

SUMMARY PROJECT FICHE

Project number: BG980502

Title: Bulgarian Post-Privatisation Fund (BPPF)

Location: Bulgaria

Objectives:

Development of the private enterprise sector in terms of strengthen corporate governance, post-privatisation restructuring and modernisation by providing equity investments and turn-around-management assistance (know-how transfer) to newly privatised medium size enterprises through the establishment and funding of the Bulgarian Post-Privatisation Fund (BPPF) operation.

This is fully in line with the Government's policy on private sector development and the economic reform priority of the Accession Partnership.

Description:

The BPPF is a post privatisation vehicle aimed at supporting medium-size enterprises in the private sector combining equity injection and turn-around-management assistance (know-how transfer). The BPPF will respond to a large and unfulfilled need for new investments, strengthened governance and management assistance and will support upgrading and modernisation of private enterprises. The BPPF's transition impact will be significant as it will be the first Bulgarian fund that will target enterprises which would normally not be able to secure private equity capital. Its financing structure will combine equity contributed by the EBRD and the Fund Manager with technical assistance provided by Phare to cover: (i) operating expenses of the fund management team, (ii) pre-investment due diligence of enterprises and preparation of business plans, and (iii) post-investment advice on restructuring. The BPPF will be capitalised with ECU 30 million provided by the EBRD, and ECU 10 million co-investment from the Fund Manager, and up to ECU 15 million in technical assistance from Phare over the period 1997-2000. Initial Phare funding was provided in an amount of ECU 1.5 million under the 1997 national Phare budget for Bulgaria.

The BPPF will be managed as a commercial professional venture capital fund by Europa Capital Management A.S., the Fund Manager selected and contracted for this purposes in compliance with standard Phare procedures in December 1997. The operation will be based in Bulgaria, and will be aiming to achieve a commercial rate of return. The BPPF will target the domestic medium-size private sector which typically will not have a foreign partner but will be fundamentally sound and able to grow and improve their performance. Investments will be made in an estimated 12 to 15 companies selected by the Fund Manager, and the average investment size will be ECU 3.2 per company. These companies have in the order of 100-1.000 employees and an annual sale of at least ECU 2.5 million. The combination of commercial equity and grant finance will make it possible to invest in enterprises that normally can not be reached by (foreign) private sector equity funds.

Two mechanisms are being established to ensure that the Fund Manager adheres to the investment policy of the fund and carries out its operations efficiently and effectively: a Supervisory Board, and an Investment Committee. In addition, a Contact Panel will strengthen the Fund's communication and links with the business and financial community.

Institutional framework:

EBRD will retain overall responsibility of the Fund whilst the Fund Manager will be responsible for the day to day operation and management of the BPPF. The EBRD will play an active role in the implementation and monitoring of the BPPF since it has:

- a majority of votes on the BPPF Supervisory Board;
- a veto right on the BPPF Investment Committee;
- a close involvement on liaison with the EC and in supervising the delivery of the technical assistance.

Budget:

The Commission and the Government of Bulgaria have agreed that the Commission makes available up to ECU 15 million in technical assistance funding for the BPPF. ECU 1,5 million has been approved and contracted under the 1997 national Phare programme (BG9704 - General Technical Assistance Facility) in order to kick-start the project. The Fund Manager has started working in February 1998 and made good progress in the initial project phase, including establishment of a deal pipeline.

Based on their planned activities over the next 18 months (see attached summary report), including conversion of the deal flow into investment proposals, and the plan to complete four investments by the end of 1999, and additional ECU 3,5 million will be allocated under the 1998 Phare programme. Subject to the performance of the Fund and based on justified needs additional technical assistance funding will be provided for up to maximum of ECU 10 million (respecting the initial commitment in principle to co-finance with a total maximum of 15 MECU) during 1999-2000 out of the annual Phare programme allocation for Bulgaria. These subsequent allocations will require the positive opinion of the Phare Management Committee in the context of the annual budget decision process.

Phare contribution to technical assistance will under this project be allocated to cover the cost of:

- (i) the Fund Manager's fee and operating costs for the first 5-6 years of operation;
- (ii) fees for consultancy services and operating costs that are directly related to the BPPF for pre- and post- investment services;
- (iii) the management fee to the EBRD to cover the costs directly related to management and implementation of the Agreement between the EBRD and the European Commission for Technical Co-operation Funds for the BPPF.

PHARE 1998	Investment (MECU) - HQ
1. Fees (Fund Manager and EBRD)	1.6
2. Consultancy and Special Advisory Services	1.9
TOTAL	3.5

Implementation arrangements:

The Fund will be a managed account of the EBRD, and as such, a contractual arrangement by which EBRD will make direct equity investments in Bulgarian companies with these investments being managed on its behalf by the Fund Manager.

The contractual responsibility for the management of the Phare funded technical assistance will be transferred to the EBRD under a Technical Co-operation Agreement made directly by Brussels. EBRD will keep these funds on an account separately from the BPPF budget intended to investment. On receipt of a request from the EBRD for funds together with a budget estimate for expenditures during the following 12 months and a report on the use of funds for the BPPF during the preceding 12 months the Commission will deposit on the funds account the requested budget, less any unused portion from the preceding 12 month period.

The EBRD has selected the Fund Manager in accordance with standard Phare procedures and with the Commission participating in the evaluation as observer. The selection and recruitment of the consultants is carried out in accordance with the standard Phare procurement rules.

Implementation schedule:

Start of tendering	Start of implementation	Completion of the 1998 allocation
ongoing ¹	ongoing	Feb. 2001

Please refer to the attached table.

Equal opportunity:

Equal opportunities will be taken into account in the preparation of all tender dossiers and in the recruitment of personnel, by placing special encouragement phrasing in the dossier. The women participation will be measured based on equal expertise levels. The Fund is an equal opportunity employer and already has a mix of female and male employees.

Conditionality and sequencing:

The Bulgarian Government shall remain committed to its privatisation programme and the objective of completing the privatisation process in the medium term. It shall pursue a policy of transparency in the privatisation process and refrain from introducing measures which will hamper the development and operation of private enterprising. Specifically, the Government shall continue to refrain from exercising political pressure or otherwise interfere in the operation of the BPPF.

The performance of the Fund is insured as the Fund Manager has invested ECU 10 million in the BPPF and will receive the carried interest, proportionally to his investment. The expected return on investment for the Fund is 20%. However, whenever the Fund Manager does not fulfil its management obligations, the EBRD can terminate the BPPF at anytime by notice in writing to the Manager.

Annexes

1. Log-frame matrix
2. Implementation chart
3. Cumulative contracting and disbursement schedule by quarter for full duration of the project

¹ Medium-term funding of the overall project was agreed to and initially funded in 1997

4. BPPF summary progress report.

Annex 1

BG980502			Date of drafting: 28/4/98
LOGFRAME PLANNING MATRIX FOR TECHNICAL COOPERATION FUNDS FOR THE BULGARIAN POST PRIVATISATION FUND (BPPF)			Total Budget 3.5 MECU
Wider Objective	Indicators of Achievement	How, When and By Whom Indicators Will Be Measured	Assumptions and Risks
<ul style="list-style-type: none"> to contribute to the economic reforms to strengthen the enterprise restructuring process 	<ul style="list-style-type: none"> economic growth increased share of the private sector in the GDP increased competitiveness 	<ul style="list-style-type: none"> Bulgarian National Statistics Office reports of the BPPF Supervisory Board regular Fund Manager (FM) progress reports to the EBRD. 	<ul style="list-style-type: none"> currency fluctuations and political instability of Bulgaria slow down of the privatization process major economic changes
Immediate Objectives	Indicators of Achievement	How, When and By Whom	Assumptions and Risks

		Indicators Will Be Measured	
<ul style="list-style-type: none"> to provide Bulgarian companies with a source of private equity capital to transfer business know how, introduce strong corporate governance and enhance entrepreneurial skills. 	<ul style="list-style-type: none"> preparation and submission by the Fund Manager of investment proposals to the BPPF Investment Committee. Justified utilization of the Technical Co-operation Funds. 	<ul style="list-style-type: none"> Investment Committee proposals EBRD annual report on the use of the TC Funds submitted to the Commission after the end of each of the EBRD's fiscal year, an externally audited financial statement of the TC funds submitted by the EBRD to the Commission. 	<ul style="list-style-type: none"> poor investment decisions by the Fund Manager lack of investment opportunities insufficient exit opportunities insufficient management talent in investee companies inability to attract experienced consultants to complement existing teams.
Outputs	Indicators of Achievement	How, When and By Whom Indicators Will Be Measured	Assumptions and Risks
<ul style="list-style-type: none"> deal pipeline established successful realisation of investments successful performance of the investee companies and improvement of their management. 	<ul style="list-style-type: none"> profit recorded by the BPPF profit recorded by the investee companies preparation of a system to record, analyze and report on the deal pipeline and deal flow. 	<ul style="list-style-type: none"> due diligence reports reports drafted by the consultants BPPF annual report, including performance investee company annual report. 	<ul style="list-style-type: none"> None

Inputs	Indicators of Achievement	How, When and By Whom Indicators Will Be Measured	Assumptions and Risks
<ul style="list-style-type: none"> • Technical Co-operation funds (MECU 3.5). 	<ul style="list-style-type: none"> • successful continuation of the BPPF project • contracting and disbursement of funds • professional legal, accounting and environmental expertise to the Fund Manager 	<ul style="list-style-type: none"> • BPPF annual report from the EBRD to the Commission on the use of TC funds • financial and accounting records concerning the use of TC funds, kept by the EBRD 	<ul style="list-style-type: none"> • poor consultants' management • lack of continuity and availability of consultants.

IMPLEMENTATION SCHEDULE

TECHNICAL COOPERATION FUNDS FOR THE BULGARIAN POST PRIVATISATION FUND

	1998												1999												2000												2001	
TASK NAME	J	F	M	A	M	J	J	A	S	O	N	D	J	F	M	A	M	J	J	A	S	O	N	D	J	F	M	A	M	J	J	A	S	O	N	D		F
1. Fees (Fund Manager and EBRD)																																						
2. Consultancy and Special Advisory																																						
Services																																						

Tendering

Contracting

[REDACTED]

Implementation
Disbursement

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&

[REDACTED]

[REDACTED]

	1st quarter	2nd quarter	3rd quarter	4th quarter	1st quarter	2nd quarter	3rd quarter	4th quarter	1st quarter
	1998	1998	1998	1998	1999	1999	1999	1999	1999
MECU (cumulative)					3,5				
%					100				
MECU (cumulative)					2,14	2,82			
%					61	80,5			

Annex 4

Establishment of the Bulgarian Post Privatisation Fund (“BPPF”)

Background

ECM Holdings was selected as the preferred manager of the BPPF in December 1997 and a conditional Agreement appointing them was signed on 17/18 December 1997. The condition was that Technical Assistance funding (“TA”) would be provided by the EU Phare programme and would amount to some ECU 15 million over the life of the Fund. On the basis of this document, new staff were recruited and existing staff transferred to the Fund. The team consists of Tony Diment, Executive Director, as senior venture capitalist, Vladimir Karolev as senior local manager, three Bulgarian analysts, the technical assistance administrator and six staff shared with ECM, an in-house lawyer, translator, accountant, receptionist and two drivers. The staff are now working. New premises have been found in a central location in Sofia which were felt to be appropriate for the Fund and effective activity of ECM Holdings started in Bulgaria in January 1998.

Activity Levels

- Since operations started

The new team reviewed all the available material on companies recently privatised in Bulgaria and monitored the information on the new wave of privatisation. In addition, applications were received from private companies advised by professional advisers who were aware of the establishment of the Fund. These applications were carefully reviewed and visits undertaken.

ECM Holdings visited companies in the pharmaceutical, wine, ceramic and paper industries and met the management of an expanding diversified distribution business with exclusive distribution agreements from Volvo, Renault, IBM, Compaq. A tour to visit the prospects was arranged.

A deal pipeline review has been established and weekly review meetings are held to progress opportunities (see attached). There are some serious prospects approaching the due diligence stage. A Letter of Intent has been drafted for signature by one of the Sofia based Privatisation Funds to enable ECM to evaluate an investment in a pharmaceutical company which will require the commissioning of three TA reports. These will comprise a report by a sector specialist, an accountants report and a legal review.

ECM had identified an opportunity for investment in the cardboard manufacturing sector and the prospect of a joint investment with them was pursued. Considerable time and resources were applied to the evaluation and preparation of a submission to the Investment Committee of the Fund. The minutes of that meeting and the due diligence reports have been provided.

A training programme is being prepared for the Technical Assistance administrator which will consolidate her understanding of the procedures manuals by practical sessions in London with the EBRD liaison team. A programme is also being prepared for the analyst team which will develop their venture capital skills by reference to carefully chosen case studies presented by experienced venture capitalists.

The Phare 1997 budget allocation as Technical Co-operation funds to the BPPF (ECU 1,500,000) has covered the Managers fees and expenses together with due diligence costs.

- Activities foreseen in the next year:

The initial level of enquiries indicate that there is a strong deal flow which needs to be pursued. The investment team is encouraged by this level of activity and is pursuing opportunities. The effort being put into developing contacts at all levels of the relevant government agencies, particularly the Privatisation Agency, is beginning to show encouraging results and this will be continued in the coming year.

The most promising industrial sectors currently are wine, pharmaceutical, paper, food production, energy and distribution. If the strong deal flow can be converted to investment proposals the plan of completing four investments by the end of 1999 seems feasible.

The 1998 budget covers, in addition to the Fund Management fee and the EBRD fee, the creation of two framework agreements for professional services, a pool of self-managed consultants and advisory services. The tendering process for these needs to be put in place as soon as possible so that due diligence work can proceed in a seamless fashion.

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Services																																						



Tendering



Contracting



Implementation & Disbursement

Annex 3

COMMITMENT AND DISBURSEMENT SCHEDULE

	1st quarter 1998	2nd quarter 1998	3rd quarter 1998	4th quarter 1998	1st quarter 1999	2nd quarter 1999	3rd quarter 1999	4th quarter 1999	1st quarter 2000	2nd quarter 2000	TOTAL
<u>Commitment :</u>											
MECU (cumulative)					3,5						3,5
%					100						100
<u>Disbursement:</u>											
MECU (cumulative)					2,14	2,82			3,5		3,5
%					61	80,5			100		100

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