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Developing Private Enterprise Internationally

The story of IFC operations in 30 countries

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Establishment of a diversified and stable economy offering the promise of better living standards and prospects for employment is one of the most urgent requirements of virtually all of the less developed countries. Most of these countries possess a narrow economy based on production and export of one or a few commodities, and thus, they are highly vulnerable to adverse changes in world demand and prices for these items.

One essential goal of development should be a sound and efficient agriculture. But, if developing countries are to achieve the blessing of a broadly based economy, industrial enterprise with its potential for diversification and for gainful employment opportunities is needed.

Formidable obstacles stand in the way of industrialization of these countries with their grave shortages of capital and lack of technical skills. Imports of foreign private capital, accompanied by technological and managerial expertise that will work with local private interests and spur local capital formation, is possibly the most practicable means for reducing the pains of industrial development.

Serving both as a participant in and a catalyst of private investment in industrial development, is the International Finance Corporation. This organization has the distinction of being the only international development agency whose function is to assist the development of private industry on an international scale. The IFC is unique in another way. It is the only one of these agencies that can and does invest in corporate shares or equities.

IFC is closely affiliated with the World Bank and membership in it is open only to Bank members. Currently, 78 countries are members of IFC and have subscribed to nearly $99 million of capital, all of it paid in gold or United States dollars and freely usable in investment operations.

Industrial Development

IFC was established in mid-1956 and by December 31, 1964, had undertaken 97 commitments in 30 countries aggregating over $127 million. About $110 million is assisting new private enterprises or the expansion of existing concerns and $17 million the establishment or growth of development finance companies in 11 countries. The latter institutions are designed to assist private industrial development in the countries where they are located.

IFC-backed financing is enabling enlargement of the steel plant of Compania Fundidora de Fierro y Acero de Monterrey, S.A., in Monterrey, Mexico. Workmen here install a motor armature at the plant's 46-inch blooming and slabbing mill

All of these operations were undertaken in the less developed of IFC's member countries, to which it limits its operations. Included in the eligible category would be such relatively advanced countries as Finland, Spain and Greece, but not Canada, the countries of the "Common Market" area or the United States.

Private Enterprise

All commitments were undertaken in partnership or in participation with local or foreign private interests or a combination of both and were in connection with the financing of private industrial enterprise either directly or through the medium of investment in a development finance company.

Operations were at a record level in calendar 1964, with nearly $25.4 million of commitments in 19 enterprises. A brief listing of these operations indicates their variety and scope. Commitments were made in development finance companies in Colombia, Spain and Thailand; in textile companies in Ethiopia, Nigeria and the Sudan and steel and steel forgings producers in Colombia and Mexico; in cement companies in Greece, Pakistan and Peru and in food processing firms in Chile and Colombia. Other commitments were to assist an automotive equipment producer in Spain; a pulp and paper plant in Argentina; a heavy construction equipment manufacturer in Mexico; a leather tanning company in Honduras; and a sugar producer in Tanzania.

In its direct investment operations IFC patterns the form of its investment to the specific requirements of each project. It may make a straight equity investment, a mixed equity-loan investment or a loan bearing stock options, conversion rights or other special features.

As the Corporation's knowledge and experience has grown, it has broadened its operations to a point where it has ceased to be merely an investor and has become an "International Investment Bank". It

gives underwriting and standby commitments to corporate issuers in connection with the sale and distribution of shares and debt obligations. Frequently, these commitments are related to the financing of a project in which IFC has agreed to take a direct investment interest, as well.

Careful Study

Other investment banking activities include a careful study of each project presented for investment consideration; working in close collaboration with project sponsors in helping to resolve technical, managerial, marketing or other problems; and service as intermediary in obtaining outside technical or managerial advice and personnel.

IFC assists in drawing up sound financial plans for projects and, where appropriate, will help the sponsors to obtain additional local or foreign investment or a combination of the two. Through the international sale of direct investments from its portfolio to other financial institutions, IFC contributes to a further broadening of the market for shares and securities issued by private industrial enterprises in less developed areas. By this means, it also replenishes and increases the effectiveness of its own financial resources. In all, IFC has sold or agreed to sell over $25 million of equity and debt items, acquired through investment operations.

In true investment banking fashion, IFC frequently maintains a close and continuing working relationship with projects and their sponsors, and further investment or commitments may result. For example, in 1964 four out of the 19 commitments made were to enterprises previously assisted by IFC; and four other commitments arose from exercise of stock options received in connection with previous financings.

Consequently, IFC in a number of instances may be regarded as the medium through which the various elements and interests necessary to the successful organization, financing and operation of a project are brought together into what might be termed an "investment package". This is the classical role of the investment banker.

Tunisian Company

A Tunisian company, N.P.K. Engrais, illustrates the role undertaken by IFC in connection with support to private industrial development. N.P.K. is constructing and will operate, at the Port of Sfax, a "triple super-phosphate" fertilizer plant with an annual capacity of 150,000 tons, and utilizing local phosphate rock for raw material.

A leading Swedish fertilizer producer originally sponsored the project, but needed additional outside financing and looked to IFC for help. IFC agreed to examine the project and in doing so came up with three substantive proposals which were incorporated into the over-all project plan. One concerned marketing of N.P.K.'s output, all of which is to be exported from Tunisia. To insure against uncertainties IFC suggested that the Swedish company enter into a long-term contract to purchase and distribute a sizable amount of N.P.K.'s production in Scandinavia. The suggestion was accepted.

IFC's study also indicated that "on site" production of sulphuric acid from imported sulphur, would in the long run be more efficient and less costly than importation of the acid. It was decided to construct a sulphuric acid plant, as part of the project, which meant a need for further capital to meet higher costs and for technical expertise in constructing and operating such a plant. Both the added capital and the technical partner were obtained by gaining participation of Freeport International Corporation, a subsidiary of a leading U.S. sulphur company.

Ultimate capitalization of the company was as follows: the Swedish company put up $3.5 million of equity capital and lent more than $2.1 million; Freeport put up equity capital of $1 million and lent $600,000; and IFC purchased $1.5 million of equity and lent $2 million. In addition, IFC actively sought the participation of private finance companies in its portion of the investment and succeeded in selling more than $1 million of its holdings—including about $340,000 in shares—to interests in Kuwait, the Netherlands, Sweden, and United States and elsewhere.

Local participation is planned in N.P.K. and the shareholders have agreed to reserve 10 percent of their equity investment for sale to Tunisians. The project is already in the initial production stage and should be completed ahead of schedule in the spring of the current year. Tunisia will benefit in several ways. A natural resource will be developed; and the country's balance of payments will be strengthened by N.P.K.'s exports. Some 360 Tunisians will find employment at the plant and a training program to provide technical, administrative and other training to Tunisian employes is incorporated in the project.

Largest Involvement

IFC's largest financial involvement has been with Cia. Fundidora de Fierro y Acero de Monterrey (FUNDIDORA), Mexico's largest privately-owned steel producer. In 1962, as part of the long-range financing of a $100 million expansion program designed to increase steel capacity from 200,000 to 500,000 tons annually, the company sought to sell 586,333 shares. IFC bought 128,000 shares valued at about $1.1 million for its own portfolio; and agreed to underwrite 75 percent of 458,333 shares, valued at about $3 million, which the company was offering to its shareholders. The remaining 25 percent of the offering equal to $1 million was underwritten by Credito Bursatil, a financing subsidiary of the Banco Nacional de Mexico.

Associated with IFC as sub-underwriters were Kuhn, Loeb & Company, Inc., of New York; Handelsfinanz A.G. of Zurich; and Morgan Guaranty International Finance Corporation also of New York. By participating in this transaction IFC assisted a major Mexican enterprise to broaden its equity base and to sell, in an orderly way, a share issue whose size would ordinarily have presented problems to the Mexican market. The offering was successful and virtually all of the shares were sold in the Mexican market, though some were disposed of on the Canadian and European markets and in other Latin American countries. One major result was an increase in FUNDIDORA shareholders from 700 to 2,500.

FUNDIDORA in 1964, again sought to broaden its equity base as part of a financial plan needed to further expand the company's annual steel capacity from 500,000 to 750,000 tons. A total offering of 1,250,000 shares valued at about $12.5 million was involved and IFC and Credito Bursatil agreed each to underwrite 50 percent of the offering. This constituted Mexico's largest offering by far on so wide a basis to stockholders of a private Mexican company; and the largest single commitment to date by IFC. The same three sub-underwriters, as in 1962, agreed to join with IFC in this financing. The offering was successful and the bulk of the shares disposed of in the market.

Better cotton is being combed by this worker thanks to a $750,000 IFC loan to Adamjee Industries, Ltd., Karachi, West Pakistan

A $2.45 million IFC loan has expanded Brazilian manufacture of Jeep vehicles at the Willys Overland do Brasil, S.A., Industria e Comercio plant at Sao Paulo, Brazil. Photograph shows plant transmission assembly area

Exercised Rights

In 1964, IFC also exercised stock rights to acquire a further $346,232 in FUNDIDORA shares for its own account. In all, IFC had commitments in over $10.5 million of FUNDIDORA shares, including more than $9 million involved in the two underwritings and purchases of $1,473,534 for its own account. As of December 31, 1964, it had satisfactorily liquidated its underwriting position; and from portfolio had sold, at a profit, over $500,000 of its direct investment in FUNDIDORA.

A major activity of the Corporation is the direction and leadership it brings to the World Bank Group—the Bank, the International Development Association and IFC itself—in helping to organize and finance "development finance companies". The Group has supplied some $300 million in loans and investments to 18 of these institutions, with the bulk coming from the World Bank in loan form. IFC's contribution amounting to only $17 million has been, however, in all-important equity financing that has broadened the equity and therefore the borrowing base of the companies. In several instances an IFC equity commitment was sufficient to broaden a development company's equity base to a point where it became feasible for the World Bank to lend to it.

Privately controlled development finance companies can contribute materially to the process of private industrial development in countries where they are located. They are sources of local capital to industry and through underwritings and other means of distributing, corporate issues can be the focal point for private capital formation and market development.

Through borrowings from the World Bank or other outside sources, development finance companies can make foreign exchange available to local enterprise in need of equipment or other essential imports. In addition, through their relationship to the World Bank Group and to private banking and financial institutions, development finance companies can serve as a bridge across which foreign financing and foreign sources of technological and other skills can flow into the development of local private industry.

For these reasons the World Bank Group strongly supports the formation, where feasible, of private development finance companies. Through the offices of IFC's "Development Finance Companies Department", the Group offers much more than financial assistance to these institutions. When required, IFC on behalf of the World Bank Group, stands ready to advise on the formation of a development company, on its organizational structure and on management and other questions that may arise. It will also assist in obtaining competent management and advisory personnel from outside and, when desirable, will recruit local and foreign interest in the financing of the company.

"Special Consultant"

An example of how the World Bank Group can assist the founding and financing of a development finance company is the "Private Development Corporation of the Philippines" (PDCP). A "special consultant" of the Bank of IFC, as well as IFC personnel, worked with a Filipino "Steering Committee" in setting up this institution. The World Bank agreed to lend PDCP $15 million and IFC gave a standby commitment covering the sale of some $4.4 million equivalent of shares out of a total of $6.4 million to be offered.

The share offering was successful and IFC's final investment was a little over $205,000. But IFC also helped to bring in substantial international capital for PDCP. In all, 18 private investment companies and banks purchased 30 percent of PDCP's shares including 14

American, two British and one German and one Japanese bank. Among the American firms involved was Continental International Finance Corporation, a subsidiary of Continental Illinois National Bank and Trust Company of Chicago.

Useful Contribution

The bulk of IFC's investments and other commitments have supported projects that are making a useful contribution to development in the countries where they are located. Many of them have grown substantially over the years and, as pointed out previously, some of the sponsors have returned to IFC for further financing to sustain this growth.

But IFC is also in a business where risks can be high and some losses must be expected. Last fiscal year, for example, it wrote off its first investment loss amounting to $92,000, as the result of a liquidation of a rubber products company in Australia in which IFC's original investment was $315,000. The $92,000 loss was more than offset by profits of $449,000 from sales of other investments in the same year.

Enlarged Role

In the future there is a prospect that IFC's role in financing private industrial development will be greatly enlarged. It has been proposed that the Charters of the World Bank and of IFC be amended to enable the Bank to lend funds to the Corporation which, in turn, would re-lend to private industry without government guarantee. The amendments, now under consideration by the member governments of the two institutions, would permit the Bank to lend to IFC an amount equal to four times IFC's unimpaired capital anl surplus, or, at present, a total of about $400 million.

If the amendments are adopted, the Bank would make a line of credit available to IFC, and the Bank's funds, through this medium, could flow to private enterprises without the inhibition of having to obtain a government guarantee, as would be the case if the Bank lent directly. IFC's special qualifications and experience in dealing with industrial development, makes it the appropriate vehicle for such transactions. One advantage accruing to the Corporation itself is that if it obtains the use of World Bank funds, it can ultimately apply all of its own resources, now amounting to some $120 million, to urgently needed equity financings.