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Investing in rural people

Management position on the Comments of Member States on the Utilization of resources under the IFAD Regular Grants Programme for the implementation of the Private Sector Engagement Strategy and other new initiatives

Note to Representatives

Focal points:

Technical questions:

Ashwani K. Muthoo
Director
Quality Assurance Group
Tel.: +39 06 5459 2053
e-mail: a.muthoo@ifad.org

Thouraya Triki
Director
Sustainable Production, Markets and Institutions
Division
Tel.: +39 06 5459 2178
e-mail: t.triki@ifad.org

Dispatch of documentation:

Deirdre McGrenra
Chief
Institutional Governance and
Member Relations
Tel: +39 06 5459 2374
e-mail: gb@ifad.org

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For: Information

Management position on the Comments of Member States on the Utilization of resources under the IFAD Regular Grants Programme for the implementation of the Private Sector Engagement Strategy and other new initiatives

I. Overall comments

1. Management takes note of the comments received by Member States on the paper on Utilization of resources under the IFAD Regular Grants Programme for the implementation of the Private Sector Engagement Strategy and other new Initiatives. The document was simultaneously posted for comments from both the Audit Committee and the Executive Board. This Addendum consolidates responses to the comments received through both platforms.
2. The support expressed by some Member States towards the overall intention for IFAD to strengthen its engagement with the private sector, including through innovative ways of leveraging funding, is acknowledged and highly appreciated.
3. On the other hand, Management takes note of the concerns expressed in terms of the proposed utilization of core replenishment resources to implement the private sector strategy and other initiatives, and in particular to the potential detrimental effect that doing so may have on the regular grant programme and on IFAD's mandate towards the poorest countries. Responses to specific comments are detailed in the section below.
4. Lastly, Management would like to confirm that all private sector operations will be submitted to the Executive Board for approval as stated in the IFAD's Private Sector Engagement Strategy (2019-2024) and reiterated in the related Framework that has been also submitted to the Audit Committee and the Executive Board.

II. Specific comments

5. **US comment: We are not supportive of using IFAD's core replenishment contributions to support the launch of the Private Sector Financing Program and other new initiatives. We think that these limited grant resources should be used to fund DSF commitments, which help poor countries in debt distress using concessional loans to eligible LICs and LMICs, and/or to address the gaps between the IFAD-11 replenishment target and contributions paid in thus far. While we support efforts to engage the private sector, we would prefer that IFAD fundraise using other, external sources.**
6. **Management:** Management would like to emphasize that this proposed allocation from the grant envelope is meant to be a one-off transfer to support the delivery of IFAD few first private sector operations and other initiatives, with the intention to demonstrate a catalytic role helping IFAD attract further funding, notably from private sector entities. Indeed, while IFAD has already started fundraising for its private sector operations, this one-off allocation from core resources (i.e. the regular grants programme) will help the delivery of pilot NSOs in 2020 and 2021. These will result in demonstration effect which will help IFAD build a track record. This will eventually encourage other financiers to join (e.g. foundations, Member States, global initiatives, impact investors and like-minded agribusiness companies). IFAD's ultimate objective through this type of engagement is precisely to achieve more impact in LICs and LMICs as well as fragility affected countries. Both the PFSP and ASAP+ will also provide alternative means to deliver finance to

countries in debt distress increasing funding going to those countries. The ongoing COVID-19 crisis also represents an opportunity for strong additionality in this type of engagement. Some detailed examples are provided below in response to further specific requests for clarification (see e.g. paragraphs 9; 10; 15; 16; 17; 21; 24; and 28).

Canada comment: "We would like to have more details on the decision to allocate the particular amount of US\$25 million, and the split between the funding of the private sector operations and the proposed ASAP+."

Japan comment: "It is not clear [what will be] the allocation of this set-aside resource between [those] purely utilised for the kick-start of the PSS operation and [those used] for other initiatives, inter alia, ASAP+."

Norway comment: "What does it imply that you changed the title from emphasizing kick-starting to implementation? [...] There is no mention of how the resources will be allocated between different programmes. [...] The text strengthens the lack of clarity as to whether the US\$25 million allocation is to be used for PSS alone, or also for ASAP+ and other new initiatives, as indicated in the title."

Sweden comment: "We would appreciate an elaboration regarding the distribution of the initiatives. The trade-off aspects in terms of IFAD11 [...] should also be outlined for clarification, as well as why the proposal is [for] US\$25 million. [...] There might be a need to change the title and the recommendations of approval from "other new initiatives" to ASAP+, seeing as this seems to be incorporated into the proposal. [...] Does the establishment of the Private Sector Trust Fund also fall under "other new initiatives"?"

7. **Management:** The amount of US\$25 million that is being requested is meant to support the implementation of IFAD Private Sector Strategy which was approved by the Board in September 2019 as well as other initiatives, notably ASAP+. The level of resources (US\$ 25 million) was estimated as the appropriate balance to ensure implementation of such initiatives and leveraging of additional resources.
8. The indicative split in the allocation of these funds is expected to be 50/50 with management keeping some flexibility for adjustment given the available opportunities and the recent high level of uncertainty resulting from the ongoing COVID-19 crisis. The ambition is to end up with a split that plays a catalytic role while optimizing IFAD relevance and impact. The criteria used to determine this allocation were relevance, expected development impact, potential for scaling up and contribution to relevant IFAD priorities (for private sector: job creation, economic empowerment of women and support to private sector efforts to fight climate change effects on smallholders; for ASAP+: building resilience of countries and smallholders to climate change with a focus on food security).
9. As far as the Private Sector Strategy is concerned, some pilots have been identified which could be launched in 2020, provided the Framework setting up the general rules and criteria is approved by the Board in April 2020 and resources are made available. The team's ambition is to implement up to six operations over the period 2020-2021, and to achieve a high co-financing ratio from the private sector. Management would also like to highlight that an increasing number of investors is approaching IFAD as the market is drying up as a result of the current COVID-19 crisis. IFAD will of course be selective and focused on its mandate when assessing potential opportunities.
10. On the change of title, this was done to further clarify that the resources will serve to implement a Board-approved strategy and not to initiate a private sector programme in the context of IFAD12, given that this was raised by several Member States as a possible source of confusion. In fact, the Private Sector Financing

Programme (PFSP), originally mentioned in the title, is being discussed in the context of the IFAD12 Replenishment Consultation to institutionalize IFAD private sector activities within IFAD12. This initiative will not become operational unless it is agreed to as part of the IFAD12 Consultation. The current proposed use of resources under the regular grant programme will rather serve to support the implementation of the Private Sector Strategy, which was approved in 2019. Implementing the strategy through the delivery of some operations over 2020-2021 will be critical to have a demonstration effect about IFAD's capacity to implement private sector interventions and attract concessional funding from foundations, Member States, global initiatives (e.g. GEF, Green Climate Fund, etc.), impact investors and like-minded agribusiness companies. The amount that is being requested is meant to support the implementation of the Strategy through an initial allocation to the Private Sector Trust Fund and another one to the ASAP+. Reference to "other initiatives" was retained to include priorities that may arise during the year, including those related to COVID-19 response.

Japan comment: "How much do you anticipate for transaction cost and how much for investment on private sector actors of how many from this allocation?"

11. **Management:** The resources being requested for the private sector operations will be entirely dedicated to support IFAD investment activities (both the investment and potential technical assistance), leveraging private funding at the project level and thus delivering impact. The transaction costs of processing these operations will not be covered by this allocation as they are expected to be covered by the management fees charged on resources mobilized and by the income that private sector operations will be generating.

Japan comment: "It is not straightforward [...] why lowering the ceiling for individual grant projects and encouraging the leveraging of co-financing leads to maximizing the value for money."

Norway comment: "It is argued that to increase efficiency, the ceiling for individual grant projects will be lowered. [...] In IFAD as a whole, the same argument (increased efficiency) has been used to argue for fewer and larger programmes. OED has substantiated that fewer and larger programmes have in fact increased efficiency."

12. **Management:** In preparation for a new grants policy, an analysis is being undertaken to clarify the role of grants and to learn lessons on their use. The decision to promote a lower ceiling for individual grant proposals was taken as part of this discussion on the revision of the IFAD policy for regular grants financing (currently posted for comments from the Executive Board in preparation for discussion in September 2020). The overall envelope for regular grants will be re-sized to ensure it is always financially sustainable – this will be achieved by discontinuing the notion of a fixed-percentage allocation and linking the level of resources available to replenishment outcomes. The revision of the grants policy rests on the underlying principle that the overall allocation may be lower than the current level, and that grant-funded initiatives will have to demonstrate a strong catalytic effect in leveraging other resources. The ceiling under the current grants policy is US\$3.5 million, consideration is being given to a possible reduction for example to US\$2 million, to be finalized as part of the implementing procedures for grants (following Board approval of the new policy), and retaining the possibility to opt for larger grants if and when deemed necessary or more efficient.
13. While it is true that, in the past, it has been advocated that larger grants would have lower transaction costs compared to smaller ones, this was done before the current evolution in IFAD's business model and financial architecture was initiated. Such evolution resulted in the definition of new instruments and programmes at IFAD's disposal to achieve its mandate, increased focus on private sector

engagement and the expectation for regular grants to play a catalytic role in establishing mutually reinforcing synergies between such instruments and the PoLG, as well as to leverage partnerships, including through co-financing. The emerging consensus is that to facilitate a results focus and catalytic effects grants should be smaller and implemented over a shorter period of time. Broadly speaking the total amount of grants committed per year will remain the same. Further, in the transition toward IFAD12, regular grants are expected to leverage greater co-financing than they did in the past (thus the increased value for money), and to be able to respond rapidly in different and potentially challenging contexts, one example being the COVID-19 crisis. In this sense, efficiency is also defined in terms of flexibility and potential for rapid response, which can indeed be guaranteed in financially smaller proposals.

Sweden comment: “[It is important] for the Board to get a holistic understanding of the financial elements - how they work, interact and relate - the risks and challenges involved, including how those will be mitigated, the leveraging aspects of co-financing and co-partnering of host countries, and the monitoring and evaluation; how does IFAD intend to measure successful private sector engagements?”

14. **Management:** The synergies between the PoLG, the PSFP and ASAP+ have been articulated in the IFAD12 paper and Management refrained from elaborating on such issues in this document, as these are mainly relevant for replenishment discussions. Further details will be provided about these issues during the second session of the replenishment consultations in June 2020 as part of the IFAD12 Business Model and Financial Framework paper. Yet, it is important to reiterate that the proposed allocation for the private sector will be used to implement the strategy and not the PSFP. A detailed Framework describing implementation modalities, risks and mitigation measures, monitoring, and role of Member countries has been submitted to the Audit Committee and to the Board for approval in April 2020. Within the context of IFAD12, the PSFP programme is meant to complement the work done through the PoLG, by strengthening IFAD’s contribution to SDG1 and SDG2. The Framework clearly mentions complementarity as one of the guiding principles for IFAD private sector operations.
15. Management would like also to emphasize the time pressure to start delivering on private sector activities, given that: (i) the Private Sector Strategy is already approved and a mid-term review assessment is planned for the end of 2021; and (ii) it is expected that, in the current COVID-19 pandemic context, public resources will not be sufficient to cover losses and challenges. This will result in a huge need to leverage private sector funding to support economic recovery and provide rapid response. Therefore, the proposed allocation will provide valuable seed funding to act quickly and in an impactful manner in leveraging private investment, preserve jobs and help smallholders by ensuring income and other services.
16. Management also considers that, if the PSFP is approved as part of IFAD12, private sector activities will be institutionalized and their resourcing will be linked to the replenishment. Should IFAD already have some track record at that point in time, this is expected to help attract more funding into the programme.
17. Management would also like to emphasize that this proposed allocation from the regular grants programme is meant to be a one-off transfer to support the delivery of the first few operations from the Private Sector Strategy and other initiatives, while at the same time playing a catalytic role. Indeed, while IFAD has already started fundraising for its private sector operations, this one-off allocation would be instrumental in helping it deliver pilot NSOs in 2020 and 2021. This will build a track record and encourage other investors to join which is ultimately expected to result in increased flows into LICs and LMICs. Hence, this ad hoc allocation should

be seen as a 'boost' from IFAD to help mobilize private sector funding as per the Addis Ababa call to action.

Sweden comment: "This paper would benefit from demonstrating the holistic approach, the interconnection and intended synergy effects among the financial elements."

18. **Management:** Indeed, through these new work streams (private sector and ASAP+) IFAD is seeking to scale up its impact in favour of small-scale producers and rural SMEs in the most fragile and vulnerable countries, building climate and environmental smart resilience, adaptation and mitigation for sustainable agriculture and agribusiness development. More specifically, through private sector activities, IFAD will be able to crowd-in private sector investments and leverage private sector know-how and innovation for the benefit of small-scale producers and rural communities, with a particular focus on job creation, economic empowerment of women and climate change adaptation and mitigation. In order to tackle climate change as one of the key underlying causes of food insecurity, and building on the experience of Adaptation for Smallholder Agriculture Programme (ASAP), IFAD is also seeking to establish ASAP+, which will provide grant-based climate finance particularly to LICs. These two activities are meant to complement and strengthen the results delivered through the PoLG and other IFAD activities creating synergies that allow IFAD to scale-up its impact. Embedded in the new United Nation's Sustainable Development Cooperation Framework (UNSDCF), this strengthened country-level programme approach enhances IFAD's ability to contribute to the SDGs.
19. Synergies will be ensured through close coordination and the use of COSOPs as the framework to identify complementary activities. Assessing complementarity will also be part of the review process of projects implemented under these work streams. Further details about implementation modalities of private sector activities are provided in the Framework that was submitted to the AC, as mentioned above. A document describing the implementation modalities of ASAP+ will also be prepared by management.

Sweden comment: "Reiterating to the substitutions risk mentioned regarding the funds, the reasoning around this challenge in the light of IFAD12 replenishment would be appreciated. It goes without saying, competing and crowding out among resources must be avoided, and to prepare the ground for the replenishment discussions in June, we believe this challenge should be sorted out before."

20. **Management:** The use of resources under the IFAD11 allocation for the regular grants programme will not have a substitution effect for IFAD12. These grant resources will in fact be used as a one-off boost to help implement the private sector strategy and ASAP+ during IFAD11 and play a demonstration effect for the approval of the PSFP by the IFAD12 Replenishment Consultations. The approval of the PFSP will then allow IFAD to mainstream, structure, and scale-up its private sector activity through a dedicated window. In terms of the type of resources for the PFSP, IFAD will seek to attract concessional resources, grants and co-financing from IFIs, social investors and private sector entities. The Private Sector Trust Fund could also accept dedicated pledges in the context of IFAD12, if the PFSP is approved by the IFAD12 Replenishment Consultations. Management is already exploring measures to avoid substitution risks, which will be discussed in the context of the IFAD12 Replenishment.

Sweden comment: "Adding a layer of analysis of the challenges and risks in connection to the COVID-19 and a world in economic and social recession would also be important to consider before the April board decision."

21. **Management:** The ongoing COVID-19 crisis is creating an opportunity for this allocation to play a countercyclical role and bring strong additionality. Indeed, over the past weeks, IFAD has been approached by several social lenders and private sector SMEs whose lines of refinancing are being cut. One example for instance is a private sector social lender with a pipeline of projects that could help preserve the jobs and incomes of over 230,000 small farmers in Zambia (LMIC), Sierra Leone (LIC), Nicaragua (LMIC), Moldova (LMIC) and Kenya (LMIC). And each US dollar IFAD is asked to provide is expected to leverage at least 1 additional US dollar from the social lender in addition to second leverage effect at the level of the individual projects that this social lender will be supporting.. Some of the risks for IFAD's engagement with the private sector identified in connection to COVID-19 include: (i) deterioration of the Agri-loan portfolio performance as a result of lower sales, food losses and lower prices; (ii) reduced availability of credit and other financial services for small-scale producers due to perceived deterioration in portfolio quality; (iii) losses and closures – particularly for small rural-based cooperatives/Fis/Agri-based MFIs; (iv) Agri-SMEs losses due to limited transport, procurement and markets (especially for higher-end and/or specialized products like organic crops, certified products, beef); and (v) lower sales negatively affecting small-scale producers livelihoods.
22. It should be emphasized that the private sector will play a critical role in mitigating potential damages incurred by IFAD target population during and following the COVID-19 pandemic. IFAD is already in the process of identifying response action to address the identified risks and private sector operations could be a rapid way for IFAD to respond. Potential examples of COVID-related programmes to be sponsored could be:
- Through the PSS - Indirect Lending: provision of lines of credit for cooperatives and other rural entities that need immediate liquidity to face the business downturn, avoid bankruptcy and preserve jobs. Such a programme would not be intended to fulfill general financing needs that are part of the ongoing business needs, but only unforeseen cash needs arisen due to the systemic effects of the COVID-19 crisis.
 - Through ASAP+: COVID-19 demonstrates the need to build resilience to external shocks (e.g. through economic diversification, savings, adaptive management, strong local institutions, etc.) which makes ASAP+ all the more relevant in today's context. Moreover, ensuring that additional food losses incurring during times of crisis is essential so that communities are not doubly affected, especially in climate-stressed areas.

Norway comment: "It is stated that the setting aside 13 percent of the grants programme to new programmes would not compromise other objectives of the regular grant programme. Are there no trade-offs? If there is no cost, how are the allocations under the regular grants programme as a whole substantiated? Will measures be put in place to ensure that IFAD's limited grant resources are not diverted away from LICs and other countries least in a position to self-finance and borrow money on IFAD's regular terms?"

23. **Management:** The current grants policy does include private sector entities as eligible recipients of grant-funded proposals; in fact, "Business opportunities and partnership with the private sector" is one of the five priority areas for IFAD's global and regional grants as identified in the Strategic Guidance Note for grants 2019-2021 (approved by Management in December 2018). This means that the allocation of some resources to implement the private sector strategy does not represent a deviation from the original plans for the utilization of grant resources during IFAD11. The emergence of a fully-fledged private sector engagement strategy has simply resulted in the availability of a new and improved channel to deliver on this

Priority Area, not only through regular grants but also through non-grant and through technical assistance options.

24. Moreover, this proposed utilization of resources represents 13 percent of the overall allocation for the IFAD11 period – therefore, it does not have a major financial impact on the delivery of the programme as a whole. As explained in paragraphs 12-13, the regular grants policy is currently under revision and will be discussed by the Board in September 2020. Of course, there are trade-offs but the emerging internal consensus is that the overall grant envelope could be reduced and the grant programme focused on creating catalytic effects. The use of these funds is consistent with this view. One of the principles of the revised grants policy is the need to establish greater synergies between grants and all other lending and non-lending instruments available to IFAD to further its mandate. This will include initiatives undertaken as part of IFAD’s engagement with the private sector, as well as through ASAP+. Ensuring the necessary conditions for IFAD to develop an initial pipeline under such initiatives will allow regular grants to fully express their catalytic potential once all these instruments are up and running. Foregone resources under the regular grants programme at this point in time can be considered as an “investment” for the new grants programme to be able to establish synergies with an expanded set of IFAD tools in the transition towards IFAD12 and beyond.

France comment: We would like to underline the fact that the document, although very clear, seems rather short for such an impactful decision. France would like to reaffirm its strong support of IFAD’s Grants programme, which spearheads its unique mandate for reaching the “last mile”. Although we do understand the impact of the economic downturn on IFAD’s Private sector strategy, we are concerned about draining the Grants programme resources in order to finance an initiative which does not pursue the same ends. [...] The increased efficiency of the Grants programme, albeit laudable, does not seem like a proper justification for such a substantial cut in its resources, regardless of the opportunities provided by the Private sector strategy.”

25. **Management:** This paper builds on other documents and discussions held with the Board and, for the sake of efficiency, Management decided not to include detailed analyses that were previously communicated. This notwithstanding, Management understands this concern and agrees with the sentiment expressed in this comment. The importance of the programme and its catalytic role has been noted in the IFAD12: Strategic Directions paper and will be highlighted in a new Grants Policy. We would like to provide reassurance that this one-off allocation is meant to play a catalytic role allowing IFAD to raise more resources, notably from non-donor Member States, in order to service and deliver on IFAD mandate of reaching the last mile. IFAD does intend to strengthen its role as an assembler of finance, but will always ensure the necessary checks and balances to avoid any mission drift. The well-being of small-scale farmers and their families continues to be squarely positioned at the heart of IFAD’s interventions. IFAD’s Private Sector operations will support and serve small-scale producers through a new channel that is not the Government, but small-scale producers will remain the main focus of all NSO-funded activities.
26. Relevance and alignment with IFAD’s mandate is one of the engagement principles of the Private Sector Strategy. NSOs are in fact meant to strengthen IFAD’s development impact and complement the work that IFAD does through its PoLG. Furthermore, the NSOs review process will ensure that each private sector intervention: (i) is aligned to IFAD’s mandate; (ii) does benefit IFAD’s target group; and (iii) is complementary to the PoLG and to other IFAD investments and activities at the country level.

Germany comment: “[Would] providing an internal loan for the private sector exposure (instead of a grant) be sufficient [?]. An internal loan will at best return to core capital. The upper limit proposed for IFAD12 must not be exceeded.”

27. **Management:** A grant from the replenishment is preferred over a loan to be able to place IFAD on solid grounds towards the implementation of its Private Sector strategy. Critical arguments that support this option include: targeting priorities, the sequencing in their implementation, and the expected returns generated from the Private Sector Trust Fund. The Strategy identifies additionality as a key eligibility criterion for all new IFAD NSOs and emphasizes high impact target groups including women, youth, and private sector actors implementing climate-smart agriculture. These are underserved sectors due to inherently high risk and low returns. Investments will be made to move these vulnerable populations towards more commercial sources of finance in the future. Overall, high social returns are expected while overall financial returns will be low and potential losses could occur. The Trust Fund may eventually fundraise from more commercial sources in the future once IFAD’s reputation, experience, and foothold in the private sector is solidified. At the onset however, IFAD will need maximum flexibility in the structuring and pricing of its private sector resources as well as sufficient capital in the long term to leverage and increase financing over time. A grant would allow for such flexibility and ensure long term commitment and a strong, secure capital base from which to grow in the future.
28. A portion of the envelope would also be allocated to technical assistance activities, which will play a critical role in all future NSOs. Specific themes to be covered through TA will include: training and coaching activities to enable smallholders to implement climate-smart good agricultural practices; technical assistance grants to digital service providers to facilitate precision agriculture training and unlock new markets; and supply side technical assistance to improve financial intermediary capacity to provide client-friendly financial services.
29. The current COVID-19 crisis provides further rationale to proceed with a grant option, rather than a loan one. Management is currently analysing a few potential NSO deals, in which IFAD would likely represent the only option available to ensure continued flow of finance to smallholders during and after the COVID-19 crisis.

Germany comment: “[It is] unclear whether initial funding for the Private Sector Trust Fund is already being considered. [...] The investment of own (core) capital is not the purpose of the private sector strategy. IFAD should only use its capital to a very limited extent in advance and only for possible risk sharing, but otherwise raise private funds for the private sector business. There should be no obligation to make a supplementary payment to the new Private Sector Trust Fund by the Fund's donor countries.”

30. **Management:** The Private Sector Trust Fund would aim to facilitate contributions for the implementation of the private sector Strategy. The one-off payment from the regular grants programme would be key to leverage other resources by supporting the delivery of NSOs with a demonstration and leveraging effect. In parallel, efforts are already being undertaken to approach Member States, non-Member States and other non-state actors, including multilateral organizations, philanthropic individuals and foundations, and other interested entities, to explore their interest in providing support to the Private Sector Trust Fund in the form of grants and low cost resources. Pledges from Member States will also be accepted under IFAD12, subject to approval by the IFAD12 Replenishment Consultation. These pledges and any supplementary funding from Member States will be entirely voluntary. It is also important to clarify that this contribution is meant to be a one-

off and that there are currently no plans for IFAD to invest further own capital in private sector activities.

Germany comment: "Germany would like to postpone this proposal, waiting for details and strategic justification The USD 25 million now proposed (following the adoption of the private sector strategy) is unfortunate, both in terms of timing and scale, and in terms of the prejudicial effect for IFAD 12. In addition, since there is still no sufficient overview of the "risk containment", the proposal requires a revision / redesign. IFAD should continue to seek to raise private funds for a separate financing window and to attract "diaspora investments".

31. **Management:** Strategic justifications and technical details have been provided in the Private Sector Engagement Strategy, NSOs Framework and Management responses to the large number of questions received from Member States. Management is committed to continue engaging with Member States on any additional concern they may have. However, the timely approval of this proposal is critical. Indeed, while raising funding for a new initiative may take time to materialize, the launch of NSO pilots in 2020 and 2021 will be highly strategic in demonstrating IFAD's capacity to deliver and attract funding. This, in turn, will provide Members with the reassurance needed to consider the proposal to establish a PSFP under IFAD12. Delays in timely approving this proposal could lead to further delays of implementing IFAD private sector agenda.
32. Management would like also to reiterate the time pressure to start delivering on the private sector activities, in view of: (i) the mid-term review of the Strategy at the end of 2021; and (ii) the COVID-19 crisis.