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Investing in rural people

## President's report

### Proposed loan to the Independent State of Papua New Guinea for the Markets for Village Farmers Project – Maket Bilong Vilis Fama

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For: Approval

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## Abbreviations and acronyms

AWP/B	annual workplan and budget
CEFI	Centre for Excellence in Financial Inclusion
DAL	Department of Agriculture and Livestock
FPDA	Fresh Produce Development Agency
MVF	Markets for Village Farmers Project
PIM	project implementation manual
PMU	project management unit
PPAP	Productive Partnerships in Agriculture Project
PSC	project steering committee
PY	project year

# Map of the project area

Independent State of Papua New Guinea

Markets for Village Farmers (MVF) - Maket Bilong Vilis Fama



The designations employed and the presentation of the material in this map do not imply the expression of any opinion whatsoever on the part of IFAD concerning the delimitation of the frontiers or boundaries, or the authorities thereof.

Map compiled by IFAD | 08-02-2017

# Independent State of Papua New Guinea

## Markets for Village Farmers Project – Maket Bilong Vilis Fama

### Financing summary

<b>Initiating institution:</b>	IFAD
<b>Borrower:</b>	Independent State of Papua New Guinea
<b>Executing agency:</b>	Department of Agriculture and Livestock
<b>Total project cost:</b>	US\$50.26 million
<b>Amount of IFAD loan:</b>	US\$25.5 million
<b>Terms of IFAD loan:</b>	Blend: maturity period of 25 years, including a grace period of five years, with interest at a fixed rate of 1.25 per cent plus a service charge of 0.75 per cent per annum
<b>Financing gap:</b>	US\$3.47 million
<b>Cofinancier(s):</b>	Financial institutions
<b>Amount of cofinancing:</b>	US\$4.22 million
<b>Terms of cofinancing:</b>	Loans to beneficiaries
<b>Contribution of borrower:</b>	Central government US\$2.85 million Provinces/districts US\$13 million
<b>Contribution of beneficiaries:</b>	US\$1.21 million
<b>Appraising institution:</b>	IFAD
<b>Cooperating institution:</b>	Directly supervised by IFAD

## Recommendation for approval

The Executive Board is invited to approve the recommendation for the proposed financing to the Independent State of Papua New Guinea for the Markets for Village Farmers Project – Maket Bilong Vilis Fama, as contained in paragraph 49.

## Proposed loan to the Independent State of Papua New Guinea for the Markets for Village Farmers Project – Maket Bilong Vilis Fama

### I. Strategic context and rationale

#### A. Country and rural development and poverty context

1. Papua New Guinea has achieved robust economic growth in recent years. Yet this has not translated into improved livelihoods for the 40 per cent of the 7.3 million population that lives in poverty. The economy of this lower-middle-income country remains dominated by two sectors: a formal, largely capital-intensive extractive sector, and a largely informal agriculture sector that employs the majority of the active population.
2. Papua New Guinea consists of more than 600 islands of various sizes. Harsh terrain and remoteness contribute to the isolation of many rural communities. Poverty is more prevalent in rural areas where people have less access to services, education, markets and economic inputs. More than three quarters of the population depends on semi-subsistence agriculture as a main livelihood strategy.
3. Agriculture employs 80 per cent of the active population and accounts for 27 per cent of GDP. Low availability and high costs of modern inputs and technologies, lack of irrigation and limited access to support services contribute to low yields. This situation is further aggravated by increasing climate-change-related threats. High logistical costs due to a poor transport network and the lack of market organization and information discourage village farmers from engaging in market-oriented production. It is estimated that only 4 per cent of the country's land is used for commercially oriented agricultural production.
4. Rapid population growth, a growing middle class and expatriate population, and rural-to-urban migration are increasing demand for more and diversified foods. Fresh produce is farmed by 94 per cent of village-based families throughout the country. The majority of produce is grown in small vegetable gardens for family consumption, with small surpluses sold on local markets for cash. As demand grows, an increasing number of village farmers see opportunities to switch to market-oriented farming. The total national market demand for fresh produce is estimated at 1.32 million tons per year, of which about 60 per cent is currently met by local production. Conversely, about 60 per cent of modern market segments (supermarkets, catering companies, hotels, public institutions) are yet to be captured by local producers. New innovative business models offer the potential to curb some of the constraints affecting the rural sector and to improve the access of small-scale producers to markets and services.

#### B. Rationale and alignment with government priorities and RB-COSOP

5. Papua New Guinea's long-term development strategy envisages a shift in the economy to broad-based growth in agriculture, forestry, fisheries, ecotourism and manufacturing in order to expand household income and enhance socio-economic

development. Accordingly, the 2010-2030 Strategic Development Plan aims to transform Papua New Guinea into a prosperous middle-income country by 2030. Specific objectives for the agriculture sector include a five-fold increase in agricultural production, mostly through improved land use and productivity. Public/private partnerships are to become a cornerstone of agricultural development. The 2007-2016 National Agricultural Development Plan aims to stimulate agriculture-sector growth by increasing incomes and private-sector participation in three priority subsectors, including food and horticultural crops.

6. Papua New Guinea seeks to achieve higher economic growth through better opportunities for rural men and women to participate in market-oriented agriculture. In line with these policies and vision, the Markets for Village Farmers Project (MVF) – Market Bilong Vilis Fama aims to improve the livelihoods of village farming households by building on a successful partnerships approach tested under the ongoing IFAD investment, the Productive Partnerships in Agriculture Project (PPAP). The PPAP promotes collaborative arrangements under which farmers will have secure and remunerative market outlets, and buyers will obtain a reliable and consistent supply of fresh produce.

## II. Project description

### A. Project area and target group

7. Target area. The MVF's fresh produce intervention will be implemented in five target provinces: four in the Highland region (Western Highlands, Jiwaka, Chimbu and Eastern Highlands) and one in the Momase region (Morobe). These five provinces encompass a continuous geographical area from Mount Hagen, the main hub for fresh produce trading in the highlands, to Lae, the second largest city and main port for supplying Port Moresby, the capital city. In addition, a galip nut intervention will target East New Britain, Papua New Guinea's main cocoa-producing province, to maximize the mutual benefit of cocoa and galip nut production. All six target provinces are characterized by dense population and high rates of poverty, deprivation and stunting.
8. Target groups. The project will target: (i) semi-subsistence households (low input/low output farmers mostly growing food crops and limited cash crops); (ii) market-oriented village farmers involved in or with the potential to become involved in the target value chains; and (iii) women and youth. Fresh produce buyers – who source from village farmers, have scope for expanding their operations and can become a conduit to provide village farmers access to markets and services – will also be involved in project activities. The project will adopt a family team approach, similar to IFAD's household methodology, to engage with households and promote sustainability. The targeting strategy combines self-targeting with specific operational measures that ensure that inclusion and gender equity are mainstreamed in all aspects of implementation.
9. The MVF is expected to directly benefit approximately 23,500 households and approximately 117,500 total beneficiaries.

### B. Project development objective

10. The project goal, as mentioned, is to improve the livelihoods of village farming households in target provinces by facilitating their transition from semi-subsistence agriculture to market-oriented production and farming as a business. The development objective is to achieve sustainable, increased returns to village farming households from marketed production.

### C. Components/outcomes

11. Component 1. Inclusive business partnerships aims to build inclusive partnerships between village farmers and buyers in which: (i) farmers will gain improved access to markets and support services; and (ii) buyers will source from

farmers to supply remunerative markets. The component has five main thrusts: (i) building on existing public/private/producer partnership approaches; (ii) promoting demand-driven business partnerships; (iii) leveraging diverse sources of finance; (iv) engaging communities; and (v) adopting a value chain approach. The expected outcome is that village farming households have access to markets, technologies and services in the target value chains. It will cover two subsectors – fresh produce and galip nuts – each addressed in a subcomponent.

12. Component 2. Supportive value chain investment complements investment in inclusive business partnerships through support seeking to impact the whole value chain by: (i) improving access to production areas through spot improvements to feeder roads; and (ii) facilitating access of farming households and other players in the value chain to affordable and diversified financial services. Three main strategic thrusts guide the component: (i) linking road improvement to partnerships; (ii) improving the outreach of financial institutions and financial products in rural areas; and (iii) developing innovative financial instruments to meet the needs of farming households and value chain stakeholders. The expected outcomes are: at least 15,000 farming households have easier access to main roads to market their production; and at least 18,000 farming households have access to credit.
13. Component 3. Collective governance and project management aims to promote a favourable policy and institutional environment to support the development of inclusive fresh produce and galip nut sectors. The main strategic thrusts of the component are: (i) organizing value chain governance and coordination; and (ii) improving access to knowledge and market information. The expected outcome is that organized industry players contribute to policy development and sector coordination for inclusive industry growth. Component 3 is organized in two subcomponents: (i) collective governance; and (ii) project management.

### III. Project implementation

#### A. Approach

14. The MVF builds on the PPAP, financed by IFAD, the World Bank and the European Union to promote public/private/producer partnerships. Through these partnerships, farmers will have secure market outlets, incentivizing increased production of better quality fresh produce and a reliable and consistent supply of this produce for buyers, in line with market demand.
15. The MVF will adapt the PPAP approach to two government priority subsectors in which production largely originates with village farmers: fresh produce and galip nuts. The majority of financing will go towards the fresh produce subsector, as domestic fresh produce markets are rapidly expanding, creating market potential. Fresh produce already has a key role in the livelihoods, food security and risk management strategies of village farmers and offers opportunities for generating income with relatively low risk. The existence of various market channels and segments offers a potential to adapt partnerships and project support to participating households, depending on their absorptive and organizational capacity. There is also a potential for increasing farmers' returns through capturing a higher share of value when selling to modern market segments.
16. While not as prominent, galip nuts have significant potential to develop into a new export cash crop, benefiting thousands of village farming households.
17. As with the PPAP, partnerships will: originate in a competitive selection process to ensure transparency and the meeting of project objectives; cover a demand-driven package of activities to secure farmers' access to inputs and technical services in accordance with the specificities of every partnership; and be matched by technical assistance to strengthen industry organization and knowledge management. However, the PPAP approach will be adapted to the specificities of the fresh produce



subsector, where buyers are smaller, source from smaller groups of farmers, and are less familiar with business management and markets than those in the cocoa and coffee sectors.

18. The project will adopt a family-based targeting approach, drawing on the family team approach developed by the Australian Centre for International Agricultural Research and the Family Business Management Training developed by CARE. This family-based approach facilitates a more-equitable distribution of family assets and labour, and a joint family vision for sustainable socio-economic development. It will form the foundation of MVF partnership development and of promotion of support services such as financial literacy, business education and extension.
19. The project is expected to start in late 2017 and will be phased in over six years. The first year of project implementation (PY1) will establish the project organizational structure and processes, undertaking scoping studies and launching a first expression of interest in partnership proposals. Each successful partnership supported by the project will last three years. Two further calls for partnership proposals will occur in PY2 and PY3. PY5 and PY6 will focus on successfully completing partnerships, promoting sustainability, knowledge management and scaling up.

## B. Organizational framework

20. The project organizational framework aligns with the current agriculture-sector organizational structure in Papua New Guinea, with the Department of Agriculture and Livestock (DAL) as the project executing agency. The Fresh Produce Development Agency (FPDA), in which the Departments of Agriculture and Livestock and Treasury hold equal shares in trust, will be the main implementing agency. Project design takes into account the recommendations of the recent Functional Expenditure Review of the agricultural sector and the resultant draft Agriculture Administration Adjustment Act – recommendations related to linkages between commodity boards and provincial and district governments and the development of farmer-oriented, market-driven, pluralistic extension services. Another key feature of the organizational framework is that it is based on public/private/producer partnerships: while the Government retains overall implementation responsibility, private-sector players (fresh produce and galip nut buyers, but also financial institutions and business development service providers) will have key roles in providing village farmers with support services and access to markets.
21. Service providers will be retained to implement specific packages of activities that go beyond FPDA competencies or capacities. The Centre for Excellence in Financial Inclusion (CEFI) has been pre-selected to implement project activities related to financial inclusion under component 2. Implementation responsibilities will be detailed in a memorandum of understanding signed by the project management unit (PMU), CEFI and DAL. CEFI will also lead the consortium responsible for implementing the family-based approach and financial education, which it will form together with an international NGO with experience in household-based methodologies in the Papua New Guinea context.
22. The project implementation set-up aims to strengthen the capacities of FPDA to steer the inclusive development of the fresh produce sector and to provide technical advisory and market support services in line with its mandate. Thus the PMU is not configured as a self-standing organization, but is embedded within FPDA and geared to work closely with the relevant FPDA divisions: the Corporate Affairs Division, which covers finance, procurement and human resources; the Planning, Research and Communication Division; and the Production and Value Chain Innovation Division.

23. The main implementing partners are summarized as follows:
- DAL is the project executing agency responsible for project oversight and coordination.
  - FPDA has overall responsibility for project implementation.
  - Provincial teams led by FPDA current staff and staffed by seconded district extension officers will be responsible for field implementation of project activities.
  - Provincial governments will facilitate project implementation at the provincial level through appointment of fully dedicated focal points. They will also significantly cofinance infrastructure investments.
  - District governments will have a similar role at the district level and will cofinance road works.
  - A project steering committee (PSC), gathering representatives of the main stakeholders involved in MVF implementation, will provide overall guidance and oversight.
  - An independent technical appraisal committee will be responsible for assessing partnership proposals and bringing transparency and objectivity to the selection process.
  - Fresh produce/galap nut multistakeholder platforms will be established at national/provincial/district levels, and will provide a venue to discuss sector challenges and constraints. These platforms will also be involved in preparation of annual workplans and budgets (AWP/Bs) and identification of policy studies.
  - The PMU, embedded within FPDA, will assist in carrying out project implementation responsibilities.
  - CEFI will be responsible for implementing activities related to financial inclusion, by virtue of a memorandum of understanding signed by the PMU and DAL.

#### C. Planning, monitoring and evaluation, and learning and knowledge management

24. The integrated system for monitoring and evaluation and knowledge management will be developed with three main objectives: (i) steer project implementation by providing project stakeholders with the information and analysis required to: measure project outcomes; assess project effects on the livelihoods of target groups, and in particular women, poor households and youth; assess the relevance of the project strategy, methodologies and implementation processes; detect difficulties and successes; and support decision-making to improve project performance; (ii) support economic decisions and policymaking by providing project stakeholders – in particular farmers and agribusiness partners, service providers, FPDA and the PMU – with the information and analysis they need to assess the return brought by innovation, to develop profitable and sustainable activities and to adapt their strategies accordingly; and (iii) share knowledge and scale up good practices by developing lessons learned and capturing good practices and successful innovations, with a view to supporting project performance and policy dialogue.

#### D. Financial management, procurement and governance

25. DAL will have overall accountability for the project, including fiduciary aspects. The PSC will approve the AWP/Bs and procurement plans for IFAD's "no objection". A good governance and mutual accountability framework between IFAD and the

Government will be adopted to strengthen accountability and transparency, in line with international best practices.

26. Day-to-day implementation will be delegated by DAL to the PMU embedded within FPDA, which will be responsible for day-to-day financial management activities, including accounting, reporting and coordinating audit processes.
27. The inherent fiduciary risk is deemed to be high (see section on good governance below). The financial management risk of the project was assessed at design, and also judged to be high owing to the lack of experience of FPDA in implementing donor-funded projects. A number of measures will be put in place to mitigate this risk, including: (i) establishment of the PMU with delegated authority to plan, manage, disburse and control project resources (including counterpart financing); (ii) contracting of key financial and administrative management with relevant experience and qualifications; (iii) preparation of AWP/Bs for review by DAL and approval by the PSC; (iv) procurement and installation of accounting software and associated staff capacity-building; (v) preparation of a financial management manual that integrates controls closely linked to the project operational dimensions and consistent with FPDA financial policies and IFAD financial and disbursement guidelines; (vi) establishment of an internal control framework, including periodic internal audits; (vii) submission of quarterly financial reports to DAL and IFAD; and (viii) coordination of external audit processes.
28. The project will be required to maintain a full set of accounts in accordance with International Public-Sector Accounting Standards.
29. The project will be audited by the Office of the Auditor General (AGO) or by a private firm outsourced by AGO, in line with current practice for the IFAD cofinanced project administered by the World Bank (the PPAP). An audit will be carried out annually and in compliance with International Standards on Auditing and the IFAD Guidelines on Project Audit. IFAD prior experience with AGO in terms of quality and timeliness is currently moderately satisfactory.
30. Flow of funds and disbursement. Two trust designated accounts will be opened to receive funds for the project from IFAD and the Government respectively. A project bank account will be opened to cover operating costs for FPDA activities at the provincial level (FPDA Provincial Team).
31. Procurement of goods, works and services financed from resources provided or administered by IFAD will be undertaken in accordance with government regulations and consistent with the provisions of IFAD's Procurement Guidelines and Handbook. Goods and services (non-consulting) procured using international or national competitive bidding, national shopping and direct contracting will follow the procedures and processes defined in the project implementation manual (PIM) approved by the PSC and IFAD. Selection of individual consultants and individual service providers will also be defined in the PIM. The PMU will submit an 18-month procurement plan immediately after the financing agreement enters into force. Procurement will be undertaken in accordance with the consolidated procurement plan submitted by the PMU, approved by the PSC and endorsed by IFAD.
32. Good governance. Papua New Guinea is ranked 136<sup>th</sup> of 176 countries, with a score of 28 in Transparency International's 2016 Corruption Perceptions Index, indicating a high risk in the overall country context. IFAD applies a zero-tolerance policy on corruption. The PMU will prepare an integrated framework for good governance, which will be included in the PIM and published on the MVF website. This framework will include provisions to ensure that procurement and the selection of enterprises that will enter into business partnerships and benefit from MVF support are carried out in accordance with government and IFAD rules (including IFAD's Policy on Preventing Fraud and Corruption in its Activities and Operations) and with project design specifications. Measures will include: (i) publication/posting

of all procurement, calls for proposals, contract awarding and business partnership details in local newspapers, at district and provincial offices and on the MVF website, including assessment criteria and weighting; (ii) participation of representatives of end-users in bid assessments; (iii) prompt communication to bidders of bid evaluation outcomes; (iv) a contract provision requiring suppliers, contractors and consultants to: ensure compliance with the IFAD zero-tolerance anticorruption policy; permit IFAD to inspect their accounts, records and other documents relating to the bid submission and contract performance; and have them audited by IFAD-appointed auditors; and (v) rules that allow potential project beneficiaries and other stakeholders to channel and address any complaints they may have on implementation of the project. This framework will also include an internal code of conduct to be signed by all PMU staff, and a code of business ethics, to be signed by all partners and beneficiaries of MVF activities and business partnerships.

#### E. Supervision

33. The MVF will be directly supervised by IFAD, which will undertake two joint review missions annually with the Government, participating partners and project stakeholders. Implementation support missions will also be fielded to provide specific support on a need basis.
34. Two interim reviews will also be organized at the end of PY3 and in PY5. The reviews will: (i) assess achievements and interim impact, the efficiency and effectiveness of the MVF, and the continued validity of MVF design; (ii) identify key lessons learned and good practices; and (iii) provide recommendations for improved performance.

### IV. Project costs, financing and benefits

#### A. Project costs

35. The total project cost is estimated at US\$50.26 million over a six-year implementation period. Indicative component costs are detailed in table 1. Indicative project costs by expenditure category and financier are provided in table 2.

Table 1  
**Project costs by component and financier**  
(Thousands of United States dollars)

Component	IFAD loan		Financing gap		Financial institutions		Beneficiaries		Borrower/ counterpart		Provinces/ districts		Total
	Amount	%	Amount	%	Amount	%	Amount	%	Amount	%	Amount	%	Amount
1. Inclusive business partnership	12 307	54.6	3 472	15.4	4 223	18.8	1 214	5.4	1 305	5.8	-	-	22 521
2. Supportive value chain investment	6 267	31.5	-	-	-	-	-	-	622	3.1	13 000	65.4	19 889
3. Collective governance and project management	6 926	82.2	-	-	-	-	-	-	923	11.8	-	-	7 849
<b>Total</b>	<b>25 500</b>	<b>50.7</b>	<b>3 472</b>	<b>6.9</b>	<b>4 223</b>	<b>8.4</b>	<b>1 214</b>	<b>2.4</b>	<b>2 851</b>	<b>5.7</b>	<b>13 000</b>	<b>25.9</b>	<b>50 260</b>

#### B. Project financing

36. The project will be financed by: (i) an IFAD loan of US\$25.5 million (50.7 per cent of the total project); (ii) a central government contribution of US\$2.85 million (5.7 per cent); (iii) a contribution by provincial and district governments of US\$13 million (25.9 per cent); (iv) a contribution by financial institutions of US\$4.22 million (8.4 per cent); and (v) beneficiary contributions of US\$1.21 million (2.4 per cent). The financing gap of US\$3.47 million (6.9 per cent) may be sourced

by subsequent performance-based allocation system cycles (under financing terms to be determined and subject to internal procedures and subsequent Executive Board approval) or by cofinancing identified during implementation.

**Table 2**  
**Project costs by expenditure category and financier**  
(Thousands of United States dollars)

Expenditure category*	IFAD loan		Financing gap		Financial institutions		Beneficiaries		Borrower/ counterpart		Provinces/ districts		Total
	Amount	%	Amount	%	Amount	%	Amount	%	Amount	%	Amount	%	Amount
<b>Investment costs</b>													
1. Consultancies	5 872	87.1	110	1.6	-	-	-	-	759	11.3	-	-	6 741
2. Equipment and materials	1 643	90	-	-	-	-	-	-	183	10	-	-	1 826
3. Goods and services	424	77.7	69	12.7	-	-	-	-	52	9.6	-	-	546
4. Grants and subsidies	3 002	43.8	3 170	46.3	-	-	682	10	-	-	-	-	6 854
5. Training and workshop	6 014	87.3	122	1.8	-	-	63	0.9	689	10	-	-	6 888
6. Works	2 574	16.2	-	-	-	-	-	-	286	1.8	13 000	82	15 860
7. Credit and guarantee fund	450	8.8	-	-	4 223	82.1	469	9.1	-	-	-	-	5 142
<b>Recurrent costs</b>													
1. Salaries and allowances	4 085	85	-	-	-	-	-	-	723	15	-	-	4 808
2. Operating costs	1 435	90	-	-	-	-	-	-	159	10	-	-	1 595
<b>Total</b>	<b>25 500</b>	<b>50.7</b>	<b>3 472</b>	<b>6.9</b>	<b>4 223</b>	<b>8.4</b>	<b>1 214</b>	<b>2.4</b>	<b>2 851</b>	<b>5.7</b>	<b>13 000</b>	<b>25.9</b>	<b>50 260</b>

\* Expenditure categories will be combined into five or six for preparation of schedule II.

### C. Summary benefit and economic analysis

37. The MVF is expected to achieve sustainable increased returns to village farming households through improved market linkages. Benefits will derive from: (i) improving smallholders' access to markets, technologies and services in target value chains; (ii) developing diverse types of business partnerships involving village farmers and agribusiness; (iii) reducing post-harvest losses; (iv) improving the value chain environment to facilitate farmers' inclusion; and (v) supporting policies and institutional capacities required to ensure sustainability. The project is expected to benefit about 23,500 households. Women will constitute 50 per cent of the beneficiaries.
38. The overall economic internal rate of return is estimated at 39 per cent for the base case. The net present value of the net benefit stream, discounted at 7 per cent, is US\$140.4 million. A sensitivity analysis shows the economic impact of a 50 per cent increase and decrease in project benefits on project viability. The analysis confirms that the economic viability of the project remains attractive, as a positive net present value and economic internal rate of return above 7 per cent are preserved in each case analysed.

### D. Sustainability

39. The project introduces a number of mechanisms to ensure sustainability of benefits. All partnerships will have access to up to three years of project support, after which they are expected to be self-sustaining. This would imply that: (i) farmers enjoy continued access to services and markets beyond the completion of their partnership agreement; and (ii) buyers have well-managed, profitable businesses with reliable markets that they are consistently able to supply with quality products.

The progressive construction of sustainable access to services and markets will be addressed as part of the preparation of each single partnership agreement, which will have a specific section devoted to building sustainability. While each partnership will develop a tailored approach that builds on local opportunities and partners' specificities, key elements of the project approach that should support sustainability include the following: (i) support to strengthening farmers' organizations; (ii) development of cooperatives and service hubs for farmers; (iii) use of local resources to develop partnerships such as business development service providers and village extension workers; (iv) capacity-building of all key stakeholders; and (v) innovative business models and knowledge management.

## E. Risk identification and mitigation

40. The main risks are: (i) low interest of agribusinesses in engaging village farmers due to risk and high transaction costs; (ii) weak technical and management capacity of farmers' organizations; (iii) limited benefits accruing to women because of social and cultural constraints; (iv) remoteness of some production areas; (v) impact of climate change and extreme climatic events; (vi) limited interest of financial institutions in extending services to rural areas; and (vii) high financial management risk. Mitigation measures, built into the project design, include: (i) building on the successful experience of the PPAP with respect to incentivizing the participation of agribusiness and ensuring extensive support to farmers' organizations; (ii) adopting a family-based approach to participation and equity; (iii) integrating climate risk assessment, promotion of climate-resilient-varieties management practices and climate-resilient feeder roads; (iv) introducing incentive schemes and risk-sharing to offset risk and build a financially literate, creditworthy clientele; and (v) setting up adequate financial management arrangements to mitigate financial management risks.

## V. Corporate considerations

### A. Compliance with IFAD policies

41. The MVF aligns with the goals and objectives of the IFAD Strategic Framework 2016-2025 and relevant IFAD policies, including those on environment and natural resource management, gender equality and women's empowerment, indigenous peoples, and preventing fraud and corruption, as well as with the strategies for rural finance, private-sector partnerships, nutrition and climate change.

### B. Alignment and harmonization

42. The MVF is expected to contribute significantly to Papua New Guinea's achievement of the Sustainable Development Goals. The MVF is set within a number of key government policies and programmes, including Papua New Guinea's Vision 2050, the Papua New Guinea Strategic Development Plan (2010-2030) and the National Agricultural Development Plan (2007-2016). It responds to the recommendations of DAL's 2014 Functional Expenditure Review and of seven commodity boards and agencies. The project design draws from and will coordinate with a number of ongoing development partner initiatives, including the PPAP, cofinanced by IFAD, the World Bank and the European Union; the Lead Firm Programme, funded by New Zealand Aid; the Pacific Horticultural and Agricultural Market Access Program, cofinanced by Australia and New Zealand; Transformative Agriculture and Enterprise Development in Papua New Guinea, cofinanced by Australia and the Australian Centre for International Agricultural Research; and the Microfinance Expansion Project, financed by the Asian Development Bank.

### C. Innovations and scaling up

43. The MVF will introduce an innovative partnership approach that leverages public and private investment to support business arrangements between agribusiness and smallholder farmers. The MVF has adapted the PPAP approach to the specific features of the target value chains, and particularly the fresh produce subsector,

where buyers are smaller, source from smaller groups of farmers, and are less familiar with business management and markets than those in the cocoa and coffee sectors. As in the PPAP, partnerships will be financed by an incentive grant aimed at decreasing partners' risk and facilitating their engagement with innovative agricultural practices and marketing arrangements. However, the portion of partnership costs covered by the incentive grant will be reduced and the project will facilitate partners' access to finance, with a view to enhancing sustainability and benefiting more farmers. Other adaptations include: providing technical and management support to buyers as part of partnership activities, so that they can consolidate and expand their businesses; providing technical and brokering services for the preparation of partnerships to ensure sound agreements that spell out a clear distribution of responsibilities and a balanced share of risks and benefits; and supporting gender equitable and socially inclusive approaches at the community level through the family-based approach in order to achieve greater impact.

44. The MVF has a strong potential for geographical scaling up within the two current value chains, but also for other agricultural commodities. The monitoring and evaluation system will facilitate knowledge-sharing and scaling up of good practices.

#### D. Policy engagement

45. The MVF aims to promote a favourable policy and institutional environment to support the development of the inclusive fresh produce and galip nut value chains. It will seek to share knowledge and scale up good practices with a view to supporting project performance and policy dialogue. This dialogue will be based on lessons and good practices from project implementation. Pre-identified policy issues include: quality standards and certification for domestic and export markets; fair contracting standards to bring transparency to contractual arrangements between village farmers and buyers, and a fair distribution of both final value added and risks; and regulation of imports to ensure access to quality farm inputs.

### VI. Legal instruments and authority

46. A project financing agreement between the Independent State of Papua New Guinea and IFAD will constitute the legal instrument for extending the proposed financing to the borrower. A copy of the negotiated financing agreement is attached as appendix I.
47. The Independent State of Papua New Guinea is empowered under its laws to receive financing from IFAD.
48. I am satisfied that the proposed financing will comply with the Agreement Establishing IFAD and the Policies and Criteria for IFAD Financing.

### VII. Recommendation

49. I recommend that the Executive Board approve the proposed financing in terms of the following resolution:

RESOLVED: that the Fund shall provide a loan on blend terms to the Independent State of Papua New Guinea in an amount equivalent to twenty-five million five hundred thousand United States dollars (US\$25,500,000), and upon such terms and conditions as shall be substantially in accordance with the terms and conditions presented herein.

Gilbert F. Hougbo  
President

## Negotiated financing agreement

### Markets for Village Farmers Project – Maket Bilong Vilis Fama

(Negotiations concluded on 8 September 2017)

Loan No: \_\_\_\_\_

Project Title: Markets for Village Farmers - Maket Bilong Vilis Fama (MVF) ("the Project")

Independent State of Papua New Guinea (the "Borrower")

and

The International Fund for Agricultural Development (the "Fund" or "IFAD")

(each a "Party" and both of them collectively the "Parties")

hereby agree as follows:

#### Section A

1. The following documents collectively form this Agreement: this document, the Project Description and Implementation Arrangements (Schedule 1), the Allocation Table (Schedule 2) and the Special Covenants (Schedule 3).
2. The Fund's General Conditions for Agricultural Development Financing dated 29 April 2009, amended as of April 2014, and as may be amended hereafter from time to time (the "General Conditions") are annexed to this Agreement, and all provisions thereof shall apply to this Agreement. For the purposes of this Agreement the terms defined in the General Conditions shall have the meanings set forth therein.
3. The Fund shall provide a Loan to the Borrower (the "Financing"), which the Borrower shall use to implement the Project in accordance with the terms and conditions of this Agreement.

#### Section B

1. The amount of the Loan is twenty five million five hundred thousand United States Dollars (USD 25 500 000).
2. The Loan is granted on blend terms, and shall be subject to interest on the principal amount outstanding at a fixed rate of 1.25 per cent and in addition a service charge of 0.75 per cent per annum payable semi-annually in the Loan Service Payment Currency and shall have a maturity period of twenty five (25) years, including a grace period of five (5) years, starting from the date of approval by the Executive Board.
3. The Loan Service Payment Currency shall be USD.
4. The first day of the applicable Fiscal Year shall be 1 January.



5. Payments of principal and service charge shall be payable on each 15 October and 15 April.
6. There shall be one Designated Account (DA) operated by the Department of Agriculture and Livestock (DAL) for receiving the Loan proceeds from IFAD.
7. The Fresh Produce Development Agency (FPDA) will maintain one project bank account in local currency to implement the project activities.
8. The Borrower shall cover all taxes and duties on all Project expenditure. In addition, the Borrower shall provide counterpart financing for the Project for an amount of approximately of USD 2.85 million to cover Project staff salary costs. The provincial and district governments shall provide counterpart financing to be determined annually on the basis of the Project design. The beneficiaries shall contribute to the Project in cash or in kind for an amount of approximately USD 1.21 million.

#### Section C

1. The Project Executing Agency shall be the DAL.
2. The Project Implementing Agency shall be the FPDA.
3. The following are designated as additional Project Parties: Provincial Governments and District Administrations, the Centre for Financial Inclusion, participating commercial banks and financial institutions.
4. The Project Completion Date shall be the sixth anniversary of the date of entry into force of this Agreement.

#### Section D

The Loan will be administered and the Project supervised by IFAD.

#### Section E

1. The following are designated as additional grounds for suspension of this Agreement:
  - (a) The Project Implementation Manual referred to in paragraph 13 of Schedule 1 hereto, or any provision thereof, has been waived, suspended, terminated, amended or otherwise modified without the prior consent of the Fund, and the Fund has determined that such waiver, suspension, termination, amendment or modification has had, or is likely to have, a material adverse effect on the Project;
  - (b) Any transfer of key Project staff in the Project Coordination Unit and the Project Management Unit located in the Department of Agriculture and Livestock and the Fresh Produce Development Agency respectively, that has not been communicated to IFAD.
2. The following are designated as additional general conditions precedent to withdrawal:
  - (a) The Project Coordination Unit within the Department of Agriculture and Livestock and the Project Management Unit within the Fresh Produce

Development Agency shall have been created and key Project staff, as defined in Schedule 1, shall have been nominated to the satisfaction of IFAD;

- (b) The Project implementation manual, including the Financial Management section, shall have been prepared in a manner satisfactory to IFAD; and
- (c) The AWPB for the first year of Project Implementation and the 18 month Procurement implementation Plan shall have been prepared in a manner satisfactory to IFAD.

3. This Agreement is subject to ratification by the Borrower.

4. The following are the designated representatives and addresses to be used for any communication related to this Agreement:

For the Borrower:

\_\_\_\_\_  
\_\_\_\_\_

For the Fund:

The President  
International Fund for Agricultural development  
Via Paolo di Dono 44  
00142 Rome, Italy

This Agreement, dated \_\_\_\_\_, has been prepared in the English language in two (2) original copies, one (1) for the Fund and one (1) for the Borrower.

INDEPENDENT STATE OF  
PAPUA NEW GUINEA

\_\_\_\_\_  
(Authorized Representative)

INTERNATIONAL FUND FOR  
AGRICULTURAL DEVELOPMENT

\_\_\_\_\_  
Gilbert F. Hougbo  
President

## Schedule 1

### Project Description and Implementation Arrangements

#### I. Project Description

1. Target Population. The Project shall benefit 23,500 households and approximately 117,500 total direct beneficiaries in six target provinces: four in the Highland region (Western Highlands, Jiwaka, Chimbu and Eastern Highlands) and one in the Momase region (Morobe) for the project fresh produce activities; and East New Britain for the project's galip nut activities (the "Project Area").

2. Goal. The goal of the Project is to improve the livelihoods of village farming households in target provinces by facilitating their transition from semi-subsistence agriculture to market-oriented production and farming as a business.

3. Objectives. The development objective of the Project is to achieve sustainable, increased returns to village farming households from marketed production. In support of the development objective, the Project would have three outcomes, each linked to one of the Project's investment components: Village farming households have access to markets and services in the target value chains. Improved value chain environment to facilitate small farmers' inclusion. Organised industry players contribute to policy development and sector coordination for inclusive industry growth.

4. Components. The Project shall consist of the following Components:

Component 1. Inclusive Business Partnerships aims at building inclusive partnerships between village farmers and buyers, whereby: (i) farmers will gain improved access to markets and support services; and (ii) buyers will source from farmers to supply remunerative markets. The expected outcome is that village farming households have access to markets, technologies and services in the target value chains. The main outputs are: (i) different types of business partnerships linking fresh produce and galip nut producing households to buyers; (ii) at least 20,000 farming households (20,000 men and 20,000 women) trained in and using good agricultural and post-harvest practices for fresh produce; (iii) around 23,000 farming households trained for family engagement in decision-making on production and marketing. The component 1 has two sub-components: (i) Fresh Produce Partnerships; and (ii) Galip Nut Supply Chain.

Component 2. Supportive value chain investment complements investment in inclusive business partnerships through support seeking to impact the whole value chain by: (i) improving access to production areas through spot improvements to feeder roads; and (ii) facilitating access of farming households and other players in the value chain to affordable and diversified financial services. Three main strategic thrusts guide the component: (i) linking road improvement to partnerships; (ii) improving the outreach of financial institutions and financial products in rural areas; and (iii) developing innovative financial instruments to meet the needs of farming households and value chain stakeholders. The expected outcomes are: at least 15,000 farming households have easier access to main roads to market their production; and at least 18,000 farming households have access to credit. The component 2 has two sub-components: (i) Spot improvements of feeder roads; and (ii) Financial inclusion.

Component 3. Collective governance and project management aims to promote a favourable policy and institutional environment to support the development of inclusive fresh produce and galip nut sectors. The main strategic thrusts of the component are: (i) organizing value chain governance and coordination; and (ii) improving access to knowledge and market information. The expected outcome is that organized industry players contribute to policy development and sector coordination for inclusive industry growth. Component 3 is organized in two sub-components: (i) collective governance; and (ii) project management.

## II. Implementation Arrangements

5. The Department of Agriculture and Livestock (DAL) will be the Project executing agency. The Fresh Produce Development Agency will be the main project implementing agency.
6. Department of Agriculture and Livestock As the Project executing agency it will be responsible for the overall accountability, oversight and coordination of the project, under the direct authority of the Secretary of the DAL. This would include the chairing of the Project Steering Committee; the approval of Annual Work Plans and Budgets and Annual Procurement Plans; the approval of technical and financial reports; the endorsement of Withdrawal Applications and Statements of Expenditure, prepared by the Project Management Unit and submitted by Fresh Produce Development Agency's General Manager, for subsequent approval by the Department of Treasury; project technical and financial reports prepared by Fresh Produce Development Agency with Project Management Unit support; the facilitation of policy dialogue; and coordination with other relevant initiatives in the agriculture sector. A small Project Coordination Unit will be established within DAL to support it executing its functions. The Project Coordination Unit will consist of a Project Coordinator and an IFAD Liaison Officer.
7. Fresh Produce Development Agency will be responsible for Project management and coordination of government and non-government agencies participating in the Project. It will also be responsible for day to day financial management activities, including accounting, reporting and coordinating audit processes. The Fresh Produce Development Agency's General Manager will have overall responsibility for project implementation. However, line responsibility for day-to-day project implementation will be delegated to a Project Manager within a Project Management Unit to be established within Fresh Produce Development Agency.
8. Provincial Teams in each of the target provinces will be responsible for implementing Component 1 in their respective provinces. Each Provincial Team will be headed by an FPDA middle manager and staffed with two seconded district extension staff, to be selected based on a competitive basis. Provincial Teams will be under the direct supervision of the Project Manager, and overall supervision of the Fresh Produce Development Agency General Manager. Fresh Produce Development Agency will open provincial offices in Chimbu and Jiwaka to accommodate the Provincial Teams.
9. Project Steering Committee will be established at the national level to provide overall guidance and oversight, to ensure alignment with national sector priorities, to share good practices and promote policy dialogue. It will approve annual work plan and budgets, annual progress and financial reports, prepared by Fresh Produce Development Agency and the Project Management Unit, endorsed by Department of Agriculture and Livestock. It will be chaired by Secretary of the Department of Agriculture and Livestock and will include representatives from relevant public and private stakeholders. The Project Management Unit Liaison

Officer based in Department of Agriculture and Livestock will provide the Secretariat to the Project Steering Committee.

10. Technical Appraisal Committee (TAC) will be established to appraise partnership proposals submitted by the Project Management Unit, rate them and provide a recommendation for their financing, prior to their approval by Fresh Produce Development Agency Board. All TAC members will be individuals with an established reputation for their knowledge of the sector and integrity.
11. Project Coordination Unit will be established within DAL to assist with implementing its responsibilities as an executing agency. The Project Coordination Unit will consist of a Project Coordinator and an IFAD Liaison Officer.
12. Project Management Unit (PMU) will be embedded within Fresh Produce Development Agency, with responsibility for daily implementation of the Project. The Project Management Unit will be accountable for the performance of project implementation and the use of funds. This will include: (i) providing strategic guidance to ensure that all project implementation partners develop activities along a common, coherent approach in line with the Project Design Report; (ii) ensuring the financial and administrative management of project resources in line with the Loan Agreement and IFAD policies; (iii) planning project activities in consultation with project stakeholders; (iv) procuring project-related services and supplies; (v) coordinating project activities with the various project partners; (vi) securing Monitoring and Evaluation and Knowledge Management in relation to all activities; and (vii) promoting inclusive approaches and the mainstreaming of targeting and gender requirements in all of the project activities. The Project Management Unit will include key project staff: Project Manager, PMU Manager, Production and Value Chain System Manager, Infrastructure Engineer, Policy Development Officer, Senior, Monitoring & Evaluation/Knowledge Management (ME/KM) Officer, Management Information System (MIS) Content Manager, Gender and Social Inclusion Officer, Financial and Administration Manager, Procurement Officer, and an Accountant.
13. Project Implementation Manual. The Project Implementing Agency (PIA) shall prepare a consolidated draft Project Implementation Manual (PIM) and submit to the Fund for its comments and no objection. The PIM may be amended or otherwise modified from time to time only with the prior consent of the Fund.

## Schedule 2

## Allocation Table

1. Allocation of Proceeds. (a) The Table below sets forth the Categories of Eligible Expenditures to be financed by the Loan and the allocation of the amounts of the Loan to each Category and the percentages of expenditures for items to be financed in each Category:

Category	Loan Amount Allocated (expressed in USD)	Percentage (net of tax, co-financiers and beneficiary contributions)
I. Works	2 320 000	100%
II. Equipment & materials	1 860 000	100%
III. Consulting services & Training	10 700 000	100%
IV. Credit, guarantee funds	410 000	100%
V. Grants	2 700 000	100%
VI. Recurrent costs	4 960 000	100%
Unallocated	2 550 000	
<b>TOTAL</b>	<b>25 500 000</b>	

(b) The terms used in the Table above are defined as follows:

"Works" under Category I, shall mean eligible expenditures incurred related to improvements of feeder roads under Component 2.

"Recurrent costs" under Category VI, shall mean eligible expenditures for operating costs, salaries and allowances.

### Schedule 3

#### Special Covenants

In accordance with Section 12.01(a)(xxiii) of the General Conditions, the Fund may suspend, in whole or in part, the right of the Borrower to request withdrawals from the Loan Account if the Borrower has defaulted in the performance of any covenant set forth below, and the Fund has determined that such default has had, or is likely to have, a material adverse effect on the Project:

The project will procure, install and customize an accounting software to satisfy IFAD's requirements and International Accounting Standards, within 6 months of entry into force of the Financing Agreement.

## Logical framework

Results Hierarchy	Indicators					Means of Verification			Assumptions (A) / Risks (R)
	Name	Baseline	Interim review 1	Interim review 2	End Target	Source	Frequency	Responsibility	
<b>Goal:</b> Improved livelihoods of village farmers' households (HH) in target provinces	<ul style="list-style-type: none"> <li>30 % increase in HH asset ownership index</li> <li>No of persons receiving services *</li> </ul>	<sup>1</sup>	0%	15%	30%	Project survey	Interim review 2 and project end	PMU + FPDA	GoPNG commitment to improve returns to farmers in agriculture value chains
<b>Development Objective:</b> Increased returns to village farming households from increased marketed production	<ul style="list-style-type: none"> <li>Percentage of total farmer fresh produce production sold to market increased by at least 40%</li> <li>Percentage of total galip nut production per farmer sold to galip plant</li> </ul>	0	15%	30%	40%	Partnership reports	Quarterly reports	Lead Partners	
<b>Outcome 1:</b> Village farming households have access to markets and services in the target value chains	<ul style="list-style-type: none"> <li>Yield in selected fresh produce crops increased by 40% on average</li> <li>Annual volume of galip nut sold to plant (tons)</li> <li>Percentage of persons reporting increase in production *</li> </ul>	0%	20%	30%	40%				Partnership reports
<b>Outputs:</b> 1.1 Different types of business partnerships involving FP/GN are implemented 1.2 Farming households in partnerships are trained to use improved technologies	<ul style="list-style-type: none"> <li>23,200 farming households (23,200 men and 23,200 women) involved in project-supported partnerships</li> <li>At least 20,000 trained in production practices and/ or technologies *</li> </ul>	0	10,000	22,000	23,200	Partnership reports	Quarterly reports	Lead Partners	
<b>Outcome 2:</b> Improved value chain environment to facilitate small farmers' inclusion	<ul style="list-style-type: none"> <li>At least 18,000 people reporting using financial services *</li> <li>At least 10,000 farming households reporting improved physical access to markets, processing and storage facilities *</li> </ul>	0	9,000	15,000	18,000				CEFI reports PMU reports

<sup>11</sup> Will be established based on the baseline study to be carried out at project start.

\* RIMS Core Indicators



Results Hierarchy	Indicators					Means of Verification			Assumptions (A) / Risks (R)
	Name	Baseline	Interim review 1	Interim review 2	End Target	Source	Frequency	Responsibility	
<b>Outputs:</b> 2.1 Financial institutions (FIs) with improved capacities to serve target value chains players	<ul style="list-style-type: none"> <li>At least 9 financial service providers supported in delivering outreach strategies, financial products and services to rural areas *</li> </ul>	0	6	9	9	CEFI reports	Biannual reports	CEFI	
2.2 Improved, climate resilient feeder roads from main production areas to main road	<ul style="list-style-type: none"> <li>100 km of climate-resilient feeder roads rehabilitated *</li> <li>Up to 20 districts have maintenance arrangements in place to sustain feeder road practicability after spot improvements</li> </ul>	0	0	50	100	PMU reports	Biannual reports	PMU	
		0	0	6	20				
<b>Outcome 3:</b> Organised industry players contribute to policy development and sector coordination for inclusive industry growth	<ul style="list-style-type: none"> <li>At least three policy and regulatory measures proposed to policy makers for approval, ratification or amendment *</li> <li>FPDA MIS operational</li> </ul>	0	0	1	3	PMU reports	Biannual reports	PMU	
		0	1	1	1				
<b>Outputs:</b> 3.1 Multi-stakeholders' platforms created and trained 3.2 Policy and regulatory instruments prepared 3.3 MIS system in place at FPDA and FPDA staff trained	<ul style="list-style-type: none"> <li>Two national, at least 3 provincial and 10 district-based multi-stakeholders' platforms supported *</li> <li>At least three policy relevant knowledge products completed *</li> <li>MIS in place and number of staff trained</li> <li>Annual set of evidence-based knowledge products posted on FPDA website as of year 3</li> </ul>	0	2/0/3	2/2/6	2/3/10	PMU reports	Biannual reports	PMU	
		0	0	2	3				
		0	1/25	1/35	1/35				
		0	1	1	1				