

## INFORMATION THROUGH VOUCHERS: WHAT NEXT, AFTER PARAGUAY?

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### **Introduction**

Economic theory highlights an information problem which helps explain the functional weaknesses of the training market: the extreme difficulty with which potential purchasers of “training” can gauge the quality of training programs in advance. Training is an “experience good” whose merits do not become apparent to the trainees until after they have consumed the good and are able to apply the newly acquired knowledge in a successful manner. Glossy brochures proclaiming the benefits of this or that training program are unable to provide training consumers the necessary information about quality. Such advertisements can make promises, but their proponents are not necessarily able or willing to keep them.

In the free market, however, no training provider would be willing to allow a customer to delay payment of course fees until the course has been completed to his satisfaction. In such a circumstance, what would compel the training customer to pay? After all, upon completion of the course, the trainee has received what he wanted to acquire (knowledge and skills), and therefore has a strong incentive to refuse payment on the grounds of dissatisfaction, regardless of how satisfied he really is with the service provided. Therefore, the only realistic system is to charge fees up front. This raises an additional problem, since usually the potential customer of training will only agree to pay if the risk of buying a training course of unknown quality is offset by a reasonable (low) price. The result: in order to keep prices low, training providers must minimize their costs, which ultimately affects the quality of the training. Thus, the quality is often poor because: the staff is ill paid, ill prepared and insufficiently qualified; the training materials are inadequate; and no additional thought has gone into addressing the needs of the trainees. The phrase “you get what you pay for,” in this case serves to reinforce and confirm the consumer’s preconception that training is of little value and high risk. Finally, the information deficits on the supply side of the training market make *adverse selection* likely, and in extreme cases, can lead to the total breakdown of the training market.

The information problem -- namely that training providers cannot credibly demonstrate the quality of their services in advance, nor can customers confirm their willingness to pay -- has led to an overall underinvestment in training. This is a problem which often the state is compelled to address, typically through the use of permanent supply-side subsidies..

Subsidies, however, are not necessarily the panacea for such market imperfections. Subsidies can induce training providers to offer training despite lack of demand for it, but subsidies do not necessarily prevent providers from offering poor quality courses. An effective instrument, therefore, would not only promote investment in the training market, but also reduce the

information gap, improve quality control, and be sustainable in the long term while minimizing the risk of fraud.

In an attempt to overcome problems related to underinvestment in the training market, programs have often oversubsidized supply (training providers), with the implicit assumption that through this intervention the information deficit on the demand side is also addressed. This underlying assumption, that both program designers and training suppliers understand the needs of microenterprises, has been a critical fallacy of many past designs. The reality is that information is lacking on both the demand and the supply sides of the market equation.

One final, and important, consideration in examining new approaches to microenterprise training market interventions, is that the externalities argument is not really applicable to the small and micro entrepreneurial training market. Experience has shown that when the relevancy and adequacy problems of the training products supply are addressed, the resulting transactions should, and can, be considered as transactions of wholly private goods: assuring that the benefits of the training be totally appropriated by the trainee is an entirely possible result of good product design. There is therefore only a limited rationale for subsidization, which should in fact be geared towards the development and deepening of an ultimately sustainable private training services market.

In the next few pages the specific problems and pitfalls encountered by previous supply-oriented programs are analyzed. Subsequently, a new approach to microenterprise training is described, which uses an information system associated with vouchers. The concluding section highlights the challenges still facing this approach, and touches on expectations for future program interventions.

### **Problems and Pitfalls of Traditional Supply-Oriented Programs and Interventions**

When Latin American training institutions were created, the problems of training were mostly on the supply side. The market would hire as many graduates as schools could produce and trainers were concerned with training materials, training of trainers, and funds to pay for increasingly large and heavy systems. The economic troubles which started with the oil crisis in the seventies and culminated with the “lost decade” of the eighties changed forever the landscape of training.<sup>1</sup> The biggest challenge in recent times has been finding a good fit between supply and demand, not simply increasing supply to meet excess demand.

Even now, most course offerings of the large training institutes created throughout Latin America remain tailored to large enterprises with greater specialization of functions, complex divisions of labor, and technologically more advanced processes.<sup>2</sup> Instead of offering practical training, one may more accurately describe these programs as consisting of an extension of the traditional concept of technical education, the curricula of which are suitable only for persons who are planning to take up positions in large-scale industry. Furthermore, because the courses are in fact

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<sup>1</sup> “The Stubborn Trainers Vs the Neo-liberal Economists: Will Training Survive the Battle?” Claudio de Moura Castro, Inter-American Development Bank, 1997.

<sup>2</sup> Ibid.

excerpts from an advanced technical education - rather than job-specific training - the examples used to transmit skills are foreign to the everyday reality of small or micro entrepreneurs. Finally, the organizational framework of the courses takes no account of the preferences of adults already working in full-time occupations: courses are too long and are scheduled at an inconvenient time of day. As a result, only a negligibly small number of microenterprises are able to capitalize on this type of technical training in any truly meaningful way. The majority of small entrepreneurs have no profitable use for it, and they are therefore not willing to take part in such courses, even when they are offered for “free”.

Some Latin American governments have developed a model for public vocational and technical education and training systems that aspires to assure the relevancy and adequacy of its products through the creation of tripartite technical school boards, which include representatives of government, business, and labor. Unfortunately, experience has shown that the market information that can actually be channeled through the business sector representatives to the board is extremely limited. The actual supply of courses by these institutions ends up addressing - in the best of cases- the demands of the more vocal and active business sectors, and furthermore tends to be expressed as a function of the specific capabilities, experience and interests of the school faculties. The tremendous variability and diversity of the actual training needs of small and micro businesses just cannot be addressed through such a centralized institutional arrangement.

A more recent supply-oriented subsidization approach has made some strides in promoting competition among training providers, although the program still falls short of developing an efficient, sustainable market. In Chile second-tier organizations, such as local government agencies, establish criteria and prerequisites for training providers to qualify for participation in their subsidized microenterprise-focused training program. Accepted training providers then compete with one another in a course-by-course tendering process. This intervention ultimately works under the assumption that the second-tier organizations know the ever-changing needs of the microentrepreneurs. Information about the training needs of microenterprises may in fact be readily available to the training providers individually, but it is rarely filtered up to the second-tier organization that makes decisions about curricula and training provision for the program. The model assumes that the crucial dimension for satisfaction of the target group training needs is price, and thus makes no allowance for demand to express its concerns regarding the other training product dimensions -contents and modalities-, which are pre-determined by the second-tier institution. The apparent market-orientation of this approach is therefore restricted to price-competition (though it is not exempt from oligopolistic price formation), with little allowance for competition regarding quality of products.

In the centralized tendering model the actual buyer of the training product is the second-tier institution, and not the entrepreneur. This produces several sub-optimal effects : a) it promotes the specialization of suppliers as providers to the second-tier institution and not to the entrepreneurs themselves (it promotes tendering capacities rather than demand-identification and marketing capacities) ; b) the second-tier institution substitutes for the entrepreneurs as clients, thereby preventing their learning process in acquiring training products and in negotiating product adequacy ; c) the purchase of training products in a centralized and aggregate manner ultimately distorts market prices.

## **The Paraguay Experience**

In 1995, the Inter-American Development Bank (IDB) financed a pilot information system and voucher training program targeting microenterprises in Paraguay. The program was experimental in nature, designed to accompany an IDB Global Microenterprise Loan, which focused primarily on attracting formal financial institutions to microenterprise lending, through a technical assistance package and a line of credit available on commercial terms.

This information system and voucher training program was conceived with the aim of overcoming the market imperfections cited above, as well as some seemingly intractable problems the IDB had encountered when financing training initiatives for microentrepreneurs in the past. Typically, training had been obligatory, linked to credit allocation, and focused on general accounting and business principles. Courses were often taught by NGO credit staff with little knowledge of the business world, and all entrepreneurs were grouped together regardless of sector or level of knowledge. As could be expected, classrooms were empty; when pressured, some entrepreneurs sent family members or other, less busy individuals to attend the training. Results were measured by number of courses given and people trained, rather than by whether skills learned were applied. It was inconceivable for courses like this to recover costs directly (although some training operations were financed through credit revenues), simply because what was being offered was not demanded by microentrepreneurs. Financing institutions like the IDB at times tried to select one institution over another to provide training, without really knowing what entrepreneurs wanted or needed.

The information and voucher program turned this situation on its head. It produced an unprecedented response from the market, both from training suppliers and from microenterprise owners and employees interested in training. The program operated independently from the larger microfinance loan of which it was a part, without discriminating between loan clients of the IDB Global program and the wider Paraguayan microenterprise sector.<sup>3</sup> Preliminary results show that the program helped to develop a private sector training market which offers products appropriate for a microenterprise clientele. Clients demonstrated that they wanted to learn specific, immediately applicable skills, and wanted courses broken up into short, easily digestible modules. Once suppliers had gotten the message and adapted their products, demand from microentrepreneurs was strong, even with a required out-of-pocket contribution. Most importantly, the program altered the balance of power in the training market, by increasing microentrepreneurs' buying power. Entrepreneurs armed with both information and vouchers could choose what they wanted to learn, when, and from whom. This new dynamic forced training institutions to compete with each other in order to attract clients, and to innovate constantly in order to keep up with a highly cyclical and rapidly evolving demand.

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<sup>3</sup> In fact, program records show that less than a third of voucher training clients were borrowers of the Global program. Approximately another third had obtained credit from another source (usually local credit unions), and the remaining third did not use credit. This is important evidence of the fact that the market for business development services overlaps with, *but is not the same as*, the credit market.

As of early 1999, the IDB has approved one attempt to replicate the voucher experience in Ecuador, and is considering additional proposals from Guyana, El Salvador, and Brazil. In addition, the World Bank has reformulated a voucher training program in Kenya, using lessons from the Paraguayan experience. The European Union financed a voucher program in Peru, which encountered significant organizational and execution problems. The Peruvian Ministry of Industry is considering a second stage, in which project design would be influenced by lessons learned in recent years.

### **How the Model Works**

The key characteristic of this new approach is its multi-dimensionality: it addresses the information problems at the root of training market underdevelopment, while injecting a demand-oriented, partial subsidy that seeks to jump-start investment in product development by existing suppliers, thus setting the stage for a more competitive marketplace, and attracting new microenterprise clients.

The program sequence is as follows:

Prior to acceptance into the multidimensional program, training providers are screened based on the following prerequisites: legal recognition as a training institution, one year or more experience in training microentrepreneurs, and the existence of adequate facilities, materials and staff to conduct the training. Once accepted into the program, training providers must also agree to unscheduled audits and evaluations. These audits serve as an important measure to minimize fraud, while at the same time they provide information to potential trainees, through the information and referral component of the program. The roster of institutions remains open during the execution of the program, with the understanding that new market entrants tend to place pressure on the leading training institutions to keep innovating.

This information and referral service, while also functioning as a voucher distribution center, provides information on the content, locations, providers, and quality of training. Training providers are ranked monthly according to how many program clients chose their courses, and clients are able to review the results at the centers. Thus, clients have the opportunity to see which courses are most popular with other entrepreneurs, information which is an indication of the relevance and quality of the courses. Most microentrepreneurs hear about the program by word-of-mouth, but advertisements for the program have also run on the radio and in local newspapers. Training institutions also provide information in an attempt to recruit new students.

Entrepreneurs obtain a limited number of vouchers from the voucher distribution center. Vouchers have a fixed monetary amount and may be used by microentrepreneurs to offset the cost of a training course of their choice. Entrepreneurs pay the difference between the cost of training program and the voucher's value. The only restriction is that microentrepreneurs must use the vouchers at institutions officially registered with, and rated by, the program. An out-of-pocket contribution by the microentrepreneur is required in all cases, with course prices ranging from double or triple the voucher amount to just twenty-five percent over the voucher's value. In Paraguay, for example, the voucher's value was set at US\$20 and the least expensive courses were \$25 each. Setting the voucher at an absolute amount rather than a percentage favors the

lower-income microentrepreneurs who may not have more than US\$5 to invest in training. Note that if the voucher value in Paraguay had been defined as 50% of the course price, this would have forced all entrepreneurs to contribute at least US\$12.50, while entrepreneurs choosing to take more expensive courses might have received up to US\$35.00 in subsidy.

Quality and information are controlled via the market in a number of ways:

- First, training providers are not entitled to submit the vouchers to the program for exchange into cash until the customer has completed the course; and even then will only receive reimbursement for those customers who attended at least 75% of the course. The program operates under the assumption that the trainee will only complete the course if he or she is satisfied with the training provided. Because the system operates on a voluntary basis only – unlike “past” programs where training was mandatory -- training providers are compelled to be responsive to the needs of their customers. Unsatisfied training consumers will most likely choose not to attend 100% of the course and therefore the voucher portion of the payment will not be received. On the other hand, the customer’s co-payment (fee over and above the amount of the voucher) must be made at the beginning of the course. Whereas the providers of training would incur a “default risk” if individual consumers were to promise to pay after receipt of services, no such risk exists within the voucher system because the program guarantees that the voucher will be exchanged for cash, conditional on satisfactory provision of the service.

Thus, the design of the program succeeds in providing support at precisely the points where the market needs help in order to function properly. The control mechanism of *ex post* payment can be introduced without imposing an intolerable burden on the providers because payment is covered by a government guarantee, as long as minimal conditions are fulfilled. Yet at the same time, control is largely exercised by those who are best able to do so, namely those who attend the courses, the consumers themselves. It would be very difficult for such broad based and “expert” control to be achieved by a centralized watchdog, which would at best be able to conduct spot checks.

- Second, the program – again, as distinct from traditional programs—uses competition between providers in the training market as a control mechanism. The microentrepreneurs are free to decide for themselves which of the recognized training institutions to enroll at, and which courses to use their vouchers to pay for. Thus, each training institution has an incentive to distinguish itself from its competitors in order to attract as many customers as possible. Clearly, the model provides a new financial incentive for all the institutions, and forces them to adapt their training product to the needs of their customers. In practice, this means providing courses in the evenings and during weekends, and also providing hands-on practice sessions from which microentrepreneurs can bring saleable skills back to their businesses. Providers do their best not to make empty promises, not only because their clients would drop out midway through the course if they did, but also in hopes that recommendations from satisfied customers will bring future business.

## **Results of the Paraguay Program**

The Paraguay program was executed in two phases, a demonstration phase, lasting two years (from May, 1995 through May, 1997) and a pilot phase, lasting from February to December, 1998. The two-phased execution was not intentional; rather, it was the result of political pressures in Paraguay and administrative complications within the IDB. The interesting result, however, is that data exist on the performance of the four leading training institutions during the program's stoppage (June, 1997 through February, 1998). These data, compared with anecdotal evidence about these institutions' performance before the program began, tell an interesting story about the voucher program's impact on the training market.

Table 1 below shows the number of vouchers redeemed per month during the program's two execution periods. The pattern which emerges is that of strong growth, with seasonal peaks and troughs, in voucher use throughout the program's life. It is worth noting that the May, 1995 starting date represents only the date that vouchers were first issued - the program required a significant gestation period during which participating institutions were recruited, administrative systems were set up, and the program was advertised. The second phase was able to "take off" faster, since a loyal client base and a critical mass of training providers already existed. Although the second phase was less than half as long as the first phase, the total number of vouchers redeemed during the second phase was higher (29,264 as compared to 19,287 during the first phase).

Also important to note is the pattern of increasing numbers of non-voucher trainees, during both phases of the program. In most cases, non-voucher participants were not microentrepreneurs, and thus did not qualify to receive a voucher. Housewives and students commonly purchased the training services offered through the program. Some non-voucher participants, however, were first-time trainees who did not know about the program; a few were also microentrepreneurs who had exhausted their quota of six vouchers, yet wanted to continue purchasing training.

**-Insert Table 1 -**

The peaks and valleys in the chart show the seasonal, cyclical nature of the demand for microenterprise training. Voucher usage tended to peak right before the Christmas and Easter holidays, times when microentrepreneurs wanted to learn how to offer new, seasonal products. The non-voucher participants represent a more stable market, growing gradually as supply expands.

During the first phase of the Paraguayan program, the number of training institutions participating started small and grew to reach over sixty. Of these sixty, about twenty participated actively, i.e., redeeming significant numbers of vouchers every month. During the second phase, the number of registered institutions was even larger, although the core participants again numbered between fifteen and twenty-five each month, rising as the program progressed. The leading training institutions, defined as those which redeemed the greatest number of vouchers, were typically small, private, for-profit operations. Directors and instructors were often owners of small businesses themselves, willing to share a few trade secrets with microentrepreneurs who they knew weren't close enough to them to challenge their market share. For some institutions, training used to be a side activity performed for extra income. Once the program provided a financial incentive in the form of vouchers, many providers expanded and invested in their training activities. Most were forced to adapt their training products to the needs of a microenterprise clientele - shortening course length, scheduling training sessions on week-nights and weekends, simplifying teaching methodologies, and relying more heavily on hands-on practice sessions.<sup>4</sup>

Another key development was the wide variety in course content which became available. Within sectors, large numbers of extremely specific courses were offered, and even the number of sectors multiplied as the program progressed. In Paraguay, the course content breakdown during 1998 was as follows: 17% management (accounting, costs, quality control, taxes, etc.); 14% decoration (cotillion arrangements, painting, serigraphy, household repair); 14% textile assembly (fabrics, pillows, clothing, etc.); 13% electricity; 11% culinary arts; 7% electronics; 7% hairdressing, and 2% each for refrigeration, handicrafts, cosmetology, shoemaking, plumbing, auto mechanics, and carpentry.

Several institutions were active in both the first and second phases of the program. During the program stoppage (June, 1997 – February, 1998), data were collected on three of the voucher program's leading institutions: the Instituto Central de Electrónica (ICE - training in personal computer repair, household appliance repair, and other electronic topics); the Instituto de Arte Culinario Maria Gloria (IMG - baking), and the Centro de Enseñanza Profesional (CEP - hairdressing and hair salon management). These data are presented in Table 2 below, along with information about the institutions' performance before the voucher program was initiated and data collected during both phases of the voucher program.<sup>5</sup>

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<sup>4</sup> See Part II, Case Study: The Paraguayan Voucher Training Program in "Preliminary Results and Case Studies on Business Development Services for Microenterprise," Microenterprise Unit, Inter-American Development Bank. Washington, DC; February 1997.

<sup>5</sup> It must be emphasized that the data presented here represent "snapshots" of the training institutions taken at four distinct moments in time. The first, second, and fourth moments (August '95, July '96, and September '98) represent relatively similar periods in the seasonal microenterprise training cycle. The third moment (November '97) is closer to the pre-Christmas peak and for this reason may show a higher volume of activities than average.

**Table 2. Indicators from three training institutions**

Key Indicators	Before joining voucher program (8/95)	During phase 1 of voucher program (7/96)	During program stoppage (11/97)	During phase 2 of voucher program (9/98)
Number of students/month	ICE – 50 IMG – 12 CEP – 15	ICE – 154 IMG – 12 CEP – 156	ICE - 54 IMG - 15 CEP - 208	ICE - 55 IMG - n/a CEP - 140
Number of courses/month	ICE – 4 IMG - 1 CEP – 1	ICE – 14 IMG - 5 CEP – 7	ICE - 11 IMG - 4 CEP - 7	ICE - 7 IMG - n/a CEP - 6
Course duration	ICE – one year IMG –one year CEP – two years	ICE - 16 hours IMG -16 hours CEP - 15 hours	ICE - one month IMG -16 hours CEP - 15 hours	ICE - 18 hours IMG -n/a CEP - 18 hours
Price of course	ICE -n/a IMG -n/a CEP - n/a	ICE - US\$26 IMG -US\$37 CEP - US\$57	ICE - US\$26 IMG -US\$40 CEP - US\$35	ICE - US\$35 IMG -n/a CEP - US\$28

The chart illustrates a clear shift on the part of the three institutions from long-term, full-time training courses to shorter, more accessible modules, with a greater variety in course topics. Prices, on the other hand, tended to move up and down depending on market conditions. The data show a significant expansion in the volume of trainees during the first phase of the voucher program, which was not sustained over the next few years. All three programs survived, however, when the supply of vouchers were cut off in May 1997; but only two of the three programs remained active in the training market throughout phase two of the voucher program (ICE and CEP). Interestingly, these two were programs which had possessed significant experience in the training field prior to the initiation of the voucher program. The third institution, IMG, was a start-up with limited experience in training, surviving primarily through its bakery sales. Although IMG did continue to offer training for some time after the end of phase 1, the enterprise turned back towards baking sales in order to generate revenue as the training market weakened. As courses attracted less students a decision was made to raise prices; this in turn led to even lower demand for the courses.

Table 3 shows the average course price over the life of the program. The clear downward trend is probably due to the fact that many institutions had to make an initial investment in the re-adaptation of their course materials and content, teaching methodologies, and delivery strategies as they reached out to attract a new clientele. Once this investment was recuperated, institutions were able to lower their prices in an effort to compete for additional clients. Stronger competition was present in the second phase of the program; records show that new training institutions entered popular sectors like electronics and baking, adding to the variety and number of courses available.

### **-Insert Table 3-**

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Although limited, this information is presented because it offers a glimpse into the workings of the microenterprise training market at times when it was unsubsidized.

A more detailed set of data from phase one of the program shows, however, that during any given month of operation, the least expensive courses were not necessarily the most popular.<sup>6</sup> Institutions with good reputations were able to charge a premium for their services. In addition, some courses were more expensive due to their content and to the materials required. Courses in electronics and baking, for example, tended to be expensive while business management courses usually cost less.

The subsidy level of the program was tracked throughout phases one and two, measured as the total value of vouchers redeemed over the total value of sales for those training products eligible for the program. For example, if Instituto Maria Gloria charged US\$30 per person for one course, trained 18 students, and collected 14 vouchers for US\$20 each, the subsidy level for that particular course would be  $(14 \times 20) / (18 \times 30)$ , or approximately 52%<sup>7</sup>. Table 3 below shows the evolution of the subsidy level over the program's history.

**-Insert Table 4-**

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<sup>6</sup> Goldmark et al, 1997, Table 21.

<sup>7</sup> To be completely accurate, adjustments would have to be made for the institutions participating in the program, which received operational subsidies in addition to voucher income. During phase 1, these were: MICROS, a credit-NGO which offered management and tax courses, and SNPP (Servicio Nacional de Promoción Profesional), which offered business management courses. In phase two, MICROS was no longer present, but SNPP continued to participate and a few other NGOs joined the program.

A clear pattern of increased subsidy is evident during phase two of the program. This could indicate that participant institutions had become adept at “capturing” the subsidy, i.e., deriving maximum voucher income from courses by attracting large numbers of voucher holders. Another plausible explanation is that the microenterprise community was better informed about the program’s existence during phase two. On the one hand, this demonstrates a positive market phenomenon, where the object is to cater to the demand of a large microenterprise clientele. Part of this demand may include pressure to keep prices low. On the other hand, this pattern does not bode well for the sustainability of the program after the vouchers have run out.

In the original design of the Paraguay program, the idea of reducing the vouchers’ nominal value over time had been discussed, but this measure was never carried out. Due to inflation, however, the voucher’s real value did decrease. The voucher was fixed at 40,000 guaranies, equal to about US\$20 at the start of the program’s first phase, and equal to about US\$15 at the end of the second phase.

In any case, the results shown in Table 4 above would seem to imply that a more active effort to reduce the nominal value of the voucher might be a healthy thing. In the Paraguay case, the program ended in December 1998. It is too early to tell whether the training market which developed as a result of the program will continue to function, and whether the microenterprise clientele will continue to demand services. The data collected during the stoppage in 1997 is interesting, but too scanty to provide a basis for firm conclusions.

### **Control and Supervision**

Within and outside the IDB, and due in part to the existence of failed and incomplete voucher programs, there has been an exaggerated perception of the potential for fraud. One clear lesson from the Paraguay case was that while infractions of the rules will occur, the frequency and impact of these infractions can be effectively minimized through a combination of mutually reinforcing supervision and control mechanisms. These mechanisms are implemented by the executing agency or unit which administers the program, independent consultants, and the training institutions themselves. The checklist below (Table 5) shows how the Paraguay program was kept honest.

The importance of a capable, and politically independent executing agency became clear when in Paraguay, several institutions had to be disqualified from participating in the program. Unhappy directors of training institutions tried to rally political support and put pressure on the voucher program administration unit to give them one more chance. An important factor in the success of the program was the fact that the Paraguayan executing unit was granted the autonomy to make these types of decisions on a purely technical basis, free from interference from interest groups. A

small non-governmental organization (NGO) in a Latin American country wishing to execute a vouchers with information training program could run up against difficulties precisely because of this issue. On the other hand, government agencies could just as easily fall prey to political influence and might not be the ideal executing institution either. The question of what type of executing institution has the capacity to impose “rules of the game” on the training market in a given country is one without an easy answer, and has represented a challenge to program designers in every country.

**Table 5. Control and Supervision Mechanisms**

<b>Control Mechanism</b>	<b>Method of Implementation</b>
1. Screening of training institutes. Criteria include adequate facilities, experience in training, courses which are eligible for inclusion in program.	Signed contract with each institution establishing clear rules and norms.
2. Client screening at time of voucher distribution.	Interview in which client is asked to give information about his/her business, including sales, supplies, credit, etc. This information can be correlated to form a picture which would be hard to invent if one did not own a business. When available, receipts and tax forms are requested.
3. Client signature on back of voucher.	Clients are asked to show identification and sign voucher in the presence of administrator. Training institutes are required to confirm the client’s identity and signature at the beginning of each course.
4. Attendance records	Training institutes are asked to confirm participants’ attendance. If microentrepreneurs attend less than 75% of the course, the training institute will not be able to redeem the voucher.
5. Surprise visits to training institutes.	Program administrators appear without warning during courses; verify course content, participants, and quality. In addition, participants may be asked to fill out evaluation forms.
6. Disqualify institutes from participating.	This last resort measure is taken only after participating institutes have been warned that their performance does not comply with program standards.

### **Other Voucher Programs - Peru**

A program using vouchers to finance training for microenterprises was initiated in Peru in 1993, before the Paraguayan program even began. The Peru program did not produce very positive results, due to both design flaws and organizational difficulties.<sup>8</sup>

<sup>8</sup> Source: interview with IDB country office specialist in Lima, Peru. Background interviews with Peruvian officials responsible for managing the voucher training program.

The Peruvian program operated on the following principles:

- vouchers were distributed only to credit clients of a European Union funded program,
- voucher amounts were defined as a percentage, from 50 to 80% of training prices,
- limited fraud control practices were developed,
- products eligible for financing through vouchers were training and technical assistance, and
- publicity for the program was mainly carried out by two agents: credit officers and training providers.

As mentioned above, evidence from Paraguay showed that the microenterprise training market overlaps with, but is not the same as, the microcredit market. From the beginning, then, the voucher program in Peru could only target a fraction of the microenterprise market for training and technical assistance, since vouchers were only made available to credit clients. The credit link was even more problematic, since loan officers tended to recommend “strongly” that microentrepreneurs accept and make use of the vouchers. Entrepreneurs who had participated in obligatory training before understood that they were to attend courses in order to better their chances of receiving a loan.

The other main information and publicity agents in the Peru voucher program were the training providers themselves. This caused a collusion problem, where dishonest trainers would collect vouchers from a number of microentrepreneurs and cash them in, without any training ever actually taking place. Apparently a significant “secondary market” developed, where vouchers were transferred and even sold from one individual to another. On the one hand, this phenomenon may not have such negative implications, in the sense that the secondary market may have allowed other microentrepreneurs who were not using credit to participate in the program, thus correcting the design error in targeting too narrow a group. On the other hand, in cases where the secondary users of vouchers were not entrepreneurs at all (housewives and students, for example) this could be quite problematic. Non-entrepreneurs, armed with increased purchasing power, would then communicate to training providers their own needs, and the dual objectives of making training accessible to and appropriate for microenterprises could no longer be achieved within the context of the program. In the worst case scenario, without fraud and quality control mechanisms, one can imagine the program spinning out of control totally and offering courses such as aerobics and English. While the Peru program did not deviate this far from the planned path, the problem was serious enough to be recognized by administrators as a major concern. In addition to these problems, it is also possible that the “percentage” value of the voucher encouraged the reporting of high course prices, to maximize voucher income.

The Peru program faced heightened difficulties in fraud and quality control - especially for non-standardized products like technical assistance. While a robust inspection program can easily eliminate the possibility of fraud by verifying the delivery of training courses, the delivery of individualized technical assistance is much more difficult, and costly, to control.

Even with the problems described above, the voucher program was perceived by Peruvian officials to have an overall positive impact on the training market, and the possibility of a second, more tightly controlled phase is being explored.

### **Other Voucher Programs - Kenya**

A World Bank training program in Kenya, originally approved in 1995, has been recently reformulated to include a voucher program for small and microenterprises. The Jua Kali Program supports the provision of both training and technical assistance. Whereas the Paraguay program operated with a one-size-fits-all voucher, the Kenya Jua Kali program offers several different types of vouchers to subsets of the overall target group. The two main target groups are small firms in manufacturing and productive services, and women start-ups and other microenterprises.

The broad outlines of the Kenya program's design follow the principles illustrated in the Paraguay case, with a few differences. An eight-page application and the requirement that entrepreneurs have a fixed business premise, represent a hurdle which, by Paraguay standards, seems excessive. The purpose seems to be to limit fraud and screen out entrepreneurs only marginally interested in receiving services. The program also has adopted a percentage basis for calculating the support to be offered through the voucher. As mentioned above, the Paraguay experience demonstrated that the fixed-value option makes the program more accessible to the lowest-income microentrepreneurs. In addition, as noted in the Peru case, using a percentage-value may encourage artificial price increases. On the other hand, the policy adopted in Kenya of reducing the subsidy offered for repeat vouchers is a new innovation, which may enhance the program's sustainability.

Results from a pilot program and the first phase (a total of 4,442 vouchers), show that the vast majority of clients tend to be women start-ups and other microenterprises, interested in purchasing sector-specific, technical skills training. Technical assistance vouchers for small enterprises have catalyzed a far less dynamic market response.

As in Paraguay, suppliers of training in the Jua Kali Program tend to be private, for-profit providers, often business owners with practical experience and tips to offer. The program has tapped into a dynamic apprenticeship system in which mastercraftworkers accept young, inexperienced workers in their workshops, to train them. These same trainers are now offering their services to a larger number of entrepreneurs in smaller, easily digestible chunks, and earning a significant financial return. World Bank project staff report that some trainers have even abandoned their original business activities in favor of more profitable training opportunities.

Both the Kenyan and Paraguayan programs raise serious questions about the sustainability of a training market directed primarily at low-income microentrepreneurs. In both countries the voucher programs seemed to fuel the growth of a formerly invisible mini-training economy. While the results of the training seem to have a favorable impact on microentrepreneurs, the question of the impact of the program's end on the training economy should not be disregarded.

### **Other Voucher Programs – El Salvador**

In the Latin American region, several incomplete voucher programs have been put into practice, with disappointing results. One example is the experience of FOMMI (Fomento de la Microempresa), a European Union-funded project which has built a quite successful microfinance support program in El Salvador. An attempt to offer training vouchers to the program’s credit clients, however, did not produce the desired results and was discontinued.<sup>9</sup> The absence of adequate supervision and control mechanisms and the failure to negotiate clearly the “rules of the game” with the many actors in the training market limited the programs’ impact on the market. In fact, only a limited number of training institutions were included in the program’s roster (less than fifteen). The results speak for themselves: of 1000 vouchers distributed to credit clients, only 100 were used. Entrepreneurs were given no orientation on the available supply of courses. Courses eligible for voucher support did not change their schedules, content, or teaching methodologies to adapt to the needs of the microenterprise clientele. Many microentrepreneurs passed the vouchers on to family members (often, young adults) who then used them to attend computer courses. This experience illustrates the necessity for the information component, which orients microentrepreneurs to the new market in which they are participants. In addition, it raises the question of whether there is a minimum “size” which a voucher program must attain, in order to be able to have an impact on the market. In a region with more than forty active training providers, for example, a program which only includes ten will no doubt have limited impact.

### **Newer IDB Initiatives in Latin America and the Caribbean**

The IDB has received proposals to finance voucher training programs in many Latin American and Caribbean countries. These proposals seem to have originated in a variety of ways, including visits to Paraguay and the reading of the first case study published on the Paraguayan program. Some proposals, such as in the Haitian case, were unrelated to the Paraguayan program and aim more broadly to reform the country’s entire human resources development system by introducing market mechanisms, including the use of vouchers. Others, such as the Ecuador program, were closely modeled on the Paraguayan experience, with an attempt to incorporate lessons learned. Table 6 below shows the status and nature of several newer proposals presented to the IDB for analysis. Note that while some have been approved and should begin to show results soon, others are tentative and may end up as different types of programs entirely. With the exception of the Paraguayan program, none of the voucher programs listed here are advanced enough to provide data on results. Those already approved are still completing the lengthy international bidding and hiring process required of IDB projects. Within a year, some preliminary statistics should be available for the Ecuador and Argentina programs.

**Table 6. Newer IDB Initiatives**

Country	Executing Agency	Stage	Comments/Issues
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<sup>9</sup> Interview with program manager.

<b>Paraguay</b>	<i>First phase:</i> Central Bank and Ministry of Industry. (public) <i>Second phase:</i> Ministry of Labor and Ministry of Industry. (public)	Completed.	Model for subsequent efforts. Was very inexpensive to administer and did not support supply upgrading.
<b>Ecuador</b>	National Financial Corporation. (public/private second-tier bank)	Approved; beginning operations.	Based closely on Paraguay experience but includes component to finance supply upgrade.
<b>Argentina</b>	Economic Development Agency of Cordoba. (public/private partnership)	Approved; beginning operations.	Drew from Paraguay lessons; implemented with the Municipality of Cordoba.
<b>Venezuela</b>	Ministry of Labor and Social Security. (public)	Approved; beginning operations.	Significantly different from Paraguay model. Program for downsized public sector workers offering extensive orientation and counseling. Training vouchers provided after a competency analysis is performed.
<b>Guatemala</b>	Chamber of Industry of Guatemala. (private)	Early design phase; nearing approval.	Vouchers to be used primarily for technical assistance to small and medium businesses, with some related training activities.
<b>Nicaragua</b>	Nicaraguan Institute for Development. (private non-profit)	Early design phase; nearing approval.	Vouchers will be used for training and technical assistance to micro, small and medium-sized enterprises; plan is to phase them out over time.
<b>Guyana</b>	Guyana Volunteer Consultancy. (private non-profit)	Early design phase; nearing approval.	Main challenge is designing the exit mechanism; one risk is the small number of suppliers.
<b>El Salvador</b>	To be defined. One private non-profit candidate.	Early design phase.	Targeting a rural, underdeveloped region; vouchers may not work in this context.
<b>Brazil – Pernambuco</b>	State Ministry of Planning and State Development Agency. (public)	Designed; pending approval.	Aim to attract coastal training suppliers to interior of the state. Plan to phase out vouchers included.
<b>Brazil - other locations</b>	Two proposals: one public, one private non-profit.	Proposed; not analyzed yet.	Model would need to be adapted to fit the Brazilian context; important BDS actors such as SEBRAE currently play a dominant role in market.
<b>Haiti</b>	State Training Agency and Private Training Association. (public/private partnership)	Delayed due to government complications.	Aims to reform entire human resources development system; microenterprise training would be only one component.

In some cases, such as Paraguay, Venezuela, and Brazil, these agencies have been public institutions, which do not themselves offer training services. In Ecuador, Argentina, and Haiti, the

programs will be executed or by institutions which represent both public and private actors. In Guyana, Guatemala, Nicaragua, and possibly El Salvador, the program will be executed entirely by a private actor. Experience thus far has shown that the most important characteristics to look for in a capable executing agency may not be directly related to its legal status. Instead, the most important attributes which contribute to an institution's ability to successfully implement an information system and voucher training program are related to administrative and financial capacity and credibility in the marketplace. A brief list of the criteria used in designing the above-mentioned IDB projects follows:

- Organizational and administrative capacity to carry out the three main activities involved (information referrals and client orientation, distribution and redemption of vouchers, and implementing a supervision and control system),
- Financial capacity, to assure smooth project execution and in order to contribute in-kind or in cash to the project activities,
- A clear separation between the technical and political leadership of the institution (to guarantee a politically "neutral" position, but one ready to fight for what is technically correct),
- Capacity to convene members of the business sector, particularly the target group, and
- Capacity to maintain dialogues with policymakers in the public and private sector, especially those active in the training sector.

### **Future Challenges and Questions**

The information system and voucher training model described in this paper has changed the balance of power within the microenterprise training market, offering greater information to potential purchasers of training, and enhancing microentrepreneurs' purchasing power and ability to voice their preferences to training providers. Equipped with a heightened understanding of microentrepreneurs' needs, training institutions are increasingly competing with one another through constant innovation in their products and services, which in turn increases demand volume, makes the market more attractive for new training suppliers, and thereby creates increased competition, in a "virtuous" circle that expands and deepens the market.

An important lesson learned thus far is the need to design and implement robust fraud and quality control systems, integrated with extensive information services which serve to orient the microentrepreneurs. Three important challenges and questions remain, however: the question of whether there is a need to support the product adaptation and upgrading phase of market development; the elusive question of program sustainability, and the importance of finding a credible, impartial institution to administer the voucher program.

The question of whether to support product development has arisen in newer voucher programs, especially those where the training market is extremely underdeveloped. The rationale for subsidizing this process would be that the same type of information problems which prevent microentrepreneurs from purchasing training in the first place, prevent small training institutions from investing in technical assistance which could help them offer better products, using new didactic methods or materials. The Paraguay program contained no incentives or financing for

institutions wishing to invest in product development. Institutions were expected to invest in new teaching methodologies or materials themselves, because they wanted to compete in the market. This laissez-faire strategy worked in some cases and didn't in others. In general, the institutions with considerable prior experience in training understood that if they were to develop a sustainable competitive advantage in the microenterprise training market, they needed to invest substantially in research and development. Start-up training institutions, which came from a business background, sometimes invested in physical infrastructure such as chairs and video projectors; but these institutions did not always understand the importance of intellectual leadership and constant innovation in training content and delivery. Even in cases where institutions were willing to invest in product development, however, information about how to upgrade their course offering was not always available in Asunción, Paraguay.

The Paraguay program managers, hired as consultants to design the Ecuador program, suggested that a substantial amount of resources be allocated towards a grant fund which could be accessed by participating institutions wishing to invest in upgrading their microenterprise training products, or conduct research in this field. After several discussions, the amount was reduced, in order to make sure the majority of resources were allocated towards the voucher fund. This decision was taken for fear that an over-dimensioned grant fund would upset the delicate demand-side balance that should be present in any voucher program.

A second issue, still unresolved, concerns the sustainability of voucher interventions. Although a gradual reduction of voucher values seems logical and has been discussed since the beginning of the Paraguay program, program designers have been reluctant to mandate this condition in newer projects. Instead, some team leaders recommend that an exit strategy be designed after the program's mid-term evaluation. This avoidance of the difficult sustainability question could turn out to be a serious mistake. It is true that in some cases, national or regional governments may be willing to "adopt" a pilot voucher program after its initial funding runs out. Tens of thousands of voucher clients, however, along with hundreds of training providers, may ultimately constitute a powerful local political constituency; and the subsidy may be hard to turn off. In addition, as the data from Table 4 shows, institutions may become more and more adept at capturing the voucher subsidy as time goes on. It is important to experiment with exit mechanisms now, in smaller pilot projects, before convincing public policymakers that such programs are worth supporting on a large scale and over sustained periods of time.

Assuming program designers, in the next few years, are able to address the issue of how and when to withdraw voucher financing, a remaining challenge remains: how to make sure the information gap does not recur. While voucher funding probably should not be a permanent intervention, the presence of a reliable second-tier institution fulfilling an information function may be desirable. This leads to the final question, which concerns the role of the second-tier institution. The question of who or what should play this role is important. An important lesson was learned in Paraguay due to mid-stream changes in the second tier institution. There are difficulties and trade-offs when working with public institutions, such as ministries or government agencies. In some instances public institutions are unable to play this role due to their inability to be transparent and impartial; their limited budgets; difficulties in hiring new personnel and firing ineffective staff; and difficulties in sharing other scarce government resources, such as buildings,

automobiles and even staff. They are unable to regulate themselves based on the standards they would need to impose on training suppliers.

There are two important criteria which an institution must possess to serve as an effective second-tier administrator in such a program: 1) administrative and financial capacity, and 2) capacity to negotiate and serve as an impartial party while playing a leadership role in the training market.

As shown in Table 6, a variety of institutional arrangements may provide the framework within which a successful information system and voucher training program can be operated. In the long run, an ideal second-tier institution would be one which could not only administer the vouchers successfully, but one which would respond to incentives to reduce the voucher funding over time, and which could potentially continue to play the role of information provider in a sustainable manner. One suggestion is to finance the information function through institutional dues, much in the way a banking superintendency is financed through dues paid by banks. On the other hand, a public subsidy may be justified to support the continued provision of the information service. In some Latin American countries, training institutions have stepped back from the market, preferring to outsource and regulate training activities rather than directly execute them. This more limited, regulatory function may correspond with the voucher administration and information service role. In countries where training institutions are serious about redefining their role and fostering private competition in the market, these institutions may be the best candidates to serve as second-tier voucher program administrators initially, and eventually as permanent information suppliers to the market.