a potential transaction with Business Partners, which unfortunately did not come to fruition. In line with the provisions of the Investment Guidelines, the EIB has then continued to provide its input in the advancement of the TPC, in particular in light of the expected restructuring of the TPC following MTR recommendations, when RCF engage negotiations with Khula regarding a potential co-operation. - *Global portfolio review conducted to monitor more clearly/accurately the Facility* As per FA/TAPs/Annex2/Activity 5.4, it was a requirement that "*each client is visited and monitored annually. The output will be a monitoring report covering the performance in all relevant areas"*. Please note that EIB did not have the opportunity to provide inputs at the occasion of the 1st Annual Survey carried out in 2009/2010. According to MTR recommendations and in light of the shortcomings identified further to the first Annual Survey, EIB proposed to review together with IDC Terms of Reference for the second Annual Survey completed in 2010/2011 in order to address i.e. issues related to the scope (e.g. BSS and E&S aspects to be covered, provide a more in depth financial review, visit RCF eligible SMEs under NFC) and the methodology used by the consultant (ensure for instance that the way data was collected was aligned with RCF reporting requirements).	this regard have been better highlighted in the report page…
15 - 16	The limited numbers of investees (however within target) supported is mostly due to cancellations and the unsuccessful Third Party channel process	Text revised to include reference to cancellations and the fact that these were sometimes outside the control of the fund. Results of the analysis done by EIB on the performance of the fund excluding

	EIB comment As of end 2011, there were actually two factors (with same weigh) explaining why commitments were below targets, namely: absence of TPC transactions and cancellations. The importance of this second factor (to some extent beyond RCF control) shall certainly be mentioned here as well. Also, looking at the performance channel by channel before cancellation, DC and TPC were on track compared to their respective targets. (see EIB presentation to Feb 2012 PSC)	cancellations has also been included.
16	Most of the other IDC managed Funds similar to RCF but with different targets do not face such stringent conditionalities in respect of the potential beneficiaries. **EU Comment** Please could you elaborate a bit on how the other funds are different (less stringent) than RCF. This is useful for us in considering any future SME programme.	Not all other funds managed by IDC have BEE components, or minimum job creation or equity or quasi equity instruments while their cost is often lower.
16	The Niche Fund channel however is managed directly by the RCF team which relies on IDC expertise as far as participation to the Credit Committees is concerned. **IDC Comment** The NFC structure do not always allow IDC participation in credit committees but rather in Advisory Committees/Boards, e.g. in Limited Partnership structure. Of the 3 Niche Funds, only Utho is structured such that IDC sits in the Investment Committee	Paragraph amended to reflect comment.
16	from 2011, **EIB comment** 2011 was definitely an important year with respect to the paradigm shift, although *"systematically"* would seem too strong (unless the reference year is 2012?) since some EIB approvals in Q4 2011 were still given on the condition that the IDC provide an acceptable Support Needs Report (SNR) – i.e. the latter was not done ex ante during the due diligence.	Be it end of 2011 or beginning of 2012 does not change the picture.
16	The effective financial instruments used were mostly long-term subordinated loans whose interest and principal repayments were linked to the availability of sufficient cash flow, with grace period, including a	Disagree with comments. While the financial instruments used achieved their purpose as it is said in the report, they did not provide equity or quasi equity type of finance. Repayment of the

	variable remuneration with an uncapped upside, and repayments being pushed back to the end of the loan duration should they not be able to be serviced. **EIB comment** Please note that we disagree with this assessment. In the case of RCF, subordinated loans can be categorised as "quasi-equity" after taking into consideration the following features: maturity, grace period, subordination variable component, uncapped upside. (if a company were to be exceptionally successful RCF would fully participate in this upside without limitations). See wording 4 paragraphs below confirming that commercial banks are rarely co-financing with RCF. Hence the subordination to IDC only is not fully relevant. While in practice, these loans did not provide a similar support as real equity, they achieved the intended quasi-equity support.	loans has to come when ever from the company's own financial resources and not from outside the enterprise (equity), draining its finance. The real equity does not have to be paid back from the enterprise's financial resources.
17	a) Workers' Trust share financing, often for significant amount of equity, through long term loans to be repaid from "investees" dividend. The few cases assessed by the evaluators showed no "real" BEE results, since the workers would not realise <u>in the best of cases</u> any income for the following ten or fifteen years. The real justification without any HDP management effective commitments, devised by the promoters of the project to obtain unsustainable financial support. **EIB comments** We disagree with this general assessment, all the more as only "few cases" were assessed. Please note that instruments used in financing SMEs with WT do not differ from SMEs without WT, RCF instrument having similar equity/quasi-equity features in both cases (until end 2011, most WT were actually based on shareholders loan or preference shares). Hence, we disagree with the assessment that when RCF investments supported a WT it increased the leverage of the SME. If so, this would imply that all RCF operations increased leverage, instead of providing quasi-equity. Meanwhile, we fully appreciate that some entrepreneurs might have tried to take advantage of the presence of a WT (but not in terms of leverage). As per the BBBEE code, and in line with RCF agreements (FA, MoU), WT have been identified as an appropriate tool to promote BBBEE, and the	Workers schemes reviewed by the mission were flawed and did not achieve the objectives of the RCF in terms of effective BEE shareholding or management. It is recognised that « reasonable » Workers trust support could be beneficial, but based on mission findings, such Workers' trust approach should be re-examined to avoid abuse.

	issue - not only for RCF but for IDC in general - seems to lie more in the implementation of WT schemes (e.g. absence of follow up and lack of provision of BSS), which needs indeed to be reviewed as recognised by IDC SED team (see PSC discussions further to IDC SED presentation on WT during August 2011 PSC).	
18	The indirect impact is even more significant at the IDC level, whereby from a single RCF development facility ten years ago, the IDC now manages thirteen different Funds structured on the RCF model, managing ZAR 17 billion provided by IDC and other partners (as against about ZAR 500 million just for RCF). **IDC Comment** This amount excludes RCF1	Corrected and now specifies that the amount is for RCF2.
18	- Development finance targeting small and medium size enterprises with high risk, a number of them at the start-up phase, cannot be effectively supported by equity instruments **EIB comment** Please note that we disagree with this assessment. In the case of RCF subordinated loans can be categorised as "quasi-equity" after taking into consideration the following features: maturity, grace period, subordination variable component, uncapped upside. (if a company were to be exceptionally successful RCF would fully participate in this upside without limitations) Thus, self-liquidating instruments with long grace periods have been preferred, often with a variable remuneration component and other equity features providing potential "upside" so as to compensate the RCF for its risk taking. The base pricing is often linked to Prime, providing a minimum level of real IRR which is generally boosted by an additional share in revenues/profits. RCF's approach is in line with other private equity funds focusing on SMEs (e.g. Enablis Entrepreneurial) which use self liquidative quasi-equity instruments in particular for liquidity reasons at exit. The EIB has continuously supported RCF's move towards more equity related financial instruments, for instance (i) by ensuring that maturity and grace periods of RCF subordinated are longer than IDC senior loan's ones, or (ii) by inviting IDC to restructure instruments initially priced at a	We maintain our analysis in as much as promoters without financial means cannot fund their expansion on equity support without losing most of their controlling shareholding, except for special case of high growth potential start-ups ; this has been included in the report. The solution devised through subordinated loans with flexible repayment terms based on cash flow availability did meet the needs of most SMEs reviewed, pushing back to the future the time for possible real equity financing.

	high fixed capped return into instruments with a lower fixed return plus an uncapped upside. Besides, the EIB repeatedly emphasized the need to structure the “upside” in an enforceable manner over the past four years, in line with MTR recommendations.	
18	- Programme should ensure that real socio and economic performance is assessed, deriving the real impact of the Programme so as to draw effective lessons learnt **EIB comment** EIB welcome this lesson learnt.	Noted.
19	- Guidelines should include some area of flexibility especially for the non-core covenants defining the size of the beneficiaries/projects and expected results **EIB comment** EIB concurs with this lesson learnt, as illustrated by IDC-EIB pragmatic approach in this regard,: - either through derogations on a case-by-case basis (as of end 2011 this concerned ca. 25% of DC and 50% of investment in Niche Funds: HDP ownership, size, cost per job, conflict of interest, job creation vs. job saving) - or through amendments to IDC-EIB Agreement. (see: cost per job, SME definition, conflict of interest, HIV, socio-cultural).	Noted.
20	Flexibility in the investment guidelines - Guidelines should include some area of flexibility especially for the non-core covenants defining the size of the beneficiaries/projects and expected results **IDC Comment** This is already the case	Slightly amended to take comment into consideration.
	Exit strategies should be addressed at the credit application level, not only from the cash flow of the enterprises, but also from other exit options, should the cash flow not match the expected returns, so as to prepare the parties on other possible options **IDC Comment** Not sure what this means. The exit strategy is always clear when the applications are submitted to the Credit Committees. Maybe the only weakness is that not more than one option is presented	This is what is meant, i.e. what happens if cash flow is not sufficient as far as exit is concerned.

22	- It is recommended that in future Programme support initiatives, EIB insists like for RCF on a rigorous monitoring of the investees, regular analysis of the portfolio and the assessment of the Programme impacts to ensure that lessons are drawn and mistakes avoided. **EIB comment** We believe that within the mandate entrusted to the EIB, we have reported as much as possible based on the tools/information made available to us. By definition the Annual Survey (referred to in FA/TAPs/Annex2/Activity 5.4) was performed once per year, i.e. actual information was updated on an annual basis. As a result, it was not possible to report more than once per year on the actual socio-economic indicators simply because it has never been envisaged that RCF will do so. Besides, the importance of the post monitoring to check on the social – economic results has all extensively and repeatedly been emphasized by the EIB. EIB has been inter alia actively involved with respect to monitoring and reporting on: HIV plans, WT, NFC performance, impairments, write-offs, exit etc. In its reporting to the PSC, according to its mandate the EIB gave a bird's eye view on the management, implementation and performance of RCF. For that purpose, the EIB developed its own independent database that tracked financial and non-financial indicators independently. The focus of EIB's reporting was not on descriptive or quantitative elements, but to perform a qualitative assessment and draw lessons. This included the following elements: - Report on certain areas not covered by the IDC in its own reporting: o review of Annual Surveys (highlighting assets/shortfalls and key conclusions) o focus on financial performance (RCF's risk profile based on approval/disbursements, analysis of reflows received vs. expected) o challenges of dealing with subsidiaries of large	Remarks point out to the need for a better portfolio reporting and more importantly a portfolio assessment and analysis, rather than to compile a list of individual investees' situations without drawing consequences for the RCF as a whole, in social and financial terms.

	group, and cancellations - Use raw data furnished by the IDC as a starting pointing to provide further analysis o determine concentration risk from both financial and development perspectives by geographies / sectors / key investees. o Peer comparison of NF performance from an RCF perspective - Put the activity of any specific quarter into the overall RCF context by comparing periods, showing evolutions and drawing trends. - Provide concrete feedback to PSC members through positive and negative lessons learnt o For example from approvals / site visits / annual surveys: RCF clear additionality, strong empowerment features, slow BS paradigm shift, lack of monitoring of HIV / upside payment / HDP ownership. As to the financial model, its necessity has been identified and its design has been supported by the EIB in connection with RCF. But, the financial model had some limits outside EIB control, e.g. absence of automatic comparisons between quarters and between cash flows received vs. cash flows expected. EIB made nevertheless the effort to extract this information manually investee-by-investee from the model to determine the percentage of return which is actually "pushed back" quarter-by-quarter (see slide EIB presentation to PSC, Quarterly Performance Review Q3-2011, III,3. Quarterly reflows). Bearing in mind that: (i) reporting by the EIB had been intended (see FA/TAPS/Annex 7) to be limited to macro-monitoring of	

	the portfolio, but in practice had to go beyond this aspect, especially to enhance its reporting on socio-economic and financial impact of the programme, as illustrated above, (ii) EIB analysis was limited by the tools / information at its disposal (such constraints being beyond its control), (iii) EIB reporting was performed in accordance with MTR recommendations (analysis of the evolution on portfolio basis by sector, concentration risk, sustainability concerns, due and delayed payments, etc.) we disagree that EIB could have insisted more on a more rigorous analysis of the RCF portfolio situation […]to ensure that lessons are drawn and mistakes are avoided. Within its own mandate (macro-monitoring), and according to MTR recommendations, lessons learnt have been especially continuously shared with PSC members by EIB (e.g. HIV plans, WT implementation, BSS paradigm shift, concentration risk, actual vs. target reflows). In other words, EIB did insist on the above, as outlined on page 78: "The EIB's intervention forced RCF to formalise more rigorously […] its reporting." Please see the EIB presentations at the PSC meetings as well as the EIB Annual Performance Review for evidence.	
24	Ensure the preparation of yearly work plans for RCF so as to have objectives against which to measure performance, assess deviation from the plan and suggest remedial actions. In such plans, SMEs could be categorised in line with the classification provided by the National Small Business Amendment Act of 2003 and 2004 (See Annex 7.1) thereby providing a further benchmark regarding the intended characteristics of the investees; **IDC Comment** All IDC units have to prepare annual strategy plans where most of these are discussed and measure at the next year's exercise. Is the point here to have this just for RCF?	This is the point, an annual work plan is recommended for RCF as such.
25	Main drawback for such SMEs' access to finance rests with their lack of transparency, detrimental to the financial institutions ability	Development Partners support should be financial but also promotional and analytical; this has been inserted in the report.

	to assess risk and therefore dispense with excessive collateral request. To improve such transparency, it is recommended to consider helping to provide a performance and credit rating service based on privately sourced due diligence review of SMEs which would outline the enterprises' strong and weak points, providing useful information not only to the enterprises' owner but mostly to the enterprises' bankers and other partners in the value chains. Similar scheme has been successfully developed in India by the National Small Industries Corporation[1] with the support of a number of private service providers in cooperation with the banks, having contracted more than 26,000 enterprises so far. As recommended above, such a scheme already under consideration by the dti must be assessed in full cooperation with the financial sector and credit rating providers. Such support could be coupled to Technical Assistance linked to the identified SMEs' weak points, including possible hands on monitoring/reporting by audit companies during the financial institution financing support. **EU Comment** **(SME Credit Rating Scheme):** Please clarify the possible type of support that would be needed from development partners in the setting up of such a scheme?	
26	the main support needed from the Development Partners being the grant support element to be blended to the commercial and public financial institutions financial lending. **EU Comment** **(Project Financing Scheme):** Please explain why the grant support would be needed in this case. If the contract is secured from the public entity and the DFI (e.g. IDC) is ready to finance the SME, why is the grant needed?	Have suggested that support from donors be used in the scoping study as well as in the initial structuring of the project finance scheme.

1. Introduction

[1] Cf. http://www.nsic.co.in/creditrating.asp

Section	Page No.	Comment	Action taken
1.4.3 – The Medium term review and ROM recommendations	43	Main recommendations implemented **EU Comment** **(The medium term review and ROM recommendations):** Please note that the recommendation on BSS was also implemented. It needs to be reflected accordingly in this section.	Text has been revised to include specific actions taken with regards to MTR and ROM recommendations on BSS.
Niche funds	43	- Niche funds are made aware of the importance of supporting investees with significant socio economic impact, however, a number of the investees, especially by Agri-Vie do not meet some of the BEE requirements[2]; **EIB comment** We do not know what the exact situation at Agrivie is at present, so this comment is more for information purpose. - RCF has always been aware that NF would not be in a position to invest only into RCF eligible investments. Hence, the covenant in all NFC transactions that at least e.g. 2.0x/3.0x RCF amount must be invested into RCF eligible SMEs (to ensure leverage). - If the current situation / pipeline for Agri-vie shows that the agreed leverage is/would not be met, the above statement will become a serious concern, but otherwise not.	Agrivie has one RCF compliant investee but this does not mean that the BEE conditionality will not be met in the future. Comment by EIB has been noted.
1.4.3 - Main recommendations not implemented	44	the fact that part of the RCF 1 reflows were assigned to another IDC fund points to a relatively lower priority for BEE SMEs and HDP employment support, relative to the aims of the other funds managed by DFD as well as to the difficulties in identifying	Paragraph maintained; it appears to the mission that the funds should still be used to support BEE SMEs via RCF as initially targeted… and that instead of channelling funds to another

[2] Seven of these investees not meeting the Social economic results are not counted as part of the RCF investees in RCF reporting

		worthwhile BEE businesses, especially in the poorer regions of the country **EU Comment** **(Main recommendations not implemented) – RCF1 and 2 not revolving**: I don't think it is an issue of low prioritisation of BEE SMEs and HDP employment by IDC. RCF1 reflows were assigned to another new fund due to an identified new area of support which was discussed and agreed at PSC level. This is more a positive than a negative. RCF is not yet revolving due to slower than expected deal flow for the various reasons mentioned in the document. I think this section should be amended accordingly. Also, IDC feedback on this point should be taken into account.	scheme, measures should be taken to increase the flows of potential businesses, especially through some review of the third party channel.
1.4.3 – Main Recommendations not implemented	44	Use RCF 1 and 2 reflows to ensure that the Funds are revolving; the fact that part of the RCF 1 reflows were assigned to another IDC fund points to a relatively lower priority for BEE SMEs and HDP employment support, relative to the aims of the other funds managed by DFD as well as to the difficulties in identifying worthwhile BEE businesses, especially in the poorer regions of the country **IDC Comment** TVC is not an IDC fund but rather a dti fund managed by IDC	OK, text amended.
MTR Recommendations	44	- Monitoring the socio economic results and the financial results on a portfolio basis to draw lessons in this respect, including more detailed analysis of HIV/AIDS and environment plan existence, satisfaction of investees with RCF process, quality of jobs created directly and indirectly and impact of “investments” per size of SMEs; **EIB comment** See EIB follow-up based on shortcomings of and conclusions from the 1st Annual Survey /site visits. - - Assessing rejected applications on a global basis to understand	Comment related to EIB’s follow up on annual survey has been noted. Acknowledged the fact that EIB encouraged a review of rejected applications in the context of the 2nd amendment to the IDC-EIB Agreement in 2011.

		main issues in this respect. **EIB comment** Please note that such a review was encouraged by EIB and carried out in the context of the 2nd amendment to the IDC-EIB Agreement in 2011.	

2. RCF Results and Outputs

Section	Page No.	Comment	Action taken
Key performance indicators relevance	46	- The RCF Programme should create 6000 new employment of which 30 % are to be held by women. These jobs should be created for HDPs; - **EIB comment** - We wonder what the basis for this statement is; it clearly appears that all RCF contracts are identifying these jobs only as HDP jobs The 6,000 target strictly refers to HDPs.	Deleted “as much as possible”.
2.2 - Other covenants introduced through the Annexe A Investment Guidelines of the EIB Agreement with IDC	47	Investment channels: Direct Channel should constitute 50 % of the portfolio by value but not exceed 60 %; Niche Fund Channel should constitute 30 % of the portfolio but not less than 25 %; Third Party Channel should constitute 20 % of the portfolio by value but not less than 15 %; **IDC Comment** This is before the addendum between IDC and EIB concluded in December 2011	Revised in accordance with the addendum.
2.3.1 – Result 1: Number of SMEs supported	48	Table 1: Number of Approvals and amounts per year in the Direct Channel as at end of June 2013 **IDC Comment**	The value includes cancellations because we are looking at total approvals.

		May need to reflect the cancellations on these tables as if one was to sum the total approvals, they actually exceed the fund size because they include investments that were cancelled	
2.3.1 – Result 1: Number of SMEs supported	48	445 438 974 **EU Comment** **(Table 4):** Please check the highlighted figure. It does not seem right and also does not agree with the total figure on Table 7. Appears too high because in total, RCF should have invested about R 416 million (net of cancellations /write offs / exits) in both the direct and niche fund channel, as at Sept 2013.	Table 4 has been changed and now shows the SMEs financed net of cancelations and the amounts invested per annum based on the IDC portfolio data. Please note that we have requested IDC to clarify the total number of SMEs financed as they have different figures in their reports. This will be amended once we obtain feedback from IDC.
2.3.1 – Result 1: Number of SMEs supported	52-53	**Error! Reference source not found.** shows investee spread across the provinces. The investment in poorer provinces was mainly driven by third party investors as opposed to individual entrepreneurs, which is indicative of the brain drain to more economically active provinces. **EU Comment** Who are third party investors? Please elaborate.	The third party investors refers to corporates or well established companies that invested in poorer provinces and partnered with HDPs, for example franchisees like Pick'nPay. This statement has been revised in the report.
Rejections	54	There have been twenty six (26) rejections in total and a majority of these were due to the following reasons: - RCF pricing impeded the viability of the transaction – 27 %; - Failure to submit information needed – 30 %; and - Failure to align to the objectives of RCF – 30 %. **EIB comment** Please note that such a review was encouraged by EIB and carried out in the context of the 2nd Amendment to the IDC-EIB in 2011. After IDC-EIB investigations and adjustments, the outcome was that HDP cost per job was the main constraint (ca.40%), followed by lack of economic viability (ca.20%), failure to submit information (ca.20%), pricing (ca. 10%), and others (SME size,	This information was extracted from IDC records on rejections.

		HDP, etc. ca. 10%). The percentage related to pricing (27%) appears therefore abnormally high (as we are not aware that since end 2011 RCF pricing terms have been increased or that other DFD funds pricings have been lowered).	
Cancellations	54	The reasons behind the full cancellations is that [3] or in some instances they failed to meet the conditions precedent. Partial cancellations arose from the fact that initially applicants sought funding for more than one project and ended up dropping some of the projects due to changes in the market conditions. **EIB comment** This assessment needs to be reviewed: as of end 2011, concerning full cancellations in the DC, none of the cancellations memos received by EIB mentioned this pricing reason (See: Besa, Mausberg, Naledi, Newco Shandon Quarry, P&P and Ninos).	As indicated in the footnote, this information was obtained during interviews with IDC staff. The team did not have sight of the cancellations memos and have deleted reference to pricing as one of the main reasons behind cancellations.
Results	55	per job not exceeding ZAR 100,000 on a deal by deal basis and ZAR 60,000 on a portfolio basis. **EIB comment** ZAR 300,000 as per the amended amount. ee 2nd Amendment to the IDC-EIB Agreement (19.12.2011) RCF is estimated to facilitate [**EIB comment**: this is not an actual figure but the expected job creation. Consistency throughout the document to be further checked. (in light of this paragraph and the table below	Corrected and revised the number of jobs created in line with new figures supplied by IDC and ensured consistency throughout the report.
2.3.2 – Result 2: Number of new jobs created	56	Table 2: RCF 2 number of jobs created end of August 2013 **IDC Comment** Shouldn't this be June	Corrected.
Result 7	63	The FA encouraged the investees to set up an environment and HIV/AIDS protection plan in accordance with the South African law in their entities. The 2010/11 RCF Client Assessment Report noted that generally larger investees have HIV/AIDS policies while the majority have no policies. The report found out that 6 investees have HIV/AIDS policies. It was also	Replaced "encouraged" with "required. The comment on the gap noted by EIB in following up HIV/Environmental plans is in agreement with our observation that there no visible initiatives to track this result.

[3] Discussions with the RCF Unit at the IDC

		established that companies with HIV/AIDS initiatives were excelling at policy formulation but lacked effective implementation of programmes due to cash flow challenges. Despite this finding, RCF does not require investees to have a formal policy but for the SMEs to have activities around HIV awareness and this seems to be the case. **EIB comment** This is actually a requirement as per FA/TAP Result 7 (p.7/) as amended after Rider 2 to the FA. The MTR noted that all investees had designed environmental/HIV interventions to raise awareness on these issues. However, there are no visible Monitoring and Evaluation initiatives put in place by the IDC for tracking this result. **EIB comment** Please note that it was part of EIB review at approval stage to receive confirmation about the existence / future existence of HIV/Environmental plans. As per Annual Surveys / site visits, a gap was however identified in terms of follow-up.	

3. Findings

Section	Page No.	Comment	Action taken
3.1.3 – Project Stricture - IDC as a the executive authority	67	the Small Enterprise Finance Agency (SEFA), (which integrated Khula and SAMAF) being a subsidiary of IDC since 2011. **EU Comment** **(on SEFA):** Please check the year - whether it is 2011 or 2012. I think that SEFA came into operation in April 2012.	Error corrected, SEFA was established in 2012.
Niche fund impact	71	The leverage of the EU funds however was somehow artificial since most of the investors in the Funds supported were public Development Financial Institutions (DFIs). Also it appears that in a number of cases, these Funds' investees have not yet met the socio economic covenants required in terms of social economic results, especially regarding female shareholding and HDP ownership. There are plans in place to achieve the targets and according to Agri-Vie; it was unrealistic to assume that the development indicators would be achieved in less than one year of the investments as it takes time to reach the targets.	Agreed; however it would have been better to leverage the funds with private investors joining in. Report amended to take comment into consideration.

		EIB comments The definition of the RCF leverage has never been restricted to private sector. If this would have been the case then few operations in the DC would have met the leverage / co-financing criterion since IDC was typically the major co-financier. Because RCF has a strong development focus, it is normal that NF into which RCF invested also attracted other DFIs interested in E&S impact too (while private investors focus on high financial return). See discussions held during Nov 2013 PSC.	
3.1.3 – Project Structure – Third Party Channel	73	These proposals did not materialise, **since IDC was apparently not prepared to simplify its risk assessment process for smaller "investments"** and that Khula faced a significant reorganisation, being finally merged within the Small Enterprise Finance Agency (SEFA). The fact that SEFA is now a subsidiary of IDC should allow efficient assessment of risks at the SEFA level. **IDC Comment** Not sure where this comes from	This comment was taken from the MTR on page 63. The evaluators were not able to provide evidence in support of the obsevation. Comment has been removed.
EIB	77	The involvement of EIB increased the duration of the credit application process, estimated on average at 30 days by the EIB which is considered acceptable by the mission. **EIB comment** As per EIB record, the average was 30 over the period 2007-2011, reducing to a minimum of 23 days in 2011 thanks to continuous joint IDC-EIB efforts to streamline approval process. (e.g. enhanced cover sheet, ex ante discussions, etc.)	Duly noted, report amended.
	79	It is regretted that no significant assessment of this issue has been conducted at the portfolio level **EIB comment** Please note that at the time discussions about the design of the financial model, unfortunately the Corporate and Structured Finance Department in charge of developing the model on behalf of RCF indicated that aspect was not easy to reflect in the model, thus limiting the possibility of its assessment. Although the principle has been reported as a lesson learnt to PSC.	This point is not about incorporating such issues into the model, but rather to know about the issue and address it in time.

3.2.2 - Delays in implementation, underutilisation of funds, absorption capacity, marketing of RCF products	80	As pointed out in the Mid Term Review[4], RCF 2 experienced a two year implementation delay **EU Comment** **(comment on two-year delay of RCF2)**: The delay was one year and not two years, since the Financing Agreement was signed by the Commission in Dec 2005, by the SA government in Feb 2006 and the first tranche was disbursed by the EC in Dec 2006. By the time of the EC disbursement, the other underlying MoAs/MOUs had been finalised.	The RCF2 MTR page 42 states "that there was a "two year implementation delay which arose from a one year delay in setting up the various contract agreements between the parties to the scheme. A further one year delay arose from the slower commitments and disbursements of funds compared to the initial planning" Both EUD's and the MTR's statements are correct. Delay referred to by the EUD was related to the EC disbursement but beyond this there was an additional one year delay in terms of slow commitments and disbursements.
		It was thus suggested that, in future guidelines and conditions should be kept at a minimum as this had a negative impact on intended outcomes as few investees can meet all the requirements **EU Comment** Please could you give an indication of what guidelines/conditions could be done away with? This ties in with an earlier comment asking how different (stringent) is RCF compared to other IDC funds. This is useful information.	The mission is of the opinion that the investment guidelines are well defined and meet their requirement as mentioned page 70. Text has been amended here to reflect these views
3.2.4 - Jobs created, HDP employed and empowered, HDP share ownership increased	82	It is important to note that some of the investees have not yet reached peak operating levels and it remains to be seen whether they will be able to create the promised number of jobs, empower HDPs or increase the HDP share ownership. However, their applications indicated that they had plans in place to achieve their developmental targets. The use of Workers' Trust in some of the investees was supposed to be a key route to increasing HDP share ownership but it is not clear as to their level of involvement in management. This issue is further discussed in Chapter 5. The review also noted with concern current low rates of HDP ownership among women. **EU Comment**	The statement has been deleted.

[4] Mid Term Evaluation of the EC-funded Private Sector Support Program Support to the Risk Capital Facility 2-SA/21.031700-05-01

		This statement does not seem consistent with the earlier analysis and Figure 9 on pg 59 which indicate that the challenges lie in women HDP involvement in management and in women participation in training. Ownership and job creation appear to be on track. Please check and amend accordingly.	
Pricing	87	The pricing levels and structure were amended over the years to address the above issues. Global interest rate was reduced to a gross IRR of 10 %p.a. [**EIB comment**: in this regard it would be helpful to refer to PSC discussion about RCF tax exemption status] with half of the interest structured as an upside based on a percentage of the profit or turnover, computed as per the budget, after EIB continuous push for the increase of the upside portion in the remuneration with a much lower minimum IRR, to be tailor-made on a case-by-case basis. It was recognised that such IRR should allow the Fund to maintain its nominal value over time. **EIB comment** Please note that EIB has supported a pricing approach to be as much as possible specific to the investee particular situation, rather than a one-size fit all pricing mechanism. The mission confirms that the pricing structures used met the requirements of the project, keeping it simple and affordable, while maintaining the value of the fund. **EIB comment** EIB has pushed for the inclusion of an upside component (linked to the cash flow or the value of the enterprise itself), and this was part and parcel of EIB approval process to ensure that an uncapped remuneration is included in the pricing. Between 2007 and 2011, cases were remuneration was capped have been the exception.	Duly recognised, EIB's involvement in this regard has been mentioned in the report
Effectiveness	88	. The few cases when the BEE shareholding cum management were not met, orfailed, like for some Workers' Trusts (e.g. Amathole Berries and Primolitos). **EIB comment** See other examples of WT: Mosplass , Berekesama, Winsharp. The latter one was visited by EIB/IDC/EC in Feb 2012 and did not appear to be a failure.	Slightly amended to reflect the special cases reviewed.
3.3.1 – Project Steering Committee	89	Finally, it is regretted that the PSC did not insist to have a better global view of the RCF performance in terms of social development	Still we maintain that the PSC could be more demanding in ensuring that the results (social and financial) are better assessed, especially on

(PSC)		impact as well as the financial position of the fund globally at least on a yearly basis, based on a thorough analysis of the portfolio which was only concluded in May 2010/11. **IDC Comment** Our view is that the PSC members are satisfied with the reporting, but improvements on the reporting are constantly effected	a portfolio basis.
PSC	89	o Finally, it is regretted that the PSC did not insist to have a better global view of the RCF actual performance in terms of social development impact as well as the actual financial position of the fund globally at least on a yearly basis, based on a thorough analysis of the portfolio which was only concluded in May 2010/11. **EIB comment** As per FA/TAPs/Annex2/Activity 5.4, it is a requirement that "each client is visited and monitored annually. The output will be a monitoring report covering the performance in all relevant areas". Please note that EIB did not have the opportunity to provide inputs at the occasion of the 1st Annual Survey carried out in 2009/2010. According to MTR recommendations and in light of the shortcomings identified further to the first Annual Survey, EIB proposed to review together with IDC Terms of Reference for the second Annual Survey completed in 2010/2011 in order to address i.e. issues related to the scope (e.g. BSS and E&S aspects to be covered, provide a more in depth financial review, visit RCF eligible SMEs under NFC) and the methodology used by the consultant (ensure for instance that the way data was collected was aligned with RCF reporting requirements).	Duly noted; EIB's involvement mentioned in the report.
3.3.2 – IDC Management of the programme	90	IDC's effective management of the RCF financing was not always as professional as it could have been, even if the RCF supported enterprises were of a high risk nature. **IDC Comment**	Agreed… We changed word to effectiveness… We fully appreciate that it is always easy to point to a different risk appreciation a few years later.

		Not sure if this is a matter of unprofessional conduct or the management of the Facility is not as effective as can be.	
EIB involvement	93	➢ Reporting by the EIB about the project progress through its yearly reporting was comprehensive. Unfortunately it was not possible for the EIB, based on information/tools available to assess the value of the payments relegated to the end of the loan duration when "investees" cash flow was not sufficient. **EIB comment** We believe that within the mandate entrusted to the EIB, we have reported as much as possible based on the tools/information made available to us. By definition the Annual Survey (referred to in FA/TAPs/Annex2/Activity 5.4) was performed once per year, i.e. actual information was updated on an annual basis. As a result, it was not possible to report on actual socio-economic indicators "at any one time" simply because it has never been envisaged that RCF will do so. Besides, the importance of the post monitoring to check on the social – economic results has all extensively and repeatedly been emphasized by the EIB. EIB has been inter alia actively involved with respect to: monitoring of HIV plans, implementation of and support to WT, joint design of template document to enhance reporting on the NFC, inclusion of more detailed information on impairments, provision of actual figures when exit/write-off, etc. As to the financial model, its necessity has been identified and its design has been supported by the EIB in connection with RCF. In particular, the following features have been added upon EIB suggestion: o Split the line "reflow" into four lines: capital, interest, upside, bullet. o Be able to track IRR performance by channel by channel.	Has been added in the report that EIB did recommend a number of adjustments which would have improved the reporting, but which have not been taken into consideration so far.

		o More detailed output information on investees impaired / written off (by number/volume based on approvals/disbursements) o Possibility to enter various tax exemption Noteworthy, EIB requested that the following items were also taken into consideration: o Compare automatically on a quarterly basis cash flows received vs. expected in terms of capital, interest, bullet (to reach minimum IRR), upside (uncapped variable remuneration) and balloon (amount pushed back) o Explain the evolution of the IRR between two quarters through: deals added / deals written-offs / reflows. ->Unfortunately, the Corporate and Structured Finance Department in charge of developing the model on behalf of RCF indicated at that time that these two could not be easily added to the model. o In the model cash flows expected to be received in the future are those forecasted at the time of approval. -> Neither the IDC nor the Annual Survey's consultant recalculated future cash flows based on updated information on the performance of the investee companies. Because the comparison between quarterly reflows expected to be received from investees and actual payments to RCF that investees made was not provided automatically through an output table/chart by the model, it had to be extracted manually investee-by-investee from the model to determine the percentage of return which is actually "pushed back" quarter-by-quarter (see slide EIB presentation to PSC, Quarterly Performance Review Q3-2011, III,3. Quarterly reflows).	

		Bearing in mind that monitoring by the EIB had been intended (see FA/TAPS/Annex 7) to be limited to macro-monitoring of the portfolio, but in practice had to go beyond this aspect, especially to enhance its reporting on socio-economic and financial impact of the programme, as illustrated above, we disagree with the assessment that EIB reporting was "weak" regarding the two aforementioned points.	
EIB involvement	93	It is regretted that the management fee of the EIB was fixed as a monthly amount regardless of the results of the Fund or of its involvement. It did not incorporate success incentives, which could have taken various forms, at the socio economic level, at the financial level or at the Third Party channel level, or a combination of those. **EIB comment** The EIB disagrees with this assessment. As a public policy driven bank the EIB is by definition incentivized by aspects beyond profits. In light of the EIB-EC relationship, the EIB has a long-term incentive for the good completion of its contribution to the project. Similarly, the EIB is exposed to reputational risk, which acts as an incentive to deliver on the EC - EIB agreement. The EIB also disagrees with the various forms of success incentives proposal for a number of reasons: (i) the EIB is not a party to the IDC finance contracts with the underlying SME investees. To link its remuneration at the financial level would imply EIB involvement in the identification, due diligence, structuring, contract negotiation, monitoring, exit support, etc. This would duplicate the efforts undertaken by the IDC and in turn would imply a very different modus operandi, with a different set of EIB ToR, and a much larger EIB team; i.e. this would imply a highly inefficient process; (ii) furthermore, under the current EIB ToR linking the Bank's	Mission still maintains its comments which try to harness human nature with incentives linked to results, socials and financials.

		remuneration to the developmental / financial performance of the portfolio clearly undermines the independence of the Bank's views and opinions by setting an incentive to maximise fees (or minimise the loss of fees) rather than providing independent expertise and candid feedback such that the Programme delivers an "optimal balance between financial and developmental goals". (FA/TAP/Annex 7); (iii) lastly, such approach could create a bias against seeking the type of risk that the Programme targets for development reasons, i.e. HDP-owned SMEs that are highly risky and otherwise would not attract funding from the commercial banking sector. The proposed incentive could in fact impair the desired development impact of the Programme by drawing funds away from the most deserving (but riskiest) SMEs. In light of the above observations the EIB proposes to delete this paragraph.	
Flexibility in the investment guidelines	104	some flexibility has been introduced on a limited number of criteria. Because all special cases can never be identified in advance, the PSC should have had the power to waive some of the requirements, on a case by case basis, under duly justified arguments. **EIB Comment** At their level (i.e. when there was no conflict with the Financing Agreement), IDC-EIB adopted such pragmatic approach: - either through derogations on a case-by-case basis (as of end 2011 this concerned ca. 25% of DC and 50% of investment in Niche Funds: HDP ownership, size, cost per job, conflict of interest, job creation vs. job saving) - or through amendments to IDC-EIB Agreement. (see: cost per job, SME definition, conflict of interest, HIV, socio-cultural).	Flexibility support by the EIB has been mentioned in the report.
Flexibility in the investment guidelines	104	and possibly in the case of developmental Micro Finance Institutions, the potential job creation at the end beneficiary levels. This in fact excluded MFIs from being targeted under RCF.	It has been reported to the mission by a PSC member that the indirect job creation induced by the investee has not be taken into consideration, which would be the case of the MFIs' clients job

		EIB comment Please explain why the potential job creation at the end beneficiary levels of MFIs would not be taken into account? With respect to RCF job creation counting methodology, it has been based on IDC comprehensive one. Besides, when appropriate, RCF has taken into account jobs saved and indirect jobs (e.g. Movini, Aristopix).	creation
Catalytic impact	107	, a specific analytical paragraph should be inserted in each credit application in addition to the "cost" per job created information. **EIB comment** In addition to the IDC application to its credit committee, RCF also attached a cover sheet when submitting an approval request to EIB. Please note that RCF additionality was captured on this cover sheet.	The statement has been revised to acknowledge the fact that RCF submitted a separate cover sheet to EIB addressing additionality during the credit application process. It is recommended that a specific analytical paragraph on RCF additionality now be included on the credit application as EIB is no longer involved.

6. Recommendations

Section	Page No.	Comment	Action taken
6.1.3 - Recommendations to the EIB	109-110	Because the EIB is involved with the support of SME access to finance through long term credit facilities granted to commercial banks in developing countries, it should be in a good position to support blending EU grants and development finance instruments such as RCF alongside its facilities to commercial banks, to ensure a wider outreach for programmes similar to RCF; in this respect, the mandate of EIB regarding RCF could have been enlarged to encompass the development of the Third Party Channel through the beneficiaries of its[5] long term SME credit lines **EU Comment** **(Recommendations to the EIB):** Is this a recommendation on possible future support to SMMEs? Should it not be included in the recommendations for possible future support to SMMEs since you are referring to how EU grants could be utilised alongside EIB credit lines and instruments such as RCF?	A comment in this respect has been added to the "Project finance support through the value chain approach" .
Recommendations to EIB	109	➢ While the contribution of EIB to the RCF support is widely	This is not intended to deny the good work provided by EIB.

[5] Or other DFIs SME wholesale credit lines made available to South African banks

		recognised and appreciated,. **EIB comment** We suggest deleting this recommendation for the following two reasons. - *Work Plan* As per Annexes C/D/G to IDC-EIB Agreement, the RCF programme benefited a multiannual Business Plan with clear KPI targets for each year of the implementation period, which enabled all stakeholders to assess RCF developmental / financial performance over time, and constituted a very clear work plan. Besides, please note that there is no reference to such work plan in the Financing Agreement, IDC-EIB Agreement or EU-EIB Agreement. Consequently we cannot see how it could be argued that the above should have been an EIB prerogative under its mandate. - *More thorough analysis of the RCF portfolio situation […] to have a more accurate appreciation of the results and impacts* We believe that within the mandate entrusted to the EIB, we have reported as much as possible based on the tools/information made available to us. By definition the Annual Survey (referred to in FA/TAPs/Annex2/Activity 5.4) was performed once per year, i.e. actual information was updated on an annual basis. As a result, it was not possible to report more than once per year on the actual socio-economic indicators simply because it has never been envisaged that RCF will do so. Besides, the importance of the post monitoring to check on the social – economic results has all extensively and repeatedly been emphasized by the EIB. EIB has been inter alia actively involved with respect to monitoring and reporting on: HIV plans, WT, NFC	This recommendation is maintained, especially regarding i) the importance of detailed annual work plans if monitoring is to be facilitated against detailed objectives and ii) the importance of having a portfolio approach in assessing RCF, especially when the fund is mature and nearly fully invested, if one want to draw generic lessons learnt.

		performance, impairments, write-offs, exit etc.
		
		In its reporting to the PSC, according to its mandate the EIB gave a bird's eye view on the management, implementation and performance of RCF. For that purpose, the EIB developed its own independent database that tracked financial and non-financial indicators independently. The focus of EIB's reporting was not on descriptive or quantitative elements, but to perform a qualitative assessment and draw lessons. This included the following elements:
		- Report on certain areas not covered by the IDC in its own reporting:
		  o review of Annual Surveys (highlighting assets/shortfalls and key conclusions)
		  o focus on financial performance (RCF's risk profile based on approval/disbursements, analysis of reflows received vs. expected)
		  o challenges of dealing with subsidiaries of large group, and cancellations
		- Use raw data furnished by the IDC as a starting pointing to provide further analysis
		  o determine concentration risk from both financial and development perspectives by geographies / sectors / key investees.
		  o Peer comparison of NF performance from an RCF perspective
		- Put the activity of any specific quarter into the overall RCF context by comparing periods, showing evolutions and drawing trends.
		- Provide concrete feedback to PSC members through	

		positive and negative lessons learnt o For example from approvals / site visits / annual surveys: RCF clear additionality, strong empowerment features, slow BS paradigm shift, lack of monitoring of HIV / upside payment / HDP ownership. As to the financial model, its necessity has been identified and its design has been supported by the EIB in connection with RCF. But, the financial model had some limits outside EIB control, e.g. absence of automatic comparisons between quarters and between cash flows received vs. cash flows expected. EIB made nevertheless the effort to extract this information manually investee-by-investee from the model to determine the percentage of return which is actually "pushed back" quarter-by-quarter (see slide EIB presentation to PSC, Quarterly Performance Review Q3-2011, III,3. Quarterly reflows). Bearing in mind that: (iv) reporting by the EIB had been intended (see FA/TAPS/Annex 7) to be limited to macro-monitoring of the portfolio, but in practice had to go beyond this aspect, especially to enhance its reporting on socio-economic and financial impact of the programme, as illustrated above, (v) EIB analysis was limited by the tools / information at its disposal (such constraints being beyond its control), (vi) EIB reporting was performed in accordance with MTR recommendations (e.g. analysis of the evolution on portfolio basis by sector, concentration risk, sustainability concerns, due and delayed payments, etc.) we disagree that EIB could have provided a more thorough analysis of the RCF portfolio situation […] to have a more accurate appreciation of the results and impacts.	

6.2.2 - Recommendation on "Lifestyle" SMEs Transparency	116-117	**EU Comment** **(Recommendation on "Lifestyle" SMEs Transparency):** I have not included a specific comment in the report but clarity is needed on how the SME rating system would impact/benefit start-ups. It seems that only existing enterprises would be able to benefit. Please clarify – it is important.	Correct; start-ups would not normally benefit from such scheme. This has been made clear in the report.

Annexes

Section	Page No.	Comment	Action taken
7.5 Annexe: Medium Term evaluation and ROM recommendations and comments	109-110	**IDC Comment** Not sure why quite a number of recommendations don't seem to have been addressed. We have attached the working documents which reflects the action plan and the latest status on each action. As far as we know all action where addressed and closed, except for those actions that are on going.	This has been revised based on additional information provided by IDC

Other Comments from EIB

Annual monitoring and reporting on actual performance of RCF2 We fully concur that this is a crucial aspect for a programme like RCF having such a strong focus on developmental/financial impact on HDP SMEs / job creation / empowerment. According to MTR recommendations and in light of the shortcomings identified further to the first Annual Survey, EIB proposed to review together with IDC Terms of Reference for the second Annual Survey completed in 2010/2011 in order to address issues related i.a. to scope and methodology. It seems that efforts in this regard discontinued after 2011.	Noted
EIB insisting on a more rigorous monitoring of the actual performance of investees We believe that within the mandate entrusted to the EIB, we have reported as much as possible based on the tools/information made available to us, both at our/RCF level. All the more as EIB has been	Already commented here above.

actively involved in the enhancement of its own/RCF monitoring and reporting, especially further to the MTR (financial model, Annual Survey, NF, WT, risk profile, concentration, reflows, BS, etc.). As highlighted on page 78, “The EIB’s intervention forced RCF to formalise more rigorously […] its reporting.” Bearing in mind that monitoring by the EIB had been intended (see FA/TAPS/Annex 7) to be limited to macro-monitoring of the portfolio, but in practice had to go beyond this aspect.	
EIB Management fee not creating an incentive The EIB disagrees with this assessment. As a public policy driven bank the EIB is by definition incentivised by aspects beyond profits, while such an approach could create a bias against seeking the type of risk that the Programme targets for development reasons.	Already commented above.
Financial instrument used Please note that we do not share the view that RCF subordinated are not equity / quasi equity instruments. RCF subordinated loans can be categorised as “quasi-equity” after taking into consideration their following features: maturity, grace period, subordination, variable component, uncapped upside. (if a company were to be exceptionally successful RCF would fully participate in this upside without limitations)	Already commented above.
Flexibility in the investment guidelines We welcome this lesson learnt, as illustrated by IDC-EIB pragmatic approach in this regard either through derogations or amendments to the Investment Guidelines as and when required.	Noted
Transactions where RCF supported a WT increasing the leverage of the SME RCF instruments used in financing SMEs with WT do not differ from financing SMEs without WT. RCF instrument had similar equity/quasi-equity features in both cases. If it was the case, this would imply that all RCF operations increased SME leverage, instead of providing quasi-equity.	Idem
Review the effectiveness of Workers’ Trusts	Idem

As per the SA BEE legislation, and in line with RCF agreements (FA, MoU), WT have been identified as an appropriate tool to promote BBBEE. However, it appeared that - not only for RCF but for IDC in general - the implementation of WT schemes (e.g. absence of follow up and lack of provision of BSS) has been problematic and needs indeed to be reviewed, as recognised by IDC SED team.	
Deals rejected and cancellations Pricing is reported as being one of or the main explanation. Please note that this did not correspond investigations carried out in 2010 and 2011 by RCF-EIB.	Noted