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**IMPLEMENTATION OF THE FIRST CYCLE
OF THE
PARTICIPATORY SMALLHOLDER AGRICULTURE AND
ARTISANAL FISHERIES DEVELOPMENT PROGRAMME
FINANCED UNDER THE
FLEXIBLE LENDING MECHANISM**

For: Information

Note to Executive Board Directors

This document is submitted for the information of the Executive Board.

Directors are invited to contact the following focal point with any technical questions about this document before the session.

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I. INTRODUCTION

1. The Executive Board approved the creation of the Flexible Lending Mechanism (FLM) at its sixty-fourth session in September 1998. The three main differences between a loan provided under the FLM and a standard IFAD loan are as follows:

- (a) longer loan periods to allow for the achievement of sustainable development objectives;
- (b) a continuous and evolving design process through implementation of distinct, three-to-four-year cycles; and
- (c) specification of clearly defined preconditions or “triggers” for proceeding to subsequent cycles.

2. Paragraph 13 of the report on the establishment of the FLM (EB 98/64/R.9/Rev.1) stipulates that “ ... for each FLM loan and prior to the end of each cycle, IFAD management will decide whether to proceed to, cancel, or delay subsequent cycles. Management will inform the Board accordingly. The document presented to the Board will set out the lessons learned from initial cycles and their incorporation into subsequent cycles, the attainment of physical targets, progress towards meeting long-term development objectives, and achievement of the pre-conditions stipulated in the loan agreements.”

3. The present paper reports on the progress made by the Participatory Smallholder Agriculture and Artisanal Fisheries Development Programme in achieving the first-cycle triggers. The contents of this paper are based on the report of the first-cycle assessment, and on the second-cycle formulation mission carried out in September 2005.

II. BACKGROUND

4. The Participatory Smallholder Agriculture and Artisanal Fisheries Development Programme was approved by the Executive Board in April 2001 and became effective on 25 February 2003. The loan has a twelve-year duration and includes four distinct cycles of three years each.

5. The programme has been designed to provide a long-term commitment to Sao Tome and Principe, particularly in the light of the sweeping rural restructuring process under way since land reforms were launched in 1991. This commitment will enable certain objectives to be achieved in terms of professionalization of rural-sector service providers and the creation of a viable rural microfinance institution.

6. The programme’s overall objective is to improve the living conditions and incomes of women and men who earn their livings through smallholder agriculture and artisanal fisheries.

7. The programme comprises four components:
8. **Restructuring of the rural sector.** This component aims to: (a) strengthen grass-roots associations; (b) develop a functional literacy programme for grass-roots associations; (c) strengthen professional organizations; and (d) contribute to the development of rural local councils.
9. **Strengthening of services provided to the rural sector.** Through this component, the programme aims to set up viable and sustainable rural-sector services, complementing the services provided through the funding of other donors. Among others, it is to: (a) develop decentralized financial services; (b) provide extension services (crops, small livestock and forestry); and (c) develop a participatory coastal fishery-resource management system.
10. **Support to economic activities and innovation.** This component aims to relieve the bottlenecks encountered by the rural poor as a result of saturated internal markets. It includes providing access to export markets, which, given the size of the country, necessarily focuses on accessing niche markets, while a strategy of diversification is to be followed for internal market expansion. Two subcomponents provide for: (a) capturing new markets (local and international); and (b) empowering the target group to access new markets, and to retain the increasing income gains resulting from these two processes.
11. **Programme management.** This component has been designed to accompany the ongoing process of rural-sector restructuring. The underlying idea is to empower the target group to increasingly take charge of its own development. In practice, this is to be translated into the creation of an association within which a partnership is set up among farmer and fisher organizations, federations, service-providing NGOs and government representatives. Within this association, as of the second cycle, the majority vote is to be entrusted to representatives of farmer and fisher groups. The programme's day-to-day management is to be entrusted to an executive body.

III. PROGRAMME ACHIEVEMENTS DURING THE FIRST CYCLE

12. During the programme's first three years (February 2003 to February 2006), corresponding to the first FLM cycle, the following achievements were made:
13. The rural-sector restructuring component is being implemented by a national NGO. Some 20 smallholder farmer associations have been restructured into organic-cocoa producer organizations having a total of 780 members (38% women). A recent survey prepared by the programme's monitoring and evaluation unit found that 68% of organic cocoa producers considered that these associations worked well, 29% felt they worked quite well, and 3% thought they worked badly. An export and marketing cooperative, comprising 20 legally registered associations, has been established. Management committees in charge of administrative and financial services in the organic-cocoa subsector have been trained. Functional adult literacy training has been provided to four cocoa-producing communities and to two fishing communities. Association leaders have been trained in financial management and bookkeeping. Information bulletins and pricing lists have also been published and broadcast over the national radio.
14. Under the component to strengthen services for the rural sector, work has been carried out in 96 communities by the Association for Agricultural Development and Environmental Protection, which assures extension services under the programme.
15. Under the economic activities and innovation component, a contract has been signed with Kaoka, a French company producing chocolate and supplying a range of renowned European and international stores. Since 1999, the bulk of smallholder farmers in Sao Tome and Principe have been producing cocoa. The emergence of the organic cocoa niche market provides these farmers with an

important buffer against the price fluctuations of conventionally grown cocoa (the export contract with Kaoka ensures a guaranteed price for five years) and the resources and incentives to further diversify. Through production and marketing of organic cocoa, farmers have almost doubled their incomes during the programme's first cycle. This has enabled smallholder farmer organizations to set up social funds for their members. It is expected that, if their future organic cocoa yields remain sufficient, these households will eventually lift themselves out of poverty.

16. Activities relative to the fresh-fish commodity chain were carried out by a national NGO. Five isothermal basins have been installed on four beaches, and are being managed individually or by groups of intermediaries who buy the fish, clean it and store it in basins, before selling it. The freshness and quality of the fish is guaranteed and the NGO has developed a quality brand name featured on the products. On the whole, fishing activities have increased by 50%, and the price at which fish is bought from the fishers and intermediaries involved has essentially doubled. The number of buyers of quality fish increased from 4 in 2003 to 105 in 2004.

17. The following triggers were established for each component:

(a) **Restructuring of the rural sector**

- (i) At least 10% of already existing grass-roots organizations are completely self-sustaining and less than one third continue to be in need of intensive support;
- (ii) Inter-community activities have been carried out.

(b) **Strengthening of services provided to the rural sector**

- (i) The three subcomponents are functional and the microfinance context has been reorganized.

(c) **Support to economic activities and innovation**

- (i) At least 10% of existing rural communities have undertaken innovative economic activities.

(d) **Programme management**

- (i) programme implementation manuals are implemented;
- (ii) programme instruments are functional;
- (iii) disbursements are coherent with the programme strategy;
- (iv) contractual relations are managed effectively; and
- (v) the monitoring and evaluation system is functional.

IV. LESSONS LEARNED

18. **Relevance of the FLM approach.** The FLM is proving to be an appropriate instrument to foster the fulfilment of one of IFAD's prime strategic objectives, that of strengthening the organizations of the rural poor. An adequate response to the pursuit of such an objective – which is tangible and structural, as well as qualitative and process-oriented – needs sufficient time and management flexibility. The choice of triggers – centred on institutional development and “inclusive

private-sector” development – has helped correctly focus the programme’s priorities and activities. The programme is highly innovative inasmuch as it supports the participation of grass-roots, private-sector institutions in the national, regional and global economy. The FLM has been conducive to promoting a spirit of learning-by-doing at the local and national levels, thus fostering a strong socio-economic dynamic towards fair and shared social and economic development. The latter has benefited from the emergence of certified organic niche markets for the supply and value chains promoted by the programme, most notably in the case of organic cocoa.

19. **Other important lessons.** In addition, a number of other lessons have been learned during the programme’s first cycle:

- (a) building on previous IFAD interventions in the country has provided the programme with a sound basis for efficient and results-based implementation;
- (b) past land reforms have contributed significantly to establishing the necessary conditions for enabling sustainable poverty reduction;
- (c) significant premiums can be commanded through organic and “fair trade” certification, and through increased storage and better quality of products;
- (d) organic cocoa is helping to increase farmers’ incomes significantly and providing the necessary resources and incentives to further diversify their production;
- (e) the commodity chain approach is useful for fostering a more equitable distribution of profits from actors downstream to actors upstream, and for bringing in more new actors and avoiding situations whereby a few individuals capture markets and profit disproportionately;
- (f) where they exist, trade-offs between outreach in terms of targeting poor communities and sustainability of activities must be managed, bearing in mind the dynamic setting within which they evolve; and
- (g) small-island economies such as Sao Tome and Principe need to make sure that the government provides an enabling environment for producers to be able to tap into niche markets for export, but this should not be done at the expense of a strong focus on the local economy and local food security.

20. **Challenges for the second cycle.** One challenge for the new phase will be to improve the institutional arrangements for implementation, providing clear “rules of the game” through a distinct separation of roles and responsibilities, the minimization of conflicts of interest, and through a clear separation of the public and private domains that remains faithful to the idea of a negotiated multistakeholder setting conducive to new public-private partnerships. Another challenge will be to enhance the programme’s contribution to the socio-economic emancipation of women through the systematic promotion of relevant activities. Finally, the second cycle will intensify activities on the island of Principe, which will involve considerable challenges in terms of, among others, logistics and monitoring and evaluation.

V. ACHIEVEMENT OF FIRST-CYCLE TRIGGERS

21. **Programme and triggers status.** The report of the inter-cycle evaluation mission states that the programme has been undertaking promising market-chain development activities with the direct support of the private sector. In the organic cocoa sector, for example, the market chain will become fully self-sustainable by the end of 2007, meaning that it will no longer require any project or other

public-sector support, with the smallholders' organic cocoa cooperative taking the leading role. The same is envisaged for the high-quality fresh-fish market chain. The report also notes that the communities participating in these market chains, particularly those in the more advanced organic cocoa market chain, have used part of the increased income from cocoa sales to set up an autochthonous, community-based insurance scheme that provides income to members during crises. This contrasts sharply with the many failed donor and/or Government-directed microfinance schemes set up to date. The evaluation mission did, however, feel that the programme's institutional set-up needed to be significantly changed in order to heighten programme efficiency and effectiveness.

22. The triggers have generally been reached. One trigger – concerning reorganization of the microfinance sphere and successful implementation of the relevant subcomponents – is no longer valid since no microfinance activities were initiated under the programme as a result of government and donor interference in this sphere. Moreover, since no microfinance activities are to be financed during the second cycle, non-fulfilment of this trigger should not prevent the programme from moving to the second cycle.

VI. CONCLUSIONS

23. In view of the foregoing and the fact that the second-cycle triggers have been reached, it is considered that the programme is ready to progress to the second cycle. At the suggestion of the inter-cycle evaluation report, a number of implementation changes have been introduced in the second cycle, loan proceeds have been reallocated and the triggers for the third cycle have been agreed upon.

24. **Amendments in the implementation of the second cycle.** In line with FLM principles and considering that the programme has made savings in the microfinance subcomponent, the inter-cycle mission proposed that a rural infrastructure development fund be created to address the strong need for communal infrastructure, especially for women. This is particularly important since no other rural infrastructure development interventions are currently under way in the country. The proposed management and implementation scheme for this fund is based on the highly successful arrangement that operated from 2000 to 2002 in Sao Tome and Principe with funding from the Export Earnings Stabilization System (STABEX) to finance communal infrastructure. The rural infrastructure fund will substitute the rural finance activities. In addition, to streamline the institutional set-up and separate private and public goods delivery, another change proposed is that the executive board of the local association for the management of family farming and artisanal fisheries development projects be responsible only for reviewing the activities of the rural infrastructure fund and not those of the market-driven commodity chains.

25. **Reallocation of loan proceeds.** The following table shows the allocation of loan proceeds up to the end of the first cycle, the projected loan proceeds required for the second cycle and the balance required for the remaining two cycles. The second cycle began on 1 March 2006 and will end on 28 February 2009. The third and fourth cycles are expected to run from 1 March 2009 to 30 September 2015.

Cost Category	Loan Amount (in special drawing rights)	Percentage of Authorized Expenditures
First-cycle expenditures		
Vehicles	155 000	100% (net of taxes)
Equipment	55 000	100% (net of taxes, or 80% inclusive of taxes)
Training and studies	80 000	100%
Technical assistance	141 000	100%
Contracts for service provision	70 000	100% (net of taxes)
Operating costs	263 000	100%
Personnel	430 000	100%
Support fund	186 000	100%
Not allocated	-	
Subtotal	1 380 000	
Second -cycle expenditures		
Vehicles	40 000	100% (net of taxes)
Equipment	390 000	100% (net of taxes, or 80% inclusive of taxes)
Training and studies	170 000	100%
Technical assistance	480 000	100%
Contracts for service provision	540 000	100% (net of taxes)
Operating costs	260 000	100%
Personnel	470 000	100%
Support fund	-	
Rural Infrastructure Fund	-	
Community infrastructure and results-based contracts	560 000	100% (net of taxes)
Management	360 000	100% net of taxes
Not allocated	100 000	
Subtotal	3 370 000	
Expenses for cycles 3 and 4	3 200 000	
Total	7 950 000	

26. **Amendment of the loan agreement.** Schedules I and III of the loan agreement have been amended to reflect the revised programme description and triggers for the third cycle. The amendments to the programme and the reallocation of funds by cost category and percentage of financing have been reflected in a revised loan agreement, which the borrower signed on 14 March 2006.

