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REPUBLIC OF AZERBAIJAN

COUNTRY STRATEGIC OPPORTUNITIES PAPER

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CURRENCY EQUIVALENTS

| | | |
|---------------|---|---------------------------------|
| Currency Unit | = | Manat (AZM) |
| USD 1.00 | = | AZM 4 900 (as of December 2002) |
| AZM 1.00 | = | USD 0.0002 |

WEIGHTS AND MEASURES

| | | |
|----------------------------------|---|--------------------------------------|
| 1 kilogram (kg) | = | 2.204 pounds (lb) |
| 1 000 kg | = | 1 metric tonne (t) |
| 1 kilometer (km) | = | 0.62 miles (mi) |
| 1 meter (m) | = | 1.09 yards (yd) |
| 1 square meter (m ²) | = | 10.76 square feet (ft ²) |
| 1 acre (ac) | = | 0.405 ha |
| 1 hectare (ha) | = | 2.47 acres |

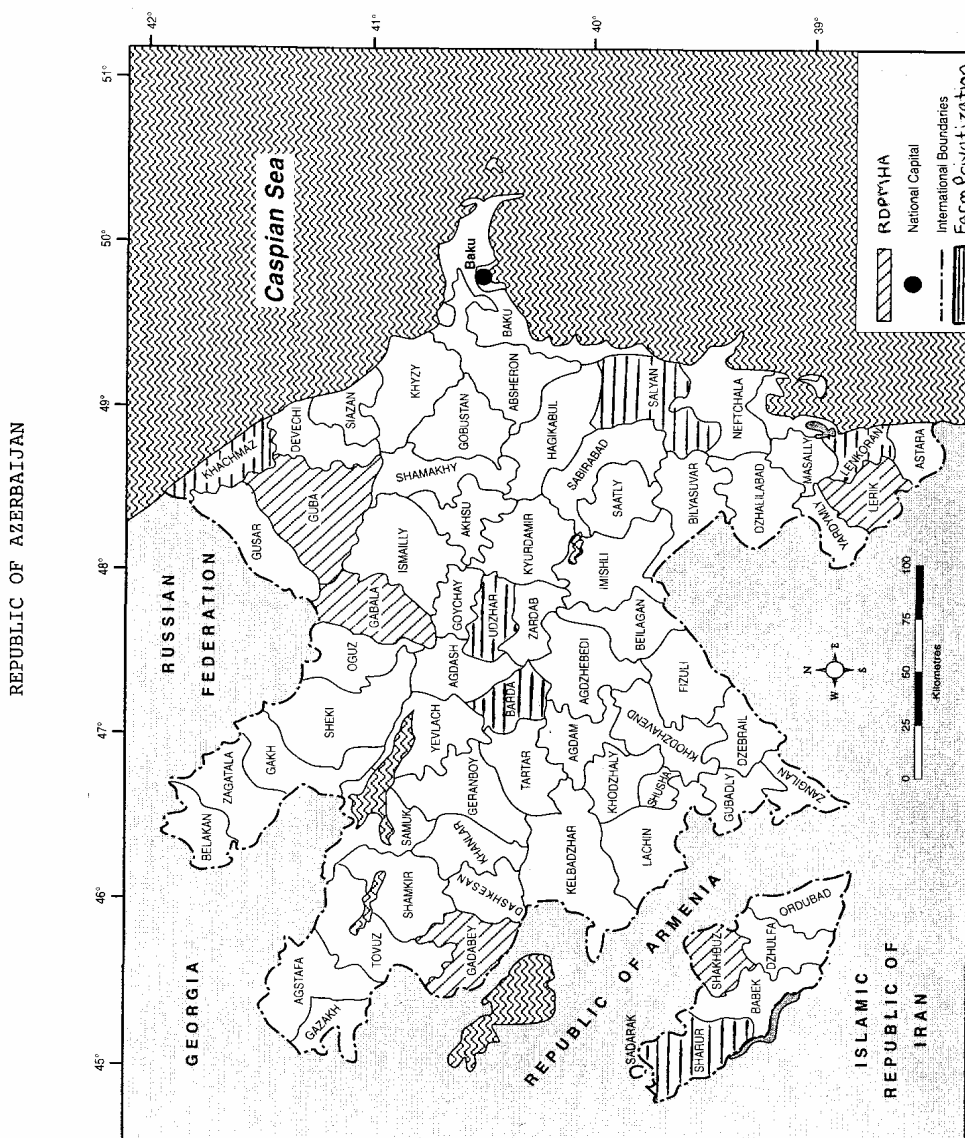
ABBREVIATIONS AND ACRONYMS

| | |
|--------|--|
| ASDAPS | Agency for Support to the Development of the Agricultural Private Sector |
| CBO | Community-Based Organization |
| COSOP | Country Strategic Opportunities Paper |
| FPP | Farm Privatization Project |
| HBS | Household Budget Survey |
| IsDB | Islamic Development Bank |
| IDA | International Development Association |
| IDP | Internally Displaced People |
| NGO | Non-Governmental Organization |
| PIM | Participatory Irrigation Management |
| RDPMHA | Rural Development Programme for Mountainous and Highland Areas |
| PRSP | Poverty Reduction Strategy Paper |
| SME | Small and Medium Enterprise |
| WUA | Water Users' Association |

GOVERNMENT OF THE REPUBLIC OF AZERBAIJAN**Fiscal Year**

1 January – 31 December

MAP OF THE PROJECT AND PROGRAMME AREAS



Source: Government of Azerbaijan.

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.

REPUBLIC OF AZERBAIJAN

IFAD PORTFOLIO OVERVIEW

| | |
|---------------------------|---|
| Project Name: | Farm Privatization Project |
| Initiating Institution: | IFAD |
| Cooperating Institution: | International Development Association (IDA) |
| Lending Terms: | Highly Concessional |
| Executive Board Approval: | 29 April 1997 |
| Loan Effectiveness: | 24 July 1997 |
| Current Closing Date: | 31 December 2003 |
| Loan Acronym: | L-I-447-AZ |
| Denominated Currency: | Special Drawing Right (SDR) |
| Approved Loan Amount: | SDR 6 450 000 |
| Loan Disbursements: | SDR 5 935 640.72 (92.03%) |

| | |
|---------------------------|---|
| Project Name: | Rural Development Programme for Mountainous and Highland Areas |
| Initiating Institution: | IFAD |
| Cooperating Institution: | United Nations Office for Project Services (UNOPS) |
| Lending Terms: | Highly Concessional |
| Executive Board Approval: | 13 September 2000 |
| Loan Effectiveness: | 1 July 2001 |
| Current Closing Date: | 31 March 2009 |
| Loan Acronym: | L-I-542-AZ |
| Denominated Currency: | SDR |
| Approved Loan Amount: | SDR 6 900 000 |
| Loan Disbursements: | SDR 490 959.77 (7.12%) |

EXECUTIVE SUMMARY

Azerbaijan became independent in 1991, following the collapse of the Former Soviet Union. In 1991-1995, the economy was affected by the breakdown of the production system, loss of Soviet Union markets, political instability and war, which led to a drop of about 70% in the country's productive capacity. Since 1995, the Government has launched a structural adjustment programme and a series of reforms to achieve macroeconomic stability, and renewed economic growth. The economy is being progressively liberalized and oil production stepped up, and land reform has been completed over 1.3 million ha of cropland (land distributed to some 850 000 rural households). The contribution of the private sector to gross domestic product has risen to 70%.

Azerbaijan has a highly diversified agricultural sector covering about 4.2 million ha – more than 1.3 million ha of which are under irrigation – that is now facing a number of serious challenges.

The number of people living in poverty account for 49% of the population and those living in extreme poverty for 17%. While there are far more poor people in the urban areas, poverty affects 42% of the rural population. The number of people employed in agriculture rose from 32% of the population in 1991 to 41% in 2000, revealing a worsening urban unemployment situation and resultant 'return to the land'. Pervasive rural poverty has many causes, including inadequate maintenance of rural infrastructure, weak agricultural services, obsolete technology, poor management capacity, the collapse of the marketing system and poor access to financial services. As a result of the armed conflict with Armenia, approximately one million people, or 12% of the country's population, are refugees or internally displaced persons (IDPs). These persons have been temporarily resettled, mostly in the urban areas, and survive on humanitarian aid.

With assistance from the international community, the Government issued a Poverty Reduction Strategy Paper (PRSP) in October 2002, setting out its strategy for ensuring macroeconomic stability, creating an enabling environment for increasing income-generating opportunities, improving health and education services and infrastructure, and for the reform of social safety nets. As far as the agricultural sector is concerned, the main thrusts aim at ensuring secure property rights, rehabilitating irrigation systems, introducing participatory irrigation management, upgrading infrastructure, improving access to rural finance, promoting marketing channels and market links, providing support for processing, developing new forms of market-oriented rural organizations, and promoting non-agricultural employment-generating rural enterprises.

To date, IFAD has contributed to the financing of two projects in Azerbaijan: the Farm Privatization Project (FPP), cofinanced with the International Development Association of the World Bank; and the Rural Development Programme for Mountainous and Highland Areas). These interventions provide a number of pertinent lessons for future strategy formulation. Under FPP, registration of land titles and the issuance of title documents have given farmers security of tenure and confidence, facilitated the emergence of an active private land market, and allowed land to be used as collateral for credit. The organization of farmers into water users' associations (WUAs) has demonstrated that participatory irrigation management (PIM) gives them a greater sense of ownership and improves prospects for the sustainability of irrigation systems. Farmers now accept that irrigation water is not provided free-of-charge and that it should be put to the best use. Azerbaijan is acquiring useful experience with regard to credit delivery through WUAs and credit unions the mobilization of savings should be encouraged and funds provided for long-term investment. FPP has also clearly established that constrained marketing possibilities and links caused by the collapse of the Soviet system are impoverishing the country's rural sector and leading to greater subsistence production, all of which is putting a brake on the commercialization of agriculture.

The objective of IFAD's strategy in Azerbaijan is to help the Government to reduce poverty on a nationwide basis. The PRSP provides the overall framework for action on the part both of the Government and of the donor community, demonstrates the former's commitment to reducing poverty, and sets out a policy framework and list of priorities. IFAD will provide support within the overall framework of the PRSP, concentrating on initiatives targeted at rural areas and thrusts that emphasize the dominant role of agriculture in the rural economy. The main thrusts of IFAD's country strategy in Azerbaijan are as follows:

Irrigation System Rehabilitation and Participatory Irrigation Management (PIM)

Experience elsewhere has shown that PIM can have a significant impact in terms of greater water-use efficiency, better scheduling and reduced social conflict. However, introducing PIM may necessitate up-front investments in system rehabilitation as many of the irrigation facilities are in such a poor state of repair that beneficiaries are unlikely to rehabilitate them without help.

Improve Produce Marketing Arrangements and Links

With the collapse of the former Soviet Union and limited effective demand within the country, agricultural producers were unable to sell their products. The availability of foreign exchange from oil revenues and the total freeing-up of imports resulted in competitive goods flooding the domestic market. Local production was unable to compete on the domestic, let alone export, markets, and farmers were driven even further into subsistence production and to selling their few assets just to survive. IFAD-financed initiatives will seek to improve the competitiveness of the country's agricultural produce by supporting the establishment of farmer organizations and other rural institutions so as to improve the small farmers' negotiating ability, both with the state and the market. IFAD will also seek to facilitate the access of such organizations to business training, skills transfer and credit, and support all marketing phases, including collection/grading/packaging, infrastructure for the physical development of produce markets, and the identification of new market potential.

Encourage the Development of Off-Farm Income Generation

The farms, including family farms, allocated under the privatization process are so small that they are unlikely to enable the farmers to rise out of poverty. The development of a land market is likely to produce larger and more economic holdings but may also lead to more landless people. Furthermore, the rural areas lack many services and products that might more efficiently be produced and/or made available locally, while agricultural produce could be processed locally in small and medium-size enterprises (SMEs). IFAD's strategy, therefore, will be to support the rehabilitation and/or development of rural SMEs, which would lead to the creation of non-agricultural employment at the local level and reduce the need for short- and/or long-term migration both to the cities and abroad. The strategy will be to provide SMEs with technical and management training, facilitate access to rural financial services, and support business development services.

Improve the Access of the Poor to Rural Finance

Although rural population is slowly developing a credit culture, this will need to be supported and strengthened. As a general policy, IFAD will support the creation and consolidation of both the provision of micro, small and medium rural credit and the mobilization of savings in rural areas. It will also support rural financial intermediaries through the banking system, establish rural finance structures within communities and among smallholders, and encourage the creation of credit unions and savings and loans associations.

Develop the Capacity of Participatory Organizations

The formation and promotion of community-based organizations (CBOs) as vehicles of change and delivery are essential elements of IFAD's strategy for targeting and empowering the rural poor. Community development activities to organize, strengthen and empower the farmers and the rural poor, including women, will be an integral part of the strategy. This process will benefit from the high level of literacy among the population.

Gender Mainstreaming

Since independence, while women have in principle retained their equal status in all fields of activity, the reality is that they are losing much of their autonomy as their economic status has fallen and the 'traditional' customs of male authority have reasserted themselves. It is important that IFAD projects should help women to improve their lot and prevent any further deterioration of their status by ensuring both that they receive a fair share of programme resources and by making sure that activities with a major economic impact on the family are evenly distributed between men and women.

In Azerbaijan, the operations of international and non-governmental organizations (NGOs) operations are mainly directed to providing relief and support to IDPs, although some of these organizations have shown interest in rural development and are increasingly involved in community organization. However, there is much suspicion among the public and within government as regards the purpose and transparency of their operations. Capitalizing on experience gained from NGO involvement in implementing FPP and other donors' projects in Azerbaijan, IFAD intends to focus on NGOs as potential service providers and/or partners.

Making the transition from a centrally planned into a market-based economy calls for major policy decisions and changes in the legal framework. These may have a significant impact on the distribution of rights of ownership, the incentive structure for production and investment, the social behaviour of individuals and communities, and on the country's poverty reduction objectives. IFAD should engage in policy dialogue with the Government with a view to ensuring the adoption of pro-poor policies and join with other donors in pursuing a constructive policy dialogue agenda, using projects as entry points for such dialogue on the following issues:

- **Vision of rural development.** The traditional mindset of government and civil service officials is still far from sympathetic towards grass-roots participatory initiatives. Moreover, many NGOs and CBOs are still very weak and not sufficiently participatory in themselves. These institutions should be strengthened and helped to become more representative of civil society and of the poor in particular.
- **Access to financial markets** is extremely limited due to the country's historical association with the former Soviet Union's central planning mechanism. IFAD and other donors are making every attempt to introduce the concept of credit to farmers, create collateral through land privatization and markets, establish modalities for rural financing and solicit the support and participation of CBOs, user associations, credit unions, loans and savings associations and NGOs.
- **Legal framework for rural finance.** At the present time, credit unions and other rural finance institutions are not allowed to mobilize savings, which both limits their outreach and increases their borrowing costs. It is important that the legal framework for rural finance be reoriented so as to allow such institutions to provide savings and other financial services and establish the necessary regulatory environment in which such activities may be conducted with minimum risk to savers.

REPUBLIC OF AZERBAIJAN
COUNTRY STRATEGIC OPPORTUNITIES PAPER

I. INTRODUCTION

1. IFAD support to Azerbaijan, with its transition from a centrally planned into a market-based economy, commenced in 1997 with the Farm Privatization Project (FPP), which it cofinanced with the International Development Association (IDA) of the World Bank. In 1999, citing similarities in the natural agricultural resource base, shared problems and market constraints – a legacy of the collapse of the former Soviet Union and its exchange markets – IFAD formulated a joint Subregional Strategic Opportunities Paper for Azerbaijan and Georgia. On the basis of that paper, IFAD developed its second intervention in Azerbaijan, the Rural Development Programme for Mountainous and Highland Areas (RDPMHA), as a long-term commitment to mountain area development in the Caucasus. In 2002, IFAD decided to review its operational strategies in Azerbaijan and Georgia and to develop a Country Strategic Opportunities Paper (COSOP) for each country.

2. Formulation of the present COSOP was based on an interactive and iterative consultation process, including a workshop held in the capital city of Baku on 20 November 2002. The workshop was held for the purpose of explaining the conceptual framework and thrust of the proposed country strategy, consulting and interacting with major stakeholders and partners to obtain feedback, enhancing participation and local ownership of the proposed strategy, and validating the conceptual framework, its relevance and implementability. Senior government representatives, including the First Deputy Prime Minister for Agrarian Reform and the Minister for Agriculture, attended the workshop. Participants included representatives of the Government (Cabinet, Ministries of Agriculture and Finance, Agency for Support to the Development of the Agricultural Private Sector (ASDAPS), and of the poor and their organizations, donors, non-governmental organizations (NGOs) and community-based organizations (CBOs).

II. ECONOMIC, SECTORAL AND RURAL POVERTY CONTEXT

A. Country Economic Background

3. Azerbaijan became independent in 1991 with the collapse of the former Soviet Union. Far from being a smooth process, the collapse led to economic disintegration, political turmoil and a conflict with neighbouring Armenia over the Nagorno-Karabakh region that resulted in the loss of 20% of Azerbaijan's territory and the displacement of almost one million people. The country subsequently experienced the worst economic and social services collapse throughout the entire Commonwealth of Independent States.

4. Azerbaijan covers an area of 86 600 km², and borders on the Russian Federation and Georgia in the north, Iran to the south, Armenia to the west and the Caspian Sea to the east. The Nakhchivan Autonomous Republic is part of Azerbaijan, although separated from the rest of the country by Armenia, and provides a narrow border with Turkey. The country covers diverse landscapes and climatic zones, as a result of variations in elevation from below sea level to more than 3 000 m above sea level. Around 43% of the area of Azerbaijan is situated at more than 1 000 m above sea level. The area is drained by two systems: the Kura River drains the central area, while the Araz River drains the southern highlands, including Nakhchivan. Both rivers originate in Turkey and flow into the Caspian Sea.

5. The population is estimated at 8.19 million (2002), growing at a rate of 1.3% per annum. The declining population is attributed to out-migration and a drop in the birth rate from 26.3 to 14.6/1000 for 1990 and 2000, respectively. The rate of urbanization is high: in 2000 it was about 51%, slightly

less than the high of 54% in 1989. The capital city, Baku, accounts for an estimated population of 1.7 million, or 21% of the population.

6. After independence, Azerbaijan faced a number of serious political, social, economic and military challenges. The year 1990 saw the collapse of the production system, high inflation, food deficits and political instability and, although a number of policy issues were taken in 1991-95, to ease social tensions (minimum wage legislation, increase in state benefits) and introduce elements of a market economy, the economy continued to slide. In 1995, the gross domestic product (GDP) was estimated at 44% of the 1990 level, and household consumption expenditures fell by about 50%. Since then, the Government has launched a series of reforms aimed at achieving macroeconomic stability, and renewed economic growth and a structural adjustment programme. Furthermore, with the stabilization of the political situation, Azerbaijan has been able to conclude a number of production-sharing agreements with foreign oil companies.

7. As a result of the foregoing, by 2001, the budget deficit had been reduced to 2% from 10% in 1994, lending rates were reduced to 7% from 250% in 1994, the country's foreign exchange reserves grew considerably and inflation dropped to just 2%. The privatization process was completed for 29 000 small and 1 000 medium and large-sized enterprises, and the private sector's contribution to the economy grew to 70% of GDP. Land reform was completed over 1.3 million ha of cropland, which was distributed to some 850 000 rural households. While the pattern of economic recovery is dominated by the oil sector, strong growth has been registered across different sectors, including agriculture. Compared with 1995, in 2001, GDP increased by a factor of 2.5, (bringing it to an estimated USD 660 per capita) industrial production by 3.5, agricultural production by three and foreign trade by 2.2.

B. Agricultural Sector and Rural Development

8. With nine agro-climatic zones, due to variations in elevation and rainfall, Azerbaijan has a highly diversified agricultural sector. Agricultural land (cropland, pastures and range) comprises about 4.2 million ha, or 49% of the total land area. Due to low rainfall, which averages less than 300 mm per year, more than three quarters of the cropped area of 1.5 million ha is under irrigation. Major crops include wheat, barley, forage crops, cotton, tobacco, vegetables, and grapes and fruit orchards. Azerbaijan is basically self-sufficient in food.

9. Agriculture, now next in importance to the oil sector, accounted for about 20% of GDP in 1997-2001. Some 31% of the labour force is employed in agriculture. Spurred by the land reforms (land privatization and registration, irrigation rehabilitation and farmer organization) launched in 1995, agriculture grew at 7-13% per annum between 1995 and 2001. There have been significant changes in the areas devoted to major crops and in productivity gains. The area put down to grains (mainly wheat) has increased from 584 000 ha to 648 000 ha and average yields have grown from 1.5 t/ha to 2.4 t/ha. The areas under potato and vegetables increased from 24 000 ha and 40 000 ha respectively, to 53 000 and 57 000 ha, but yields are still somewhat lower than in 1995. The area planted to cotton has decreased from 264 000 ha to 101 000 ha, with yields falling from 1.3 t/ha to 0.9 t/ha. The area under grapes and fruit has also declined dramatically from 181 000 ha and 136 000 ha to 14 000 ha and 83 000 ha, respectively, while yields have stagnated for the last ten years at around 3.5 t/ha, and remain extremely low by world standards.

10. Azerbaijan's post-Soviet agricultural sector faces a number of serious challenges. For more than 70 years under the former Soviet Union, agricultural production was not determined by the principles of comparative advantage or market competition but rather on the basis of predetermined specialization within a given closed market. As a result, the sector adopted highly cost-inefficient, out-dated and non-sustainable technologies. It also suffered from the lack of maintenance of irrigation systems, obsolete agricultural machinery and the total lack of or limited access to rural financial markets. Furthermore, the collapse of the former Soviet Union led to unprecedented produce market failures. The emerging agricultural sector is in need of modern extension services as well as

appropriate technical packages. Decision-making that was the prerogative of high-level officials is now vested in private landowners that were the recipients of the privatized land. These new owners, for all practical purposes, are ex-farm workers with very limited managerial capacity or farming skills. Despite the importance of agriculture in Azerbaijan, the discovery of increasing amounts of ever-greater reserves means that it is now of secondary importance.

11. Agriculture's share of exports was 10% in 1994, compared with about 30% prior to independence. This decline was both relative thanks to increased oil production and exports, and absolute due both to both the country's traditional markets for wine, cotton and other agricultural commodities and to the drop in output. Falling production and productivity are attributed to the shortage of inputs, agricultural machinery and equipment, deterioration of irrigation infrastructure and salinity. Other limiting factors are poor availability of, and access to, rural credit, limited access to markets and loss of competitiveness on export markets.

C. Constraints on, and Opportunities for, Rural Poverty Reduction

12. Although Azerbaijan did not receive subsidies from the central government of the former Soviet Union, it ranked tenth among the 15 Soviet Republics in terms of living standards. Moreover the average monthly wage in the country was one third less than that of the former Soviet Union average, whereas at that time the wage bill represented more than 70% of the population's earnings. The result was that, by Soviet standards, in 1990, more than 35% of the country's population was living below the absolutely minimum subsistence level.

13. Azerbaijan harbours an estimated one million refugees and internally displaced people (IDPs) or 12% of the population. For the most part, refugees are Azerbaijanis who returned to the country after the break up of the former Soviet Union, whereas the IDPs mainly come from the Nagorni-Karabakh region and surrounding areas following the conflict with Armenia. These people have been temporarily resettled, mostly in urban areas, and survive on humanitarian aid

14. As part of its preparations for formulating the country's poverty reduction strategy, the Azerbaijan State Statistical Committee launched a new Household Budget Survey (HBS) in 2001, which set the poverty line at AZM 120 000 (USD 25.8) per capita per month and the extreme poverty line at AZM 72 000 (USD 15.5), estimating that about 49% of the population live in poverty and 17% in extreme poverty. The gini coefficient stands at 0.35. While the urban areas contain more poor people, poverty affects 42% of the rural population. The lower incidence of poverty in the rural areas attributed to the fact that since rural people rely on their own food production, their average per capita food expenditure is 62% that of urban households (USD 11.6 rural; USD 18.5 urban). As the poverty line is mainly calculated on the basis of the food basket there is an overall skewed view of poverty, with insufficient consideration to social services and physical infrastructure. If these items were better covered, the balance between urban and rural poverty would be shown differently: the rural population suffers more from the collapse of infrastructure, unreliable supplies of electricity and gas, and worsening access to health and education services. The largest difference in expenditure relates to health, with rural people spending USD 0.5 per capita/month on health compared with USD 2.0 spent by the urban population.

15. Health data are good indicators of poverty. In the case of Azerbaijan, these show that the situation has improved in the decade since independence, with the infant mortality rate dropping from 23/thousand in 1990 to 12.5/thousand in 2001 and the mortality rate of children under five years of age falling from 40.5/thousand to 25/thousand in the same period. However, reduced optimism about the future is reflected in the total fertility rate, which has dropped from 2.8 to 1.8 children/woman during the period since 1990. The decline in maternal mortality is less significant (from 28.6 per 100 000 births in 1989 to 25.4 in 2001), but the number of abortions dropped from 22.1 per 1 000 women in 1989 to 7.9 in 2001, thanks to the Government's policy for promoting contraception.

16. Households headed by better-educated persons are less likely to be poor. In terms of education, there is now a clear difference between the sexes: women are over-represented at technical colleges that provide a lower level of education than universities, where men are over-represented. While enrolment rates remains high, the quality of education has deteriorated in recent years, especially since teachers' salaries are very low and no equipment and supplies are available. This situation is likely to influence the future gender distribution.

17. The number of people working in agriculture rose from 32% in 1991 to 41% in 2000, revealing both a worsening urban employment situation and a 'return to the land' by those who no longer earn industrial or other urban incomes. According to the HBS, increased agricultural employment is also a consequence of the privatization of land and its distribution to most of the rural population, thus providing agricultural employment opportunities for people who were previously engaged in other types of work.

18. In regional terms, the highest poverty rate is to be found in the Absheron-Guba region (58%) – the most urbanized part of the country – and the lowest in Shirvan (38%) in south-east. The areas of central Azerbaijan (Mugan-Salyan, Ganja-Gazakh and Karabakh-Mil) have a poverty rate of over 50%. However, in terms of extreme poverty, the highest rates are to be found in the urban area of Absheron-Guba (25%), the rural areas of the north-western mountain areas of Sheki-Zagatal (27%), and the central areas of Mugan-Salyan (20%) and Karabakh-Mil (21%)

19. Larger households, especially those with more than three children, are more likely to be poor; those with no children have a lower-than-average poverty rate (38%). Households of more than six persons show a poverty rate of 63%, whereas those headed by persons of more than 60 years of age account for 53% of such households among the poor.

20. It is hardly surprising that 63% of all IDP households and 55% of refugee households are poor. The difference here may be explained by the higher level of support available for refugees from international agencies. Recent legislation allowing the distribution of land to IDPs and refugees may assist in reducing their levels of poverty.

21. There are a number of causes for the currently pervasive rural poverty, for example:

- (a) failure to maintain the irrigation and drainage systems and the breakdown of rural infrastructure and power supplies;
- (b) lack of agricultural services, the collapse of the input supply system and the inability of farmers to apply appropriate technical packages (for both technical and financial reasons);
- (c) collapse of the Soviet-era marketing system and processing industry and the slow emergence of alternatives;
- (d) limited opportunities for accessing credit for farm investments; and
- (e) lack of farm management capacity and decision-making ability among former farm workers-turned-land owners.

D. National Strategy for Rural Poverty Reduction

22. With the assistance of the International Monetary Fund and World Bank, the Government issued a Poverty Reduction Strategy Paper (PRSP) in October 2002. To that end, the Government established a number of task forces with broad participation from all national institutions, political parties, NGOs and the donor community. These task forces provided in-depth analyses of issues relevant to poverty in each sector and outlined both the plans and policy measures needed to deal with such issues.

23. As presented in the PRSP, the Government's poverty reduction strategy is to:
- (a) Create an enabling environment for increased income-generating opportunities;
 - (b) maintain macroeconomic stability;
 - (c) improve the quality of, and equity in access to, basic health and education services;
 - (d) upgrade infrastructure, including roads, utilities, communications and irrigation;
 - (e) reform the existing system of social protection to provide more effective protection for the vulnerable; and
 - (f) improve living conditions and opportunities for the refugee and IDP population.
24. It was also recognized that the development of agriculture, within the framework of a comprehensive rural development strategy, is crucial for development of the non-oil sector, which in turn is critical for reducing differences in living standards between the area of the capital city and other parts of the country. The PRSP estimated that employment in agriculture had increased from about 1.1 million to over 1.5 million persons (representing some 40% of the labour force, divided almost equally between men and women) and stressed the importance of the sustainable use of the country's natural resources.
25. As far as the agricultural sector is concerned, the main thrusts of the PRSP include:
- (a) continuing the land reform and developing an institutional and legal framework to ensure secure property rights and the development of land markets;
 - (b) rehabilitating irrigation systems and introducing of participatory irrigation management (PIM);
 - (c) improvements in agricultural infrastructure (services, veterinary, processing, marketing);
 - (d) ensuring easier access to credit and other rural financial services;
 - (e) promoting marketing channels and market links, including support to processing, packaging and produce grading;
 - (f) developing new forms of market-oriented organizations in rural areas (cooperatives, farmer unions, producer associations, etc.);
 - (g) promoting non-agricultural employment-generating rural enterprises (rural tourism, small and medium-sized enterprises (SMEs), etc.);
 - (h) setting up information systems to introduce new technologies; and
 - (i) rectifying infrastructure problems that constrain agricultural development, mainly in the water and energy sectors.

III. LESSONS LEARNED FROM IFAD EXPERIENCE

26. To date, IFAD has participated in financing two projects in Azerbaijan: the FPP, cofinanced with IDA, and RDPMHA. The Government sees the former project, which is due to close in December 2003, as having contributed to the revival of the rural sector and to the country's transition into a market-based economy. Although RDPMHA became effective in 2001, implementation has just started. While limited field implementation experience has been acquired, some lessons can already be learned from the implementation of FPP.
27. Land privatization, a prerequisite for the development of produce and financial markets, has been successfully completed over 95% of the area allocated for that purpose, i.e. 26% of all agricultural land. The remainder of the agricultural areas consists of pasture and rangeland for which disposal procedures have not yet been finalized. A legal framework for land title registration is in place, and most of the privatized land is now being mapped and registered. There is ample evidence to suggest that the registration of land titles and issuance of title documents have given farmers security of tenure and confidence that they will reap the benefits of any work or resources they use to improve their land. It is also expected to lead to the emergence of an active private land market in the near future. Farmers are now using land as collateral for credit.

28. Farmers in the six pilot areas have been successfully organized into water users' associations (WUAs). Indeed, the WUA model has been replicated in irrigated areas outside these pilot areas, although this has not been problem-free. One problem is the limited capacity of ex-farm workers-turned-farm owners to take management decisions. Another is the impact of the power structure and operating procedures of the former style of farm management on the WUAs, which have become major common interest groups. Nevertheless, a sense of the ownership of the land and irrigation facilities is developing among members. Farmers are now gradually accepting that they have to pay for the irrigation water, although the charges do not yet reflect the costs incurred by the Government. The complete elimination of subsidies is causing some difficulties, including the question of equity (since the cost of irrigation varies considerably between areas), weak managerial capacity of WUAs and low effective demand on local and international markets for the produce of newly-privatized farms.

29. Nonetheless, it has been demonstrated that PIM gives a greater sense of ownership and increases prospects for the sustainability of irrigation systems. Farmers increasingly recognize that management of water supplies, optimization of water use and application, and payment for irrigation water are essential elements for the well-being of their farms and households.

30. With practice, farmers are developing the capacity to understand the principles of credit. However, the credit programme suffers from one fatal shortcoming: low loan repayment rates that jeopardise the sustainability of credit operations. There are many reasons for this. First, there is the complete lack of a credit culture in a society that, until recently, was accustomed to receiving state subsidies. Secondly, poor access to markets has meant that farmers have found it difficult to dispose of their produce thus hindering their ability to repay loans. Thirdly, the difficult financial situation of most rural households forces them to divert credit resources to meet short-term consumption needs for household survival. Lastly, farm workers-turned-farm-owners are not well equipped to take judicious farming decisions and to effectively manage the financial resources they obtain through credit.

31. That Azerbaijan has experience with credit delivery through WUAs and credit unions points to the need for: (a) building up the capacity of both members and officers of such bodies through training and skills transfer; (b) enforcing better loan management practices; and (c) encouraging savings mobilization to increase the use of internal resources. At the present time, only short-term credit is provided, which both limits the farmers' ability to invest in farm improvements likely to have longer-term benefits and constitutes a further constraint to rural development. In addition, credit programmes suffer from limited risk management options (e.g. credit insurance schemes) and a lack of flexibility in rescheduling loans that have not been repaid due to *force majeure*.

32. Experience under FPP shows that the limited marketing possibilities and poor links caused by the collapse of the Soviet system are impoverishing the rural sector. The farm sector suffers from both weak effective demand on local markets (with competition from high-quality imported goods as a result of the expanding oil sector and liberalization of import policies) and the failure to establish international markets. Subsistence production reduces the scope for commercializing agricultural produce, limits potential funding for farm investments and may lead to severe indebtedness among the farming population. The sector should be helped to improve its competitiveness through increased productivity, better quality and reduced costs. Product processing would also help by adding value to production. Establishing farmer organizations and other rural institutions (WUAs, credit unions, etc.) and supporting these through business training, skills transfer and credit would allow farmers to exploit economies of scale in production and marketing and improve their negotiating power both on the market and with the Government.

33. Progress under the community development component of FPP has been disappointing. There is clearly a lack of understanding of, and interest in, community-based approaches both within the Government and among senior project management. Furthermore, technical assistance became necessary due to the lack of local organizational capacity, but the NGO hired to provide such services

was incapable of furnishing the necessary support as its staff suffered from the same approach constraints as those of the Government. However, that communities are keen to participate in drinking water supply schemes may provide a means for launching a new approach to activities. This demonstrates the need both to ensure that interventions and approaches that are new to the socio-economic context are implemented by institutions with the highest level of capacity and standards, and for top-quality staff capable of developing and adapting methodologies appropriate to the new circumstances. Flexibility in programming is also essential.

IV. STRATEGIC FRAMEWORK FOR IFAD

A. IFAD's Strategic Niche and Proposed Thrusts

34. The goal of IFAD's strategy in Azerbaijan is to assist the Government to substantially reduce poverty and improve living conditions (increased incomes and food security) among disadvantaged and resource-poor communities. This is to be done through the development of viable small-scale farm units that contribute to protecting and restoring the environment.

35. The adoption of sound macroeconomic policies that would stabilize the economy, use oil revenues in a judicious manner, enhance the competitiveness of non-oil sectors and, in particular, ensure that the non-oil productive sectors (such as agricultural) are not penalized by the appreciation of the national currency, are essential elements in the fight to reduce Azerbaijan's poverty.

36. The major opportunity for poverty reduction is in completing the transition from a centrally controlled to a market-based economy. The critical elements in that process involve expediting the transformation of new recipients of farmland from farm workers to decision-making farmers and improving farmers' access to appropriate technical packages, rural credit and input /produce markets.

37. Recognizing the depth of Azerbaijan's rural poverty and its permeation of the two main farming systems – the mountainous areas and lowlands – IFAD intends to continue its support to the irrigated sector, which constitutes the major resource for rural employment and national food security, while supporting disadvantaged communities in the mountainous and highland areas. However, while past support was directed to piloting efforts in small areas scattered throughout the country, future efforts will be directed to scaling up successful experiences to cover sizeable and contiguous areas.

38. The PRSP provides the overall framework for government and donor action aimed at reducing poverty and lays the basis for sustained economic growth. The paper demonstrates the Government's commitment to reducing the country's poverty and to drawing up both a policy framework and a list of priorities. IFAD will provide support within the overall framework of the PRSP, concentrating on initiatives targeted at rural areas and thrusts that emphasizes the dominant role of agriculture in the rural economy. The main thrusts of IFAD's country strategy are as follows:

Improving the Production, Productivity and Competitiveness of Agricultural Produce

39. **Irrigation system rehabilitation and participatory irrigation management.** Water is becoming a scarce commodity for Azerbaijani agriculture. In addition, the constrained public finance situation means that budget outlays for system operation and maintenance are becoming increasingly inadequate, which in turn leads to system failure. PIM is essential for overcoming these two constraints. Experience has shown that participatory system management leads to greater water-use efficiency, better scheduling and reduced social conflict. Farmers have accepted the notion that water is not free of charge and that they not only have to pay for it but also manage its supply and use. Future projects will continue to build on this momentum. However, the introduction of PIM may require up-front investments in system rehabilitation as many of the irrigation facilities are in such a poor state of repair that beneficiaries are unlikely to be able to rehabilitate them without help.

Improve Produce Marketing Arrangements and Links

40. It is widely accepted that the rural sector has been impoverished by lack of markets for agricultural outputs. Azerbaijan was formerly part of a large, integrated and interregional Soviet market by means of which domestic markets were supplied with agricultural and industrial products both from local sources and from elsewhere in the former Soviet Union. Producer and consumer prices were administered by the huge state planning apparatus, and were not based on principles of comparative advantage, cost effectiveness or international competitiveness. With the collapse of the former Soviet Union and the low effective demand in the country, agricultural producers have been unable to sell their produce. To aggravate the situation, the availability of foreign exchange from increasing oil revenue and the complete liberalization of import policies allowed competitive imported products to flood the domestic market. Local production could not compete on domestic, let alone export markets, as a result of which farmers were driven even further into subsistence production and to selling their few assets just to survive.

41. The re-establishing of market links represents an urgent, strategic priority for the Fund in Azerbaijan. IFAD-financed initiatives will seek to improve the competitiveness of agricultural products by supporting the establishment of farmer organizations and other rural institutions that improve the ability of small farmers to negotiate with the state and on the market. IFAD will also seek to facilitate the access of such organizations to business training, skills transfer and credit, and will support all phases of marketing, including collection/grading/packaging, infrastructure for the physical development of product markets, and the search for new market potential.

Encourage the Development of Off-Farm Income-Generating Activities

42. Even with optimum management, the extremely small individual and family farms distributed under the privatization process are unlikely to generate sufficient income to ensure living standards above the poverty line. The expected development of a land market once farmers are allowed to sell their land (five years after receiving it) is likely to produce larger and more viable holdings but may also result in many landless households. Some household members are likely to be able to find casual and/or longer-term farm employment but many will not. Rural areas now lack many services and types of produce that were previously available, but much agricultural produce could be processed by local SMEs, thereby increasing efficiency, ensuring cost-effective enterprises and producing the type of quality products that are in demand.

43. In addressing these issues, IFAD's strategy will also call for supporting the rehabilitation and/or development of rural SMEs, which would lead in turn to the creation of non-agricultural employment at the local level and reduce the need for short and long-term migration both to the urban areas and abroad. This would allow the younger generation to stay in the rural areas and to develop viable lifestyles at the local level. The types of enterprises involved might include small-to-medium-scale agro-processing (fruit, vegetables, medicinal plants, etc.), rural micro enterprises involved in the repair and manufacture of goods that are needed locally, agro-tourism, and private agricultural/veterinary service providers. IFAD's strategy will be to assist such enterprises through technical and management training, provision of rural financial services and support to business development services. Another bottleneck in promoting rural SMEs and generally improving access to markets for their products, is the limited availability of business counselling services in the rural areas. Such a capacity could be enhanced in partnership with the international and national NGO community and other service providers.

Improve the Access of the Poor to Rural Finance

44. Rural financial services are essential for the development of farming and non-farming rural enterprises. The rural population is slowly developing a credit culture but, given the history of grants and the lack of management experience of the rural population in the country, this will need to be supported and strengthened. As a general policy, IFAD will support both the provision of micro, small

and medium-range rural credit and the mobilization of savings in rural areas. It will also support rural financial intermediaries through the banking system, establish recipient and delivery structures within communities and among smallholders for rural finance, and assist in the creation of credit unions and savings and loans associations.

Develop the Capacity of Participatory Organizations

45. The formation and promotion of CBOs as vehicles of change and delivery are essential elements of IFAD's strategy for targeting and empowering the rural poor. The collapse of the political, social and economic institutions of the communisera has left behind a vacuum that will need to be filled by alternative and competent pro-poor institutions and by the people themselves. Community development activities to organize, strengthen and empower the farmers and the rural poor, including women, will therefore form an integral part of IFAD's strategy.

46. Azerbaijan has a highly literate population, which should be an important social asset and springboard for active community organization and development. IFAD's strategy will be to facilitate the empowerment of communities through inclusion of strong community development and grass-roots participatory elements (community development committees, women's organizations, WUAs, pasture-range associations, cooperatives/producer associations and credit unions) in all its projects. This will assist the population, and in particular the rural poor, to develop a spirit of initiative and self-confidence in their ability to solve their own problems and to live reasonably well within the new socio-economic environment. It will also equip them to properly manage community affairs and resources and improve their bargaining power both with the authorities and in the market place. Significant sensitization, advocacy and skills transfer at the operational and policy levels will be needed to improve the receptivity of the Azerbaijan administration to such an approach and to overcome the lack of experience within the country. This may require considerable input from IFAD, possibly on a grant basis.

Gender Mainstreaming

47. Officially, women enjoyed equal status with men throughout the Soviet period. Although there was no gender balance in the power structure, women played a major role as professionals, particularly in the lower-paying health and education sectors and in manufacturing. Since independence, while they have in principle retained equality in all fields, in reality women are now losing much of their autonomy and status as their economic status has fallen and 'traditional' male authority has reasserted itself both in practice and as the philosophical norm. It is important that IFAD projects should help women to improve their plight and prevent any further deterioration in their status. IFAD should insist that women receive a fair share, as beneficiaries and participants, of the Fund's programme resources, and that any activities that have a major economic impact on the family are evenly distributed among men and women, e.g. credit, training, farm inputs, technology, etc. If this objective is to be achieved, however, certain institutional and regulatory changes may be needed in some sectors.

B. Main Opportunities for Innovations and Project Interventions

48. The efficient replication of the successful FPP experience, with emphasis on improving the comparative advantage of commercial production and enhancing marketing prospects, represents a major opportunity for IFAD. In the north-eastern parts of Azerbaijan, the break-up and distribution of the large farms to smallholders under the privatization programme has largely been achieved. The challenge is now how to consolidate such farms, ensure sustainable management of irrigation water, allow for economies of scale, provide rural credit and increase the small farmers' bargaining power in the market place. Major innovations will relate to efficient and sustainable PIM, effective delivery of rural financial services and establishment of profitable links to markets.

C. Outreach and Partnership Possibilities with Non-Governmental Organizations and Other Civil-Society Institutions

49. International NGO operations in Azerbaijan are mainly concerned with providing humanitarian relief to IDPs. A number of NGOs that have shown interest in rural development are now increasingly involved in community organization. National and international NGOs are required to register with the agency responsible for social welfare, and there is much suspicion within the Government and among the public regarding the objectives and transparency of their operations. In May 2002, the Government issued a Presidential Decree that required NGOs to disclose their sources of funding and spending and called for greater accountability.

50. Capitalizing on experience gained from NGO involvement in implementing FPP and other projects, IFAD intends to focus on NGOs as potential service providers and/or partners. The philosophy, approaches and mandate of service provider NGOs will need to be consistent with those of IFAD. Such NGOs must also be willing to review their approaches and practices with a view to adopting and applying new concepts and methodologies for community development and organization.

D. Opportunities for Strategic Links with Other Donors and Institutions

51. IFAD and World Bank have been strong supporters of farm privatization. Opportunities exist for benefiting from World Bank support to the institutional framework for PIM. In addition, both World Bank and the Islamic Development Bank (IsDB) have been active in the rehabilitation of the irrigation superstructure, and IFAD may create synergies with the efforts of those organizations by focusing both on the rehabilitation of on-farm irrigation systems and on PIM. In addition it should be possible to mobilize cofinancing from both the OPEC Fund and IsDB and, where the superstructure has already been rehabilitated, scale up the successful experience of the FPP on a wider scale.

52. With support from the Swiss Agency for Development and Cooperation IFAD is funding a regional collaborative programme in Azerbaijan and Georgia for mountain area development, which is implemented by the Swiss Centre for Mountain Regions. The aim of the programme is to deepen the learning process with regard to mountain-area needs and development approaches in Caucasian countries.

53. With support from Germany, IFAD is also implementing a gender-mainstreaming programme in Eastern Europe and the Newly Independent States, including Azerbaijan, funded by a technical assistance grant. Under this grant, IFAD-supported projects in each country are expected to develop proposals for pilot or complementary activities that ensure the equal access of men and women beneficiaries to development opportunities, services and resources. Such proposals will be eligible for limited financing under the grant.

E. Areas for Policy Dialogue

54. Making the transition from a centrally controlled to a market-based economy calls for major policy decisions and changes in the legal framework. These policy decisions and their legal manifestations require close scrutiny because they have a direct and significant impact on the distribution of rights of ownership (e.g. land), the incentive structure for production and investment (including food), the social behaviour of individuals and communities, and poverty reduction objectives. Policy dialogue between IFAD and the Government will be necessary with a view to influencing the adoption of policies and legal frameworks that create an enabling environment in which poverty reduction initiatives may succeed. With the experience gained from project implementation and as the politico-socio-economic situation unravels, policies and laws will need to

be revisited and adjusted. IFAD will join with other donors in pursuing a constructive policy dialogue agenda, using projects as entry points for policy dialogue on the following issues:

- (a) **Vision of rural development.** The traditional mindset of government and civil service officials is still far from sympathetic towards participatory initiatives at the grass-roots level. Much still needs to be done to persuade the Government of the positive advantages of community-based activities. Moreover, many NGOs and CBOs are still very weak and not sufficiently participatory in themselves. These institutions should be strengthened and helped to become more representative of both civil society and of the poor in particular.
- (b) **Access to financial markets** is extremely limited due to the historical association with the former Soviet Union's central planning mechanism. IFAD and other donors are making serious efforts to introduce the concept of credit to farmers, create collateral through land privatization and markets, establish modalities for rural financing and solicit the support and participation of CBOs, user associations, credit unions, and savings loan associations and NGOs.
- (c) **Legal framework for rural finance.** At present, credit unions and other types of rural finance institutions are not allowed to mobilize savings, which limits both their outreach and increases their borrowing costs. The legal framework for rural finance should be reoriented towards allowing such institutions to provide savings and other financial services and establish the necessary regulatory environment in which these activities may be conducted with minimum risk to savers.

F. Action Areas for Improving Portfolio Performance

55. **Counterpart funding problems.** With increased budgetary resources (as a result of greater oil revenues), the local funding of projects is likely to remove the major obstacles to project implementation.

56. **Participatory development.** In principle, the Government has accepted that participatory development is important and recognized the need to involve the NGO community. Further action has been agreed to facilitate the registration of local organizations, e.g. WUAs, and enhance their effective involvement in providing a variety of services to members.

G. Tentative Lending Framework

57. IFAD's programme in Azerbaijan will continue to focus on the two main farming areas: the mountainous areas and the irrigated plains of the Kura and Araz Rivers. From an operational perspective, IFAD will seek to maintain a minimum of two, and a maximum of three, ongoing operations at any given time, with at least one operation in each main farming area.

58. IFAD is already committed to a longer-term programme for the mountainous areas. The first phase of RDPMHA became effective in July 2001, but implementation through an NGO service provider was only expected to start at the beginning of 2003. A mid-term evaluation (MTE) of the project, scheduled for 2005/06, will assess implementation progress, identify successful interventions and modify non-performing activities. It should also put forward recommendations on the total duration of the project and for speeding up the pace of implementation. The MTE should also provide guidance with regard to the preparation of a second phase in 2006, which might be launched while the first phase is still in progress.

59. For the irrigated areas, the aim will be to strengthen and support the irrigation sector, based on the FPP model but adjusting design in accordance with the constraints and successes of the earlier project. A new initiative to scale up successful FPP innovations will commence in early-2003 and be hopefully finalized within the same year, prior to the closure of the current phase of FPP. The proposed new project, the Northeast Development Project, would cover a large, contiguous area in the north-eastern part of the country that receives irrigation water from the Samur River and its tributaries. Rehabilitation of the irrigation superstructure is either ongoing or will commence shortly with financing from other donors. The new project would aim to enhance the remonetization of production in the irrigated areas, increase both the farmers' share of the market and the marketability of their produce, and assist in organizing and empowering the rural poor, particularly women. This project is expected to benefit from an IFAD loan of about USD 15.0 million and possible cofinancing support from the OPEC Fund and IsDB.

APPENDIX I

COUNTRY DATA

AZERBAIJAN

| | | | |
|--|-------------------------|---|-----------|
| Land area (km² thousand) 2001 1/ | 87 | GNI per capita (USD) 2001 1/ | 650 |
| Total population (million) 2001 1/ | 8.11 | GDP per capita growth (annual %) 2001 1/ | 9 |
| Population density (people per km²) 2001 1/ | 94 | Inflation, consumer prices (annual %) 2001 1/ | 1.5 |
| Local currency | Azerbaijani Manat (AZM) | Exchange rate: USD 1 = | AZM 4 900 |
| Social Indicators | | Economic Indicators | |
| Population (average annual population growth rate) 1995-2001 1/ | 0.9 | GDP (USD million) 2001 1/ | 5 585 |
| Crude birth rate (per thousand people) 2001 1/ | 16 | Average annual rate of growth of GDP 1/ 1981-1991 | n.a. |
| Crude death rate (per thousand people) 2001 1/ | 6 | 1991-2001 | -0.3 |
| Infant mortality rate (per thousand live births) 2001 1/ | 77 | Sectoral distribution of GDP 2001 1/ | |
| Life expectancy at birth (years) 2001 1/ | 65 | % agriculture | 17 |
| Number of rural poor (million) (approximate) 1/ | n/a | % industry | 47 |
| Poor as % of total rural population 1/ | n/a | % manufacturing | n/a |
| Total labour force (million) 2001 1/ | 3.67 | % services | 36 |
| Female labour force as % of total 2001 1/ | 45 | Consumption 2001 1/ | |
| Education | | General government final consumption expenditure (as % of GDP) | 10 |
| School enrolment, primary (% gross) 2001 1/ | 98 a/ | Household final consumption expenditure, etc. (as % of GDP) | 65 |
| Adult illiteracy rate (% age 15 and above) 2001 1/ | n/a | Gross domestic savings (as % of GDP) | 25 |
| Nutrition | | Balance of Payments (USD million) | |
| Daily calorie supply per capita, 1997 2/ | 2 236 | Merchandise exports 2001 1/ | 2 315 |
| Malnutrition prevalence, height for age (% of children under 5) 2001 3/ | 20 a/ | Merchandise imports 2001 1/ | 1 675 |
| Malnutrition prevalence, weight for age (% of children under 5) 2001 3/ | 17 a/ | Balance of merchandise trade | 640 |
| Health | | Current account balances (USD million) | |
| Health expenditure, total (as % of GDP) 2001 1/ | 1 a/ | before official transfers 2001 1/ | -228 |
| Physicians (per thousand people) 2001 1/ | n/a | after official transfers 2001 1/ | -52 |
| Population using improved water sources (%) 2000 3/ | 78 | Foreign direct investment, net 2001 1/ | 129 a/ |
| Population with access to essential drugs (%) 1999 3/ | 50-79 | Government Finance | |
| Population using adequate sanitation facilities (%) 2000 3/ | 81 | Overall budget deficit (including grants) (as % of GDP) 2001 1/ | -3 a/ |
| Agriculture and Food | | Total expenditure (% of GDP) 2001 1/ | 23 a/ |
| Food imports (% of merchandise imports) 2001 1/ | 16 | Total external debt (USD million) 2001 1/ | 1 219 |
| Fertilizer consumption (hundreds of grams per ha of arable land) 2000 1/ | 13 | Present value of debt (as % of GNI) 2001 1/ | 19 |
| Food production index (1989-91=100) 2001 1/ | 86 | Total debt service (% of exports of goods and services) 2001 1/ | 5 |
| Cereal yield (kg per ha) 2001 1/ | 2 648 | Lending interest rate (%) 2001 1/ | 20 |
| Land Use | | Deposit interest rate (%) 2001 1/ | 9 |
| Arable land as % of land area 2000 1/ | 19 | | |
| Forest area as % of total land area 2000 1/ | 13 | | |
| Irrigated land as % of cropland 2000 1/ | 76 | | |

a/ Data are for years or periods other than those specified.

1/ World Bank, *World Development Indicators* CD ROM 2003

2/ UNDP, *Human Development Report*, 2000

3/ UNDP, *Human Development Report*, 2003

APPENDIX II

LOGICAL FRAMEWORK

| | Narrative Development Goal | Verifiable Indicators | Assumptions Risks |
|--------------------------------|---|---|---|
| Goals | Improve living conditions and household earnings for about 48% of the Azerbaijani population in irrigated lowland and mountainous areas: the poorest rural people | Reduction of poverty incidence to pre-1990 levels Increased remonetization of farm sector, land and products Use of oil revenues and land products for rehabilitation of rural infrastructure and market expansion Improved competitiveness of agricultural produce | Political stability prevails/political solution found to Nogorno-Kavabakh conflict Macroeconomic policies in favour of productive sectors. Oil revenues invested in social and economic infrastructure Privatization (of land and other entities) proceeds on rational basis Corruption is reduced Government/civil service managers change mindset and become more pro-poor |
| Objectives/ Purpose | Two-pronged programme: Continuation with RDPMHA – areas of concentration of rural poor Increased productivity and remonetization of farm sector Focus would be on: Support marketing of agricultural produce and improve factor and produce market Establish recipient and delivery structures within community of new smallholders for rural finance Support rural financial intermediaries Support improved technical packages and delivery mechanisms Capacity-building and expansion of grass-roots organizations/WUAs, credit associations or CBOs Support replications already initiated in WUAs Emphasis on marketing and marketability Expand produce markets Enhance competitiveness of crops | WUAs replace the old system of state-managed water distribution, and the model is successfully replicated. Credit unions and associations receive group credit and deliver the same to individual farmers Markets developed and farmers have increased production of crops with higher comparative advantage Cooperatives or similar genuine grass-roots producer organizations are created and functioning WUAs and credit unions established and functioning Capacity-building activities undertaken by the project for project and non-project CBOs Partnerships with NGOs and other civil-society institutions and project support to these activities Expansion of crop and animal production and higher productivity | Oil revenues are not ploughed back into productive sectors and Government depends on cash transfers to deal with poverty. Negative impact of oil sector on non-oil sector, particularly agriculture; negative externalities of over-valued exchange rate on competitiveness of agricultural products. Continued market failure due to lack of public investments in rural infrastructure. Lack of investments and provision of critical social and economic services (health, education, gas and electricity supplies, and drinking water supply) lead to rural out migration. Continued authoritarian approach of civil service and Government staff Replications are premature and not true to type, allowing previous Sovkhozes and Kolkhozes power structures to take over. Failure to achieve capacity-building of CBOs, whether social or productive Failure of partnerships with NGOs Failure to provide improved technical packages and delivery mechanisms to reach small farmers. Unavailability of capable NGOs, hence failure of their operations; Top-down management of investments |

STRENGTHS, WEAKNESSES, OPPORTUNITIES AND THREATS (SWOT) ANALYSIS

| Institution | Strengths | Weaknesses | Opportunities/Threats |
|--|--|--|--|
| Ministry of Agriculture | <ul style="list-style-type: none"> - Knowledge of the rural situation and technical potential of the different agricultural zones - Technically skilled personnel (agronomists, livestock experts, etc.) | <ul style="list-style-type: none"> - Centralized and bureaucratic approach; poor managerial capacity - Lack of understanding or sympathy with the market economy - Unwillingness of staff to relocate to rural areas - Unwillingness to allow farmers and community members to take initiatives and manage their own affairs | <ul style="list-style-type: none"> - Ministry and its role may be restructured to an advisory, rather than implementing, capacity - Structural adjustment may allow technically competent staff to develop an interest in setting themselves up as private service providers in agriculture skills, livestock and marketing |
| ASDAPS | <ul style="list-style-type: none"> - Has managed World Bank and IFAD projects and has some familiarity with projects financed by international financial institutions. - Has built up experience and benefited from training in market-oriented approaches. - Benefits from a number of high-quality staff. | <ul style="list-style-type: none"> - Centralized approach - Lack of commitment to participatory approach | <ul style="list-style-type: none"> - Competent management staff may be able to deal with disbursement and other necessary procedures - Over-centralization may hinder project implementation - Hostility to participatory community development approach may affect implementation of projects based on this approach |
| Committee for Amelioration and Water Management (deals with irrigation management) | <ul style="list-style-type: none"> - Experience of management of large-scale irrigation networks. - Technical expertise in engineering aspects. | <ul style="list-style-type: none"> - Opposes decentralization of the management of irrigation systems - Opposition to management systems that would undermine its control over the irrigation systems - Reluctance to hand over authority for part of the irrigation system to the WUAs | <ul style="list-style-type: none"> - Technically competent staff may be available to the private sector and WUAs; - Opposition to decentralization of irrigation could be a major hindrance to irrigation projects involving main canals |

ACTIVITIES OF OTHER PARTNERS IN DEVELOPMENT – ONGOING AND PLANNED

| Donor/Agency | Nature of Project/Programme | Project/Programme Coverage | Status | Complementarity/Synergy Potential |
|---|--|--|--------------------------|---|
| World Bank | - Agriculture and Credit Development Project | - National | - Ongoing | - Addresses issues of marketing (training farmers and others in marketing techniques and price settings) - Should establish a rural credit institution |
| | - Forthcoming Second Irrigation Project | - National | - Under design | - Could be complementary as it should cover different areas to proposed IFAD-financed project |
| Asian Development Bank | - Irrigation Rehabilitation Project | - Samur-Absheron canal and Kura river basin | - About to start/started | - Focus on main canals and physical rehabilitation of major water distribution networks; could complement by ensuring less wastage of scarce water in the major waterways |
| European Union | - Environment project | - Mountainous regions | - Ongoing | - Some technical packages may be useful for RDPMHA |
| United States Agency for International Development (through various NGOs such as Cooperative for Assistance and Relief Everywhere, etc. | - Various community development programmes, mainly with refugees and IDPs. - Microcredit programmes with same target group. | - Various locations, mostly near ceasefire line and major cities | - Ongoing | - Have some community development experience and have trained Azeri staff in community development and participatory approaches |

APPENDIX V

IFAD'S CORPORATE THRUSTS AS RELATED TO THE PROPOSED COUNTRY PROGRAMME

1. The thrusts of the present COSOP are in line with IFAD's strategic framework objectives of enhancing the capacity of the poor and their organizations (SO 1), improving the access of the poor to productive natural resources and technology (SO 2), and improving the access of the poor to financial services and markets (SO 3). It is also in line with IFAD's regional strategy for Central and Eastern Europe and the Newly Independent States (CENIS), as it calls for supporting activities that are firmly associated with the five main thrusts of the regional strategy, namely, institutional development to empower the rural poor; enhancing farm productivity; increasing opportunities for income-diversification; enhancing market links; and improving natural resource management.

2. The COSOP targets farming systems that support high concentrations of rural poor and entrusts an important role to women in the development process. Through the community-based development approach, the COSOP advocates focusing on building up the capacity of community and user organizations, such as WUAs and credit unions; enhancing their ownership of resources, particularly land and irrigation systems, and of project social and infrastructure investments, and seeking to empower the new farmers through training and extension. The COSOP also proposes consolidation of the Government's privatization efforts thereby ensuring improved access of the poor to productive assets and technology. The COSOP recognizes that the development of rural financial services is a fundamental pre-condition for sustainable economic growth and advocates support for the development of self-sufficient and sustainable community-based rural financial institutions. It also pays attention to the creation of the links and financial services essential to fostering the development of new relationships between the private sector and small-scale producers.

3. The COSOP provides insights on ways to improve implementation performance and impact. It also provides for involvement in policy dialogue with the Government and for targeting strategic partnerships with other donors aimed at creating a policy and institutional framework supportive of poverty alleviation.