



OFFICE OF INSPECTOR GENERAL

AUDIT OF USAID/PAKISTAN'S ENTREPRENEURS PROJECT

AUDIT REPORT NO. G-391-12-005-P
APRIL 20, 2012

ISLAMABAD, PAKISTAN



Office of Inspector General

April 20, 2012

MEMORANDUM

TO: USAID/Pakistan Mission Director, Andrew B. Sisson

FROM: Office of Inspector General/Pakistan Acting Director, Michael Hutchinson /s/

SUBJECT: Audit of USAID/Pakistan's Entrepreneurs Project
(Report No. G-391-12-005-P)

This memorandum transmits our final report on the subject audit. In finalizing the report, we considered your comments and included your response in Appendix II.

The report contains two recommendations to help improve the Entrepreneurs Project. Based on information provided by the mission and USAID's Office of Economic Growth, management decisions have been reached on the report's recommendations. Please coordinate final action with the Audit Performance and Compliance Division in the Office of the Chief Financial Officer.

I want to thank you and your staff for the cooperation and courtesies extended to us during this audit.

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SUMMARY OF RESULTS

According to USAID/Pakistan, the country faces economic challenges that threaten its stability and limit business development. Small and medium-sized businesses constitute 90 percent of Pakistani firms, employ 78 percent of the nonagricultural workforce, and contribute more than 3 percent of gross domestic product. Loan requirements for businesses have become stringent, imports have become expensive, and the unemployment rate is rising. To help address these challenges, USAID/Pakistan initiated the Entrepreneurs Project in June 2009. It awarded a 5-year, \$30 million cooperative agreement to Mennonite Economic Development Associates to significantly increase the incomes of 120,000 predominantly female owners of microenterprises (microentrepreneurs) in 20 districts in Pakistan.

In March 2011, the mission modified the project's goal in response to a shift in U.S. Government strategy because of changing conditions in Pakistan—namely, the displacement of more than a million people in the Swat Valley as a result of conflict and the devastating floods of 2010 throughout Pakistan. The initial project goal of increasing the incomes of 120,000 microentrepreneurs was reduced to 75,000.

To achieve the goal by June 2014, the project focuses on developing value chains in four sectors—dairy, embellished fabrics, medicinal and aromatic plants, and honey. Value chains take products from raw materials to processing and ultimately to distribution and sale. The value chain concept is based on the premise that when the microentrepreneurs are in control of this process, they earn higher incomes.

The project is being implemented with local partners, the majority of which have limited work experience with USAID. Also, since the value chain concept is relatively new in Pakistan, local partners have limited capacity in applying it. The project seeks to build capacity by providing formal and on-the-job training to partners. Partners, in turn, provide training to predominantly female microentrepreneurs in finance, product design, marketing, and quality assurance in the four sectors. Examples of training by sector are:

- Taking proper care of dairy animals to increase milk quality and yield.
- Designing fabrics, determining color palettes, and determining cost and pricing in the embellished fabrics sector.
- Identifying high-value medicinal and aromatic plants and collecting and processing them using improved preservation and storage techniques.
- Applying better harvesting techniques, preventing disease in honeybees, and introducing affordable beehives that will lead to increases in honey production.

Furthermore, having helped improve the products with the above training, the project helps microentrepreneurs target the right markets and sell their products to maximize profits.

USAID's Office of Inspector General in Pakistan (OIG/Pakistan) conducted this audit to determine whether USAID/Pakistan's Entrepreneurs Project made progress in building the capacity of local partners and expanding opportunities for microentrepreneurs.

The project provided compliance and technical training (page 3). First, the project has provided training to local partners on USAID's administrative requirements related to financial management, procurement, and human resources. Second, local partners have received technical instruction in the value chain concept to enable them to help microentrepreneurs expand opportunities by improving their commodities' quantity, quality, and marketability. The project trained more entrepreneurs than expected in business development, achieving 123 percent of its target, and achieved 80 percent of its target for providing training in business management and marketing.

However, building capacity in developing value chains did not start until May 2011, almost 2 years after the award. Two factors contributed to the delays. First, USAID/Pakistan used project resources to provide assistance to internally displaced persons in Swat as a result of conflict and the devastating floods of 2010. Mission officials acknowledged this work diverted time and resources from the project's activities, as no additional funding was provided to cover the costs. Approximately \$4 million was allocated to this assistance work. Second, local partners' lack of awareness of the value chain concept caused delays in implementing the project. Specifically, the project undertook a laborious process for selecting and training local partners before work could begin to help microentrepreneurs. As of December 2011, only \$6.6 million had been allocated to helping microentrepreneurs develop value chains.

In addition, the audit disclosed the following challenges to achieving the overall project goal of substantially increasing microentrepreneurs' incomes:

- The project did not measure the change in beneficiaries' incomes to assess project impact (page 5). Although the project collected baseline income data when registering beneficiaries, USAID/Pakistan had not yet begun tracking changes in beneficiaries' income. As of February 2012, no information was available to determine whether the project has succeeded in increasing microentrepreneurs' incomes.
- The project made little progress in developing the honey sector (page 6). The mission took longer than expected to approve the local partner's grant application and then required a feasibility study to determine the best bee species to use and explain why bees in the target area died in the recent past. The lack of progress makes it unlikely that the project will achieve its objective for this sector on schedule.

Therefore, the report recommends that USAID/Pakistan:

1. Develop and implement a framework to collect information about changes in beneficiaries' sales and incomes. The information should be stored in a standardized format and should be updated routinely so that well-timed project assessments can be performed (page 5).
2. Develop and implement an action plan to increase the pace of development in the honey sector, or redefine or revise the activity objectives (page 7).

Detailed findings follow. A description of the audit scope and methodology appears in Appendix I. Full text of management comments appears in Appendix II, and our evaluation of management comments is included on page 8.

AUDIT FINDINGS

Project Made Progress in Compliance and Technical Training

In accordance with Modification 7 of the cooperative agreement, a key component of the USAID/Pakistan's Entrepreneurs Project is to build the capacity of selected partners in developing value chains in four sectors—dairy, embellished fabrics, medicinal and aromatic plants, and honey. The value chain concept traces products from raw materials to processing and ultimately to distribution and sale. The project seeks to build capacity by providing formal and on-the-job training to the partners. These partners, in turn, provide instruction to predominantly female microentrepreneurs in finance, product design, marketing, and quality assurance in the four sectors.

Capacity building consists of two types of training. One is to train the partners on compliance with USAID's requirements for financial management, procurement, and human resources so that partners can receive and administer USAID funds. This type of training strengthens the partners' operations by imparting best practices and organizational models. The other is technical training of the partners and the microentrepreneurs to improve the quantity, quality, and marketability of their products.

As of December 2011, the project had made progress in building the capacity of the partners. For example, seven of the nine local partners were awarded subgrants as a result of completing compliance training. The project also provided extensive technical training to these partners and the microentrepreneurs. For example, a team of international experts provided 5 days of training to 15,000 producers on improved production practices in dairy, embellished fabrics, medicinal and aromatic plants, and 201 female sales agents received training in the basics of business management, product design, and marketing.

Table 1 shows the two key targets for technical training and the corresponding results.

Table 1. Technical Capacity Building for 2011 (unaudited)

Indicator	Target	Result
Number of microenterprises receiving business development services	18,750	23,002
Number of microentrepreneurs trained in the basics of business management and marketing	18,750	14,923

Note: Targets are those shown in the project's latest annual implementation plan for 2011; the results come from the progress report for the quarter ending December 2011.

The 2011 target was to train 18,750 microentrepreneurs in the basics of business management and marketing to improve the quality of the products. The project trained 14,923 people out of 18,750, meeting 80 percent of its target.

During our field visits to 15 locations in Khyber Pakhtunkhwa (where we took the following photo), Punjab, and Sindh Provinces, we found that beneficiaries appreciated the training they received through the project. Further, some beneficiaries said their incomes had increased because of the technical training. In the three sectors reviewed—dairy, embellished fabric, and medicinal and aromatic plants—beneficiaries gave positive feedback about the training and wanted more technical support from the project. Additionally, beneficiaries said that through project interventions they have established contacts with buyers at regional and national levels and are able to sell their products at better prices.



In Khyber Pakhtunkhwa, a woman engaged in the embellished fabrics sector displays a handbag made using a project-provided pattern. (Photo by OIG/Pakistan, December 2011)

Despite the progress in training made thus far, the project faces challenges. According to USAID/Pakistan, the reasons for not achieving the intended target of training all 18,750 microentrepreneurs in business management and marketing are:

- The newness of the value chain concept to the partners and microentrepreneurs and the time-consuming coaching they require on it.
- Lack of familiarity with USAID's requirements for grants compliance, procurement, and monitoring and evaluation.
- Lack of familiarity with state-of-the-art databases used by the project.
- Restricted mobility for women because of local norms.
- Volatile security situation in areas where the project is implemented.

Although the project made progress on its training goals, the areas below need to be improved to achieve the overall project goal of substantially increasing the incomes of 75,000 microentrepreneurs by June 2014.

Project Did Not Measure Change in Beneficiaries' Incomes to Assess Impact

USAID's Performance Monitoring and Evaluation TIPS No. 6, "Selecting Performance Indicators," states that an important criterion for an indicator is its directness, "the extent that it clearly measures the intended result." According to the cooperative agreement, the core objective of the project is to increase the incomes of 75,000 microentrepreneurs. Thus, the primary direct measure of performance is change in income, on which data should be collected periodically to provide timely feedback in management decision making.

Although the project collected baseline income data when registering beneficiaries, USAID/Pakistan did not develop a clear framework to track beneficiaries' income changes. OIG/Pakistan visited 15 locations in various parts of Pakistan from December 20 to December 30, 2011. Beneficiaries said their incomes had increased because of project interventions. However, partners were not collecting data regarding changes in income, even though the data was available. For instance, local milk collectors maintained weekly collection records and amounts owed to beneficiaries. However, this data was not being accumulated and stored by partners. Hence, complete, reliable, detailed data regarding income was not available to project managers to measure progress in increasing incomes of the microentrepreneurs.

The mission has set a target of increasing the incomes of 75,000 beneficiaries. Because during the planning phase of the project, the mission overlooked the need for collecting and measuring changes in incomes, the project lacked a standardized method to collect this information across the four sectors. The lack of standardization may limit the data's value in determining project effectiveness.

Without periodically collecting and recording data on change in income, the project's primary performance indicator, the mission may not be able to make timely adjustments, if needed, to project implementation. Mission officials informed us that they are developing a framework that will track increases in income. This effort will involve hiring an external organization to conduct a survey on changes in incomes of beneficiaries. However, this survey will be conducted only twice: midway and toward the end of the project. This approach by itself may not provide a timely measure of the project's success. For instance, according to the annual work plan, one of the principal goals was to achieve sales of approximately \$1.2 million by the end of 2011; because it did not track and periodically measure the changes in sales, the mission may not be able to determine how much of this target was achieved. To ensure that changes in income can be properly evaluated, we make the following recommendation.

Recommendation 1. *We recommend that USAID/Pakistan develop and implement a process to collect information about changes in beneficiaries' sales and incomes. The information should be stored in a standardized format in a database and be updated routinely so that well-timed project assessments can be performed.*

Project Made Little Progress in Developing the Honey Sector

The 2011 annual implementation plan states that 1,000 beneficiaries should be trained in beekeeping and achieve sales of \$19,200 in 2011. Further, the local partner's subgrant approved by USAID/Pakistan requires identification of 200 community sales agents and 50 lead community agents by January 2012 for assisting beneficiaries in selling honey products.

The audit found that little progress had been made in the honey sector because of the delayed approval of the subgrant by the mission. From the time the local partner was selected by the project in December 2010, it took approximately 10 months for the mission to approve the subgrant in October 2011—more than double the budgeted timeline of 5 months under the 2011 annual implementation plan. Further, the audit noted that from the signing of the contract in October 2011 through February 2012, about 16 weeks later, the local partner issued only two weekly reports, and no substantial work had been performed as of February 2012. Table 2 summarizes the lack of progress made toward some key targets.

Table 2. Lack of Progress in Honey Sector (unaudited)

Target	Results
Formation of 100 interest groups	4
Identification of 200 community sales agents	0
Training of sales agents	0
1,000 skilled beekeepers trained	0

Mission officials informed us that the approval process is lengthy because a thorough evaluation of the local partner is necessary. Value chain development is a relatively new concept in Pakistan, and because of the novelty of this approach in the honey sector, the local partner needed help developing the appropriate subgrant that would comply with USAID policies. Further, the due diligence performed by the agreement officer regarding the partner selection process pushed back the approval of the subgrant. In addition, the local government raised quality concerns regarding tool kits provided to local honeybee farmers by the partner under a previous humanitarian assistance activity. Mission officials stated that, to address these concerns, the project had to provide clarity and additional background information to the mission, thus lengthening the approval period. Mission officials also commented that progress was slow after approval because of a feasibility study that is being conducted to (1) determine the specific cause of the death of bees in the past in the target area and (2) identify which species would be best for small traditional beekeepers to use to achieve the objective.

We believe that the mission should have conducted this feasibility study before deciding to develop the honey sector. Both implementing partner and mission officials agreed that work in the honey sector is lagging and needs to accelerate to enhance the incomes of 1,000 beekeepers through value chain development activities by March 2014.

To address the delay, we recommend the following.

Recommendation 2. *We recommend that USAID/Pakistan develop and implement an action plan to increase the pace of development in the honey sector or redefine or revise the activity objectives.*

EVALUATION OF MANAGEMENT COMMENTS

USAID/Pakistan agreed with the findings and two recommendations in the report. Concerning the report's finding that the project made little progress in developing the honey sector, the mission remarked that the audit might not have accounted fully for challenges in selecting a suitable partner that could operate in the remote areas of Khyber Pakhtunkhwa. We believe the audit fully addresses this concern on page 6 of this report.

Based on our evaluation of USAID/Pakistan's management comments (below), management decisions have been reached on the recommendations.

Recommendation 1. USAID/Pakistan agreed to develop and implement a process to collect information about changes in beneficiaries' sales and incomes. The mission plans to have this process fully functional by October 31, 2012. Accordingly, a management decision has been reached on Recommendation 1.

Recommendation 2. USAID/Pakistan agreed to develop an action plan to increase the pace of development in the honey sector. The plan is to be implemented by August 30, 2012. Accordingly, a management decision has been reached on Recommendation 2.

The Audit Performance and Compliance Division will make a determination of final action on completion of the planned corrective actions for the two recommendations. The mission's written comments on the draft report are included in their entirety as Appendix II.

SCOPE AND METHODOLOGY

Scope

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions in accordance with our audit objective. We believe that the evidence obtained provides that reasonable basis.

The purpose of this audit was to determine whether USAID/Pakistan's Entrepreneurs Project made progress to build the capacity of local partners and expand opportunities for microentrepreneurs. The cooperative agreement for this project started June 2009 and is to end on June 2014. This audit focused on building the capacity of selected partners in value chain development from June 2009 through February 2012. As of December 2011, USAID/Pakistan has obligated and expended approximately \$22 million and \$11.5 million, respectively, for this project.

The audit covered activities from June 2009 through February 2012. The audit team reviewed mission documents concerning project management, agreements, implementation plans, progress reports, the monitoring and evaluation plan and procedures. Additionally, the audit team conducted interviews with USAID/Pakistan project administrators, implementing and local partner officials, and project beneficiaries.

We reviewed applicable laws and regulations as well as USAID policies and procedures pertaining to USAID/Pakistan's Entrepreneurs Project, including Automated Directives System Chapters 200 and 201 and supplemental guidance. The audit relied on the following sources of evidence: the agreement; interviews with officials from the implementing partner, local partners, and USAID/Pakistan, as well as from beneficiaries; and documents maintained at the mission and at the implementing partner's Islamabad headquarters. Audit fieldwork was performed at the USAID/Pakistan mission and the implementing partner's main office located in Islamabad from October 25, 2011, through February 28, 2012.

In planning and performing the audit, the audit team assessed relevant controls used by the mission to manage the project and to ensure that USAID/Pakistan provided adequate oversight of project activities. These controls included maintaining regular contact with the implementing partner and reviewing project files.

Methodology

To answer the audit objective, the audit team interviewed officials in the mission's Economic Growth and Agriculture Office, which manages project implementation; the implementing partner's main country office; and local partners' offices and beneficiaries. Through interviews and documentation, the audit team obtained an understanding of (1) the project's main goals, (2) how performance indicators, targets, and baseline data were determined to measure the progress of the project, (3) how the mission ensures the quality of the data reported by the implementing partner, (4) how the mission monitors the implementation of

activities, and (5) whether the mission is aware of any allegations of fraud or other potential illegal acts or noncompliance with laws and regulations.

To achieve these, the audit team reviewed the agreement and modifications, USAID correspondence with the implementing partner, the 2011 implementation plan, and weekly and quarterly project reports. The audit team interviewed staff from USAID, the implementing partner, and seven of the nine local partners. The audit team judgmentally selected 15 locations and made site visits to Dir and Swat Districts in Khyber Pakhtunkhwa, Sukkur and Larkana Districts and Karachi in Sindh, and Bahawalpur in Punjab between December 20 and 30, 2011, and interviewed the entrepreneurs (beneficiaries) to determine the impact of the training provided under this project.

MANAGEMENT COMMENTS



MEMORANDUM

Date: April 03, 2012

To: Joseph Farinella
Director OIG/Pakistan

From: Andrew Sisson /s/
Mission Director

Subject: Management Comments on the Audit of USAID/Pakistan's Entrepreneurs Project

Reference: Draft Report No. G-391-12-00X-P dated March 16, 2012

In response to the referenced draft audit report, please find below Mission management comments on the recommendations included therein.

Recommendation No. 1 We recommend that USAID/Pakistan develop and implement a process to collect information about changes in beneficiaries' sales and incomes. The information should be stored in a standardized format in a database, and should be updated routinely, so that well-timed project assessments can be performed.

Management comments:

USAID/Pakistan concurs with the recommendation and agrees to develop and implement a process to collect information about changes in beneficiaries' sales and income. In this respect, the Mission is already working with the Independent Monitoring and Evaluation Contractor to develop a standardized database that will be periodically updated. The database would help generate information relating to impact in a timely fashion and on a regular basis. In addition to the detailed survey which will be conducted twice, as also mentioned in the audit report, sample surveys will be carried out on a quarterly basis throughout the term of the project to measure impact and extrapolate sales and incomes increases. This database should be fully functional by the end of October 2012.

Recommendation No. 2 We recommend that USAID/Pakistan develop and implement an action plan to increase the pace of development in honey sector, or redefine or revise the activity objectives.

Management comments:

Mission management concurs with the recommendation and agrees to develop an action plan to increase the pace of development in the honey sector and revise the activity objectives.

The audit report notes that from the time the honey sub partner was selected by the primary partner to the actual award of the grant, it took the Mission ten months to approve the sub-grant. Note that each shortlisted candidate organization has to undergo a process of due diligence by the primary partner during which the organization's internal control, financial and human resource management systems and technical capabilities are thoroughly evaluated and assessed. This process is in compliance with the Mission approved grants manual and is often time intensive. The final sub-grantee is selected based on the recommendations of this assessment. From the call for Expressions of Interests to the signing of the sub-award can take up to 5-6 months. Honey sector under this project experienced further delays due to reasons already mentioned in the audit report. However, in this respect, the Mission would like to note that the audit may not have fully accounted for USAID/Pakistan's efforts to ensure that proper due diligence was performed to select a suitable local partner that would be able to carry out the implementation of a promising but challenging project with the aim to develop the honey value chain in remote areas of Khyber Pakhtunkhwa. There are not many local partners who have the technical capacity to assess the favorability of the physical, agro-climatic, cultural, and overall agricultural situation in Swat and surrounding areas for beekeeping and to identify the requirements needed for a viable beekeeping business. Existing practices of Swat's small traditional beekeepers, production constraints and prevalence of diseases make apiculture a particularly challenging area to work in which also explains slow implementation pace since the start of the project.

The new action plan to increase the pace of development in honey sector will be completed, approved and ready to implement by August 30, 2012.

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