



**IFAD**  
**INTERNATIONAL FUND FOR AGRICULTURAL DEVELOPMENT**  
**Executive Board – Seventy-Sixth Session**

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**STATUS REPORT ON THE**  
**FLEXIBLE LENDING MECHANISM**

**I. INTRODUCTION**

1. At its Seventy-Fifth Session in April 2002, the Executive Board requested that a status report on implementation of the Flexible Lending Mechanism (FLM) be prepared for discussion at its subsequent session. The key operational elements of the FLM, implications for IFAD loan portfolio and programme management, and the potential advantages and risks were elaborated in document EB 98/64/R.9/Rev.1, Flexible Lending Mechanism, when the FLM was approved (see sections IV-VII). Inputs to the present report included a review of relevant project documents and interviews with country portfolio managers (CPMs) of FLM projects. The report focuses on design elements of approved projects and their appropriateness, and assesses their implementation status to the extent possible, given that all FLM projects (FLMs) are at an early stage of implementation. The design issues examined include:

- a) justifications for structuring the selected loan projects under the FLM;
- b) articulation of 'triggers' (performance indicators) in the project design, for advancing from one phase or cycle of implementation to the next;
- c) special activities undertaken to ensure the establishment and functioning of reliable and timely monitoring and evaluation (M&E) systems; and
- d) ways in which FLM designs have addressed the issue of flexibility in budgeting.

2. The report begins with a brief review of the major characteristics of the FLM as laid out in the 1998 document. It then presents the implementation status and basic data of approved projects. The four design issues listed above are analysed, as well as other pertinent issues. Finally, the Executive Board is invited to discuss measures planned by management to build on FLM design and the implementation experience to date.



## II. MAIN CHARACTERISTICS OF THE FLM

3. In September 1998, the Executive Board approved introduction of the FLM. The rationale for this new mechanism, and its objectives, included:

- a) reinforcing participation of target beneficiaries in project design and implementation through a continuous and evolving design process that would enable IFAD “learning by doing”;
- b) allowing a sufficient time frame, in the range of 10-12 years, for the attainment of sustainable development objectives through implementation cycles of 3-4 years, with carefully selected milestones (‘triggers’) for moving from one cycle to another;
- c) increasing flexibility in design and implementation to respond to changes in beneficiary priorities and capitalize on previous experience;
- d) enhancing IFAD’s involvement in, and contribution to, project implementation; and
- e) offering Member States diversified financial instruments.

4. **Design.** The projects and programmes designed under the FLM are expected to spell out clearly the goals, long-term development objectives and planned development impact during their entire period. Programming, management and monitoring modalities should also be specified, with special attention to participatory methods, in order to support a process of ongoing performance review and validation of activities. A cyclical design process over the longer period allows flexible resource allocation and planning. Activities of the first phase are specified in detail, as are those in conventional projects, on the basis of participatory demand estimates. Subject to satisfactory performance in the initial phase, the experience gained – supplemented by preparatory and background studies and the evolution of stakeholder priorities and demand – will determine the range of activities to be supported in subsequent phases, within the framework of the set objectives and goals.

5. **Triggers.** Determination of whether the project is on track in achieving its stated long-term goals and objectives, and whether it should thus proceed to the subsequent phases, is based on a set of ‘triggers’, or milestones, that constitute an integral part of the project design and loan agreement. These include the critical physical and normative targets whose attainment is considered imperative for moving to the next phase. An appropriately established and functioning M&E is an important trigger in all projects. Assessments are to be carried out jointly by IFAD, the Government, the cooperating institution (CI) and other stakeholders. The decision to proceed to the next phase rests with IFAD management, and the Executive Board is informed accordingly.

6. **Cost estimates.** Cost estimates for FLMs reflect the cyclical design process. Detailed estimates are calculated for phase I activities only, but for the whole period for the management structure. Overall estimates for the subsequent phases are presented as lump sums and included in the loan agreement as “non-disbursing” allocations. On completion of the initial phase – and the decision by the evaluation team on whether to proceed to the next phase – a decision would be made to either distribute the unallocated funds to the loan categories, based on the articulated requirements for continued activities, or to cancel the loan if the required preconditions were not met.

7. **Loan delivery costs.** On the basis of an anticipated increase in loan sizes and an implementation period of 10-12 years for FLMs, delivery costs of FLM loans were expected to be roughly the same as those for non-FLMs, including a shift from the initial processing costs towards more implementation support from IFAD.

### III. APPROVED PROJECTS

8. **General.** From September 1998 to April 2002, there were 19 projects approved for inclusion under the FLM (as compared to 90 non-FLM projects over the same period). The complete list of these projects, regional distribution, loan effectiveness dates, loan sizes and other relevant data are given in the Annex. Of these 19 loans, seven (37%) are not yet effective; five (26%) have been effective for one year or less; and six (32%) have been effective for between one and two years. Only one loan has been effective for more than two years.

9. **Loan size and ratio in the portfolio.** A review of the average loan size of FLMs and non-FLMs indicates an IFAD-wide difference of 10% higher for the former (see Table 1). If the current average 10% mark-up of FLM loans is compared with the 50% larger average loan amount for FLMs mentioned in the 1998 Executive Board paper, delivery cost of FLM loans may actually be slightly higher than that of standard loans of 5-6 years' duration, rather than the cost-neutral position posited initially. However, this would be mitigated if the higher delivery cost eventually results in fewer projects and, in particular, fewer second phases.

**Table 1. Average Loan Size of FLM and Current Projects by Division**

Division	Average Loan Size Standard Projects (USD '000) *	Average Loan Size FLMs (USD '000)	% of FLM Average vs. Standard Loans
PA	12 191	13 394	110%
PF	15 274	15 245	100%
PI	17 619	19 543	111%
PL	16 793	16 966	101%
PN	13 351	15 432	116%
Average IFAD	14 935	16 407	110%

\* September 1998 - April 2002

10. For the period September 1998 to April 2002, the share of FLMs in overall IFAD lending stands at 19% (Table 2). The average implementation period is slightly over 10 years, to be carried out, on average, in three cycles.

**Table 2. Flexible Lending in Regional Divisions**

Division	Amount Recently Approved (USD '000) *	FLMs Approved (USD '000)	FLMs as % of Recently Approved	Average Duration of FLMs (years)
PA	322 987	66 972	21%	10.6
PF	351 210	45 735	13%	9.8
PI	434 392	117 258	27%	9.5
PL	302 792	50 899	17%	11.0
PN	244 484	30 863	13%	10.3
Total IFAD	1 655 865	311 727	19%	10.2

\* September 1998 - April 2002

### IV. CHARACTERISTICS OF APPROVED PROJECTS

11. IFAD-funded projects aim to improve the livelihoods of poor rural households. Achievement of this objective is highly dependant on the reflection of the diverse and evolving needs and priorities of target beneficiaries in project design, as well as on the participation of grass-roots communities in



implementation. The advent of the FLM has facilitated a flexible approach to design and implementation on a cyclical basis. It has also facilitated longer implementation periods in recognition of the inherently slow process of development efforts and of sustainability at the grass-roots level.

12. Institution-building and reinforcing the participation of target groups in continuous design and implementation processes are the main justifications for the flexible approach and longer implementation periods of FLMs. While these are explicitly spelled out in most current projects, presentation of the mechanisms for “managing flexibility” to achieve FLM objectives is still a work-in-progress. This section examines the major issues of FLM design (as listed in paragraph 1 above) and the degree to which they have been adhered to in approved FLMs.

13. **Justifications for structuring projects under the FLM.** The basic justifications given for nearly all FLM projects take into account the objectives spelled out in paragraph 3 above. The projects appear to be demand driven and their successful implementation calls for flexibility in design and longer gestation periods. In a few cases, additional justifications are given, such as provision of technical assistance, or testing methodologies for various purposes. These justifications appear less convincing.

14. **Articulation of triggers.** Appropriate design of triggers and their objective evaluation for different cycles of implementation is a critical aspect of FLM projects and requires the utmost attention. Ideally, they should cover the most important aspects of implementation, with a balanced view on quantitative and qualitative aspects. When they are stated in absolute terms (fixed quantities), they become fixed objectives for management to achieve before the end of each phase. This carries the risk that participatory and demand-driven methods could be compromised.

15. For most FLMs, major activities during the first phase focus on essential institutional arrangements and various operational modalities and procedures, including M&E. These necessitate a set of triggers reflecting not only physical achievement (project office, procurement of equipment, etc.), but also quality, appropriateness and functionality of institutional set-ups (project staffing, implementation manual, M&E, partnership with non-governmental organizations, sensitization and promotion programmes and results, etc.). Depending on the stage of implementation, triggers must also reflect the technical and financial viability of activities undertaken by target groups and indications of the impact on their livelihoods.

16. All approved projects have articulated sets of triggers for moving from one implementation phase to another over a 10-12-year period. There is, however, some heterogeneity in how triggers are conceived and designed, ranging from balanced focus on quantitative and qualitative triggers to relatively greater dependence on quantitative targets versus qualitative and normative indicators. Good examples of the former include (but are not limited to) projects in Bangladesh, Cape Verde, India, Malawi, Mali, Nicaragua, The Sudan and the United Republic of Tanzania. While projects exist with greater emphasis on quantitative aspects, they are in the minority.

17. The number of triggers varies from project to project, depending on the nature and scope of the project under consideration. The usual range is from 5 to 15. In some projects, however, there is a need to review existing triggers with a view to limiting their number to the minimum congruent with the expected quantitative and qualitative outcomes of project activities in each phase. It is inherent in the nature of the FLM that such issues are subject to periodic review.

18. **Monitoring and evaluation.** A functioning M&E system is indispensable for all development projects, and for FLMs in particular. For this reason, FLM guidelines call for “special provisions in the project design, for establishing a properly functioning M&E system, in an orderly and timely fashion”. To further emphasize the significance of the M&E system in FLM projects, its “proper functioning” has been singled out as one of the crucial triggers for moving from one phase to another.



19. Provisions for establishment of an M&E system are included in the design of all FLMs. However, review of the documents and consultation with CPMs indicated that specific measures, over and above those for conventional projects, are not spelled out in some project design documents.

20. **Flexibility in budgeting.** Flexibility in design and implementation requires flexible budgeting and resource allocation on an evolving basis. Thus FLM cost structures vary from those for conventional loans. The total project cost estimate covers three elements: (i) detailed cost estimates for the first phase only; (ii) management cost for the duration of the loan; and (iii) lump-sum estimates for subsequent phases, leaving their detailed elaboration until just before the commencement of each phase. The majority of approved FLM projects have applied this budgeting approach. In some cases, however, detailed cost estimates have been prepared for the entire programme.

21. Virtually all projects have justifiably stipulated that additional and more intensive IFAD and CI support will be necessary for implementation and monitoring of FLM projects. In the oldest FLM, the Mali Sahelian Areas Development Fund Programme – which is also supervised by IFAD – there is strong evidence that this is occurring. The Guatemala Rural Development Programme for Las Verapaces, which became effective in September 2001 and operational in March 2002, has been visited three times in the current year (twice by the CI and once by the CPM). Consistent and general follow-up may require further attention to budgeting for supervision and IFAD follow-up.

22. Considering the short periods within which FLM projects have been operational, meaningful assessment of implementation performance is not yet possible. Review of the Mali results will be undertaken in November 2002. This will undoubtedly be a useful exercise for IFAD-wide learning about the FLM. The box below provides an overview of this project.

23. Three additional projects (in Bhutan, Cape Verde and Rwanda) will have been effective for 2.5 to 3.0 years by the end of 2003 (see Annex). This will coincide with, or be close enough to, the completion of the first phase of those projects to allow for assessment of phase I performance. The next IFAD-wide status review (or evaluation) is thus recommended for mid-2004.

**Mali: Sahelian Areas Development Fund Programme**

**Total cost:** USD 46.0 million; **IFAD loan:** USD 22.0 million (SDR 15.65 million)  
**Approval:** 12/98      **Effective:** 10/99      **Start-up:** 12/99  
**Implementation period:** 10 years, in three phases (3-4-3 years)  
**End-phase-I review:** 11/02      **Under implementation:** 2.5 years  
**Supervision missions:** 8/00, 3/01 and 6/02 (IFAD direct supervision)

**Overall objectives:** Reduction of incidence of poverty among rural households in the Sahelian zone. Major components: (i) support to the establishment and management of associations by stakeholders for financing microprojects; and (ii) decentralized financing systems for meeting effective demand for loans and deposits.

**Triggers for moving to phase II:** (i) associations established and programme mechanisms tested and effectively adopted; (ii) training programmes completed for the establishment and operation of microprojects; (iii) 50-75% of groups in place and functioning satisfactorily; (iv) half of the target villages have undertaken at least one microproject; and (v) M&E system functioning well.

**Implementation status:** Despite somewhat slow progress in the initial periods of implementation, most, if not all, triggers are expected to be in place for moving to phase II of the project. However, additional support is needed to fully achieve triggers (iii) and (v). A June 2002 supervision mission has taken measures in this regard.



## V. CONCLUSIONS

24. In the light of the IFAD mandate and its lending objectives, the FLM appears to be suitable as an additional tool in the IFAD lending programme. In addition, given the explicit emphasis on periodic assessment of performance based on achievement of triggers, it has the potential to facilitate a more performance-based approach to lending, as well as to place greater importance on implementation. However, as with any innovative undertaking, application of the FLM to IFAD projects requires that well-conceived approaches and guidelines be fully institutionalized. In general, approved FLMs have been adequately justified and meet the prescribed objectives and design criteria for this type of lending. There are, however, areas needing further attention and refinement in order to derive the fullest possible benefit. IFAD management intends to adopt the following measures for improving future FLM design and the performance of already approved FLMs. The Executive Board is invited to comment on their appropriateness.

- **Selection of FLM projects.** FLM guidelines are available and should be followed in their entirety in the preparation of projects proposed as FLMs. Special care will be taken during Project Development Team (PDT) and Technical Review Committee (TRC) meetings to ensure that FLM-specific issues are adequately addressed. Concretely, for any project proposed for financing under the FLM, the initiating regional division will provide a clear justification to the Assistant President for the Programme Management Department at the inception stage. This choice will be re-validated at each subsequent step of the design process. TRC and Operational Strategy Committee meetings will more explicitly review justification, quality and appropriateness of triggers, management and M&E processes, and other FLM-related issues.
- **Design considerations.** Design of FLM projects should be seen in terms of a process rather than identification of detailed activities. Consequently, mechanisms for evolving planning and programming as well as for participation by target beneficiaries in implementation will be clearly specified in design documents. The “IFAD Strategy” section of appraisal and president’s reports will include specific reference to the justifications for the inclusion of the relevant project under the FLM.
- **Triggers.** These have to be carefully designed and prioritized on the basis of their significance for project performance. Their number should be limited, with emphasis on normative and qualitative results, in particular with regard to building institutions that ensure sustainability of support measures in subsequent phases. Triggers should be included in all loan agreements for FLM projects. A supervision mission to the Mali project in November 2002 will assess the phase I triggers. Building on the lessons learned during that mission, IFAD will systematically reassess the triggers of all existing FLMs and propose remedial action on a case-by-case basis, as appropriate.
- **Costing.** At the initial design stage, detailed costing will be required only for the first phase.
- **Institutional learning.** A concerted effort will be made to promote cross-unit learning within IFAD through periodic meetings among: CPMs in charge of designing new FLMs and overseeing ongoing FLMs, the General Counsel, Controller’s Office/Loans and Grants, and CIs. Participants will exchange experiences on problems encountered and best practices. For new FLMs, initiating CPMs will request participation in the PDT of at least one other CPM with experience in FLM design and implementation.
- **Implementation support.** In the context of the evolving change management process and the strategic framework’s emphasis on enhancing implementation performance and



impact, IFAD management will consider the additional resources required for implementation support to FLMs. Along these lines, several FLMs will be selected for the testing and finalization of the Office of Evaluation and Studies (OE) publication, *A Guide for Project M&E: Managing for Impact in Rural Development*. As the thrust of the guide is towards using M&E for proactive management learning and adaptation, its use can greatly enhance achievement of FLM objectives, which are very similar.

- **Evaluation of FLM experience.** Given the probable timing of completion of the first phases (see paragraph 23 above), it is recommended that an OE-conducted evaluation including selected field visits be carried out in 2004.





## BASIC DATA FOR APPROVED FLEXIBLE LENDING MECHANISM PROJECTS

Region	Country	Project ID	Project Name	Board Approval	Loan Effective	Estimated Implementation Years	Number of Phases/Cycles	Loan Amount (SDR Million)	% Distributed at 30/04/02
PA	Cape Verde	1015	Rural Poverty Alleviation Programme	08/09/99	14/07/00	9	3	6.95	9%
PA	Guinea	1135	Programme for Participatory Rural Development in Haute-Guinée	09/12/99	18/01/01	10	3	10.20	3%
PA	Mali	1089	Sahelian Areas Development Fund Programme	02/12/98	14/10/99	10	3	15.65	9%
PA	Niger	1139	Rural Financial Services Development Programme	03/05/00	08/06/01	10	3	8.80	0%
PA	Sao Tome and Principe	1027	Participatory Smallholder Agriculture and Artisanal Fisheries Development Programme	26/04/01		12	4	7.95	0%
PF	Malawi	1164	Rural Livelihoods Support Programme	12/09/01		9	3	10.70	0%
PF	Rwanda	1149	Umutara Community Resource and Infrastructure Development Twin Project	04/05/00	05/12/00	10	3	11.85	8%
PF	Tanzania, United Republic of	1151	Rural Financial Services Programme	07/12/00	12/10/01	9	3	12.80	6%
PI	Bangladesh	1165	Sunamganj Community-Based Resource Management Project	12/09/01		11	3	17.55	0%
PI	Bhutan	1094	Second Eastern Zone Agricultural Programme	08/09/99	17/05/00	8	2	6.95	17%
PI	India	1121	National Microfinance Support Programme	04/05/00	01/04/02	7	2	16.35	0%
PI	India	1155	Orissa Tribal Empowerment and Livelihoods Programme	23/04/02		10	3	16.05	0%
PI	Indonesia	1112	Post-Crisis Programme for Participatory Integrated Development in Rainfed Areas	04/05/00	31/01/01	8	3	17.50	9%
PI	Nepal	1119	Western Uplands Poverty Alleviation Project	06/12/01		11	2	15.60	0%
PL	Guatemala	1085	Rural Development Programme for Las Verapaces	08/12/99	06/09/01	10	3	10.85	9%
PL	Haiti	1171	Productive Initiatives Support Programme in Rural Areas	23/04/02		10	3	17.40	0%
PL	Nicaragua	1120	Technical Assistance Fund Programme for the Departments of León, Chinandega and Managua	09/12/99	20/06/01	12	3	10.15	4%
PN	Lebanon	1188	Cooperative Rural Finance Programme	12/09/01		10	3	10.25	0%
PN	Sudan	1140	South Kordofan Rural Development Programme	14/09/00	12/02/01	10	2	13.30	10%
Total:		19 projects						236.85	5%

PA - Western and Central Africa; PF - Eastern and Southern Africa; PI - Asia and the Pacific; PL - Latin America and the Caribbean; PN - Near East and North Africa; SDR: Special Drawing Rights

