Filling in the Gaps: Matching Venture Financing with USAID Technical Assistance in Morocco

VEGA Special Program Update

"The developing world…faces a dearth of risk capital that has and will continue to constrain growth. Donors need to face the reality that the young companies that can really move the needle on innovation, inspiration and employment need high-risk, reasonably-sized, equity investments to grow."

- Alan J. Patricof and Julie E. Sunderland, Venture Capital For Development

The Context

A key area of mutual interest between economic development actors and venture financing is building successful small and medium enterprises (SMEs) and business ecosystems that have a significant positive impact back into their economic environment. In emerging markets, even growing and growth oriented SMEs with strong potential for expansion often have difficulty accessing capital and overcoming the challenging business climate. A lack of internal capabilities and the limited capacity of their backers can stunt innovation and competitiveness.

Focused technical assistance (TA) to venture backed SMEs, working to address local ecosystem gaps and improve competency in order to be internationally competitive, can help alleviate systematic weakness, attract more venture financing to such firms, and generate more sustainable and higher quality employment opportunities.

In the past twenty years or so, across most emerging and frontier markets, a class of venture investors have emerged that are seeking to invest in local SMEs that are poised to grow. Despite the clear benefits of growth-focused SMEs to emerging and frontier markets, potential venture investors face significant challenges with investment and business climates that make it very difficult to profitably invest. In general, overall profits (or returns) to equity investors in SMEs and entrepreneurs from venture investments are not covering the losses or are not attractive enough to pull money away from "more certain bets" like real estate.

For the venture investor, technical support represents a better chance to achieve the impact-investor level of returns needed to attract further outsider investors and thus increase available intelligent funding to this category of SME.

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About VEGA:

VEGA, the world's largest consortium of economic growth volunteer organizations, with 23 member NGOs has assisted 140 developing countries & mobilized more than 25,000 experts to promote economic growth activities over the past 5 decades. VEGA's track record includes over 30 programs worth more than $250 million. VEGA is a 501 (c)(3) nonprofit organization and was founded in 2004 by the US Agency for International Development through a Leader with Associate (LWA) award cooperative agreement. This LWA is available to all USAID Missions.

USAID FROM THE AMERICAN PEOPLE

VEGA's F2F Pilot Bridges the Gap in Morocco

The USAID funded Farmer-to-Farmer (F2F) pilot project ***Engaging Venture Capital to Strengthen Agricultural Value Chains in Morocco*** that VEGA implemented from 2012 to 2013 arose from two key observations initially made by Program Advisor William Fellows, a former venture investor and long-term advisor to venture/risk capital funds in the Maghreb region:

1. Despite bringing 'smart' capital to growth oriented SMEs in Morocco, Venture Funds face real and impactful constraints. VC funds in emerging markets are typically staffed by purely or largely financial staff, ex-bankers, or chartered accountants who do not have the expertise necessary to help solve pressing industrial challenges, whether in production, technology, or management.

2. Local markets can have decent basic expertise to develop and call on, but often lack in depth expertise to support industrial innovation, particularly for new markets. It is usually cost and time prohibitive to search out and bring in specialized expertise on their own, and typically the investor teams lack the time and networks to address specialized issues that a firm may face, such as specific certification issues for a given market or improvement in industrial processes.

The project established a partnership between the Moroccan national venture capital association (AMIC) and VEGA as an important screening mechanism to identify technical assistance needs for high-potential, innovative agribusinesses. It also was conceived as a mechanism to assist the agribusiness sector better understand the long-term business and economic value of equitable win-win relations, in particular with small holder farmers. The key rationale behind this is that serving as positive business role models for the agriculture sector, newly competitive agribusinesses engaged in win-win solutions will contribute to improving the overall sector and laying a positive basis for scaling agricultural productivity and opportunity.

Association membership response was strong, with three to four times as many eligible projects being proposed as the pilot could handle. Needs focused particularly on issues where the entrepreneurs and investors saw themselves as being weak, such as issues around international certifications, related market development for export and in adopting new, energy efficient production technologies. Three quarters of the beneficiary firms were early stage firms setting up methods of production and processes that are new and innovative for Morocco.

The pilot project's focus on delivery of shorter-term senior level voluntary expertise in specific industrial and management areas, matched well with the needs of entrepreneurs. Response was strong, with 3 to 4 times as many eligible projects being proposed as the pilot could handle. Straddling mentorship and expert advisory missions, the project brought advanced insight to skilled entrepreneurs to help them overcome potentially fatal issues in setting up their industrial processes or entering new markets. Longer-term expertise, either using local consultants or long-term international advisors to transfer competency, was also identified as being useful to build firm management capabilities and help champions emerge.

Conclusion

Poor returns among SMEs in emerging markets are holding back impact investors. The VEGA F2F pilot in Morocco has shown that by providing targeted technical assistance to agribusiness start-ups with growth potential risk can be reduced and profitability improved. By transferring skills and expertise and assisting management to overcome hurdles, performance is enhanced and thus the overall financial return is more attractive. Not only does the technical assistance improve performance at the firm level, it is also helpful in strengthening the local staff of venture capital funds to incorporate analysis and support that goes beyond mere accounting and financial factors for success.

Despite the popularity of entrepreneurship-focused development programming over the past decade, insufficient attention has been paid to the sustainability and scalability of efforts. Active collaboration with the world of venture finance can help stakeholders put their time and money where they will be able to make a real difference in the economy. Venture capital funds with investments in emerging markets will in turn see improvements in their returns as the supporting environment for innovative, risk-taking entrepreneurs across all sectors is steadily improved.

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