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REPUBLIC OF TURKEY

COUNTRY STRATEGIC OPPORTUNITIES PAPER

For: Review

Note to Executive Board Directors

This document is submitted for review by the Executive Board.

To make the best use of time available at Executive Board sessions, Directors are invited to contact the following focal point with any technical questions about this document before the session.

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TABLE OF CONTENTS

CURRENCY EQUIVALENTS	iii
WEIGHTS AND MEASURES	iii
ABBREVIATIONS AND ACRONYMS	iii
COUNTRY MAP	iv
PORTFOLIO OVERVIEW	v
EXECUTIVE SUMMARY	vi
I. INTRODUCTION	1
II. ECONOMIC, SECTORAL AND RURAL POVERTY CONTEXT	1
A. Country Economic Background	1
B. Agricultural Sector	2
C. Rural Poverty	5
D. National Strategy for Rural Poverty Reduction	7
III. LESSONS FROM IFAD'S EXPERIENCE IN THE COUNTRY	8
IV. STRATEGIC FRAMEWORK FOR IFAD	9
A. IFAD's Strategic Niche and Proposed Thrusts	9
B. Main Opportunities for Innovations and Project Interventions	11
C. Outreach and Partnership Possibilities with NGOs and the Private Sector	12
D. Opportunities for Linkages with Other Donors and Institutions	13
E. Areas for Policy Dialogue	14
F. Action Areas for Improving Portfolio Management	14
G. Tentative Lending Framework and Rolling Programme of Work	14
APPENDICES	
I. COUNTRY DATA	1
II. LOGICAL FRAMEWORK	2
III. STRENGTHS, WEAKNESSES, OPPORTUNITIES AND THREATS (SWOT) ANALYSIS	3
IV. IFAD'S CORPORATE THRUSTS AS RELATED TO THE COUNTRY PROGRAMME	5
V. ACTIVITIES OF OTHER PARTNERS IN DEVELOPMENT – ONGOING AND PLANNED	6

CURRENCY EQUIVALENTS

Currency unit	=	Turkish lira (TL)
US\$1.00	=	TL 1.35
TL 1.00	=	US\$0.74

WEIGHTS AND MEASURES

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

ABBREVIATIONS AND ACRONYMS

ACC	agricultural credit cooperative
ARIP	Agricultural Reform Implementation Project (World Bank)
COSOP	country strategic opportunities paper
DIS	direct income support
EU	European Union
GAP	South-eastern Anatolia Project
HDI	human development index
IPA	Instrument for Pre-Accession Assistance
IPARD	Instrument for Pre-Accession Assistance – Rural Development (EU)
MARA	Ministry of Agriculture and Rural Affairs
PBAS	performance-based allocation system
SIP	strategic investment plan
UNDP	United Nations Development Programme

GOVERNMENT OF THE REPUBLIC OF TURKEY**Fiscal Year**

1 January - 31 December



Turkey Country map



Source: IFAD

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

PORTFOLIO OVERVIEW

Region: Near East and North Africa
Country: Turkey

Project Name	Initiating Institution	Cooperating Institution	Lending Terms	Board Approval	Loan Effectiveness	Current Closing Date	Loan/Grant Acronym	Denominated Currency	Approved Loan/Grant Amount	Disbursement (as % of approved amount)
Erzurum Rural Development	WB: IBRD	WB: IBRD	O	31 Mar 82	03 Dec 82	31 Dec 89	096 - TU	SDR	17, 200, 000	0.76
Agricultural Extension and Applied Research	WB: IBRD	WB: IBRD	O	03 Apr 84	05 Sep 84	30 Jun 94	143 - TU	SDR	9, 700, 000	0.65
Bingöl-Mus Rural Development	IFAD	UNOPS	O	14 Sep 89	10 Jan 90	31 Dec 99	243 - TU	SDR	15, 500, 000	0.70
Yozgat Rural Development	IFAD	UNOPS	O	13 Dec 90	23 Sep 91	31 Dec 01	277 - TU	SDR	11, 500, 000	0.79
Ordu-Giresun Rural Development	IFAD	UNOPS	O	14 Sep 95	25 Aug 97	30 Jun 06	387 - TU	SDR	13, 400, 000	0.61
Sivas-Erzincan Development	IFAD	UNOPS	O	11 Sep 03	17 Jan 05	30 Sep 12	616 - TR	SDR	9, 250, 000	0.04

O = ordinary

EXECUTIVE SUMMARY

1. Since 1982, Turkey has received IFAD loans totalling US\$99.4 million for six projects. The Sivas-Erzincan Development Project, approved in September 2003, is the only active project and there is no further proposal in IFAD's pipeline for Turkey. In recent years, the Government has introduced numerous successful measures to stabilize the economy, control inflation and improve governance. Interest rates and inflation have fallen and the currency has strengthened, resulting in good economic growth and greater investor and consumer confidence. The move towards European Union (EU) accession has intensified under the present Government and actions to enhance convergence with the EU *acquis communautaire* are a prominent part of the political agenda. Issues surrounding EU accession and arrangements for the drawdown of funds under the Instrument for Pre-Accession Assistance (IPA) necessarily have major implications for the nature of future IFAD investment. This country strategic opportunities paper (COSOP) takes account of these factors, the associated institutional and legislative reforms being undertaken, and previous project implementation experience to provide a guide for future investment in Turkey in line with IFAD's performance-based allocation system (PBAS).

2. Turkey occupies a strategic geopolitical position at the crossroads of Europe and Asia. It has a land area of 780,000 km² and is largely an agricultural country with a total agricultural area of approximately 26 million hectares, excluding pastures and meadows. The population of 73 million (2005) has grown over the past five years at an average rate of 1.6% per year, down from 2.4% in the 1980s. The urbanization rate is high, with over 67% of the population living in cities and towns. Westward migration and emigration are a continuing phenomenon, especially from the less-favoured eastern parts of the country. Gross domestic product (GDP) has grown substantially over the past two decades at an average annual rate of about 6% in United States dollar terms and is estimated at US\$4,128 for 2005. Following a serious economic and financial crisis in 2001, when per capita GDP fell by about 9%, the economy has rebounded and has grown on average at 6% over the past three years.

3. Until 2000, the agriculture sector policy was both interventionist and protectionist. Intensification of land use was encouraged by subsidies and other interventions to stimulate agricultural production and investment. The domestic market was highly protected to encourage food self-sufficiency. Commodity exports formed a vent for surplus production, with public agencies extensively involved in the process. These policies pushed inflation up, while benefits tended to accrue to rich landowners rather than poor, small-scale farmers. In 2000, agricultural reform programmes were introduced and included provision for direct income support (DIS) payments as a replacement for the Government's former support policies. Following the introduction of DIS payments nationwide in 2001, transfers to farmers have been reduced. The new Agriculture Strategy 2006-2010, approved in December 2004, recognizes the need for competitive agriculture within the EU framework but also acknowledges the continuing importance of the agriculture sector as a source of employment and incomes in rural areas. The strategy reduces the proportion of funding going to DIS payments and includes a range of support measures for agriculture, albeit at less than historic levels.

4. Partly because of interventionist policies, the level of rural finance in Turkey is comparatively low, with limited household exposure to formal borrowing, especially in poorer regions of eastern and south-eastern Anatolia. Formal rural finance is provided mainly through the state-owned Ziraat Bank and agricultural credit cooperatives (ACCs). Agricultural loans remain subject to explicit credit subsidies but are available only for loans extended through Ziraat Bank or the ACCs, effectively excluding private banks from agricultural lending. This situation is likely to change following the anticipated privatization of Ziraat Bank and the restructuring of the ACCs.

5. In a country of such topographical, climatic and economic diversity, generalizations concerning the root causes of rural poverty should be treated with caution, although certain common factors exist, namely large family size and its corollary, small landholdings; long-term environmental problems such as overgrazing in rangelands and soil erosion in deforested areas; lack of infrastructure, especially roads and markets, in remote locations; and the lack of an effective welfare safety net for the very poor. The structure of landholdings is highly fragmented in all regions with the exception of the prosperous and progressive areas of the Aegean and Marmara coastal regions. According to the 2001 agricultural census, around 90% of farms were owner-occupied and the remaining 10% were held by tenants and sharecroppers. Two thirds of all holdings were less than five hectares. The national figures conceal striking regional disparities, with the worst of the poverty to be found in the eastern and south-eastern anatolia regions, followed by certain areas of the Black Sea coastal region. The average per capita GDP of the eight poorest provinces, all located in the east or south-east, was less than 30% of the national average.

6. Growth in the agriculture sector is increasingly recognized as a necessary but insufficient basis for more equitable development and, in particular, the improvement of living standards among the rural poor. The corollary is that diversification in the rural economy is critical to reducing unemployment and counterbalancing the continuing trends of westward and rural-urban migration, emigration and rural depopulation. The Government's approach to the reduction of poverty and income disparities is laid down in its Long-term Strategy 2001-2023. Social inclusion and combating poverty form one of five key elements in the programme.

7. IFAD's strategy over the past two decades has largely focused on multicomponent rural development in area-based projects in poorer provinces, aiming to provide comprehensive support to targeted villages according to their identified needs and with heavy emphasis on increasing agricultural productivity. Projects have tended to be institutionally complex. As a result, substantial implementation difficulties have arisen from coordination problems associated with the highly centralized and bureaucratic nature of a government administration that is poorly suited to inter-agency and even interdepartmental coordination. Problems have been compounded by the historically adverse and unstable macroeconomic conditions that have prevailed throughout much of the period of IFAD's engagement.

8. Given (a) the structural and institutional changes anticipated in the agricultural sector over the medium-term; (b) the fundamental importance to the reduction of poverty and regional disparities of creating diversity in off-farm employment; (c) the importance of maintaining consistency with the processes of EU accession; and (d) the level of IFAD funds that can be made available for Turkey under the PBAS, a modification of IFAD's investment strategy and focus is warranted. It is proposed that IFAD's strategy, while building on the themes set out in the 2000 COSOP and reflected in the two most recent projects, will further integrate the new policy directions outlined in the Government of Turkey's Medium-term Programme 2002-2008 and its Agriculture Strategy 2006-2010. This entails a greater emphasis on (a) the profitability and marketability of the promoted activities; (b) the site-specific opportunities available in terms of natural resources, market linkages and private-sector involvement; and (c) the support of small- and medium-sized enterprises to provide the market linkages and increase self-employment and job creation opportunities. The broad aim would be to ensure that people who are able and interested could engage in economic activities that generate incremental income.

9. This will entail exploring and supporting alternative on-farm and off-farm sources of income. It is therefore proposed to introduce the concept of the strategic investment plan (SIP), an important innovation in the Turkish context. SIPs are tools for reducing poverty within a market economy context and for understanding interrelationships aimed at improving efficiencies in key agricultural commodity supply chains. The concepts should be developed for commodities of particular relevance to poor people, including rural women, and involving producers, processors, traders and financial

institutions. Following a participatory approach, constraints and opportunities for associated business growth should be identified and a series of relevant investment activities should subsequently be developed and financed at each level of the supply chain. Depending on the commodity, such investments may include such diverse projects as financing, small-scale infrastructure, technology transfer, technical or vocational training of the labour force, provision of business planning skills or improved methods for natural resource management. In addition, IFAD will explore the introduction of a number of innovative instruments in seeking to pioneer and fill the present vacuum in medium- and long-term financing in rural areas including setting up refinancing mechanisms at the local province level and awarding competitive contributory grants. The introduction of these innovative measures – especially in the areas of financial service provision and investment planning based on enhanced market analysis – IFAD should aim at taking on the role of direct supervisor and provide specialized technical back-up. This will also facilitate knowledge management, a fundamental function in any renewal process.

10. In terms of policy dialogue, it would be more strategic for IFAD to focus on the area of rural finance, where it has expertise and can bring value added. IFAD will be engaged in informing the debate on financial sector reform to avoid distortions and promote healthy competition among providers of commercial financial service to rural areas. IFAD will also be involved in pushing for the development of the microfinance sector. Future developments in the microfinance subsector would involve close collaboration with the World Bank and the United Nations Development Programme (UNDP).

11. The country's current PBAS rating is quite positive with respect to macroeconomic and sectoral indicators, whereas the portfolio performance still requires improvement. Based on current PBAS projections, Turkey qualifies for loans of about US\$6 million to US\$7 million a year. A low-case scenario, which could be triggered by the worsening of the policy and institutional framework and lack of improvement in the portfolio performance, could push the PBAS projection lower. However, this is highly unlikely, given Turkey's strong policy and institutional performance over the past few years. On the contrary, and in view of the move towards EU accession, it is expected that the policy and institutional framework will improve further. It is also expected that, with the new partnership with UNDP and the restructuring of the Ministry of Agriculture and Rural Affairs, portfolio performance will improve. This calls for a scenario of about US\$7.5 million to US\$8 million per year with no more than three years' allocation committed under any one project. IFAD will maintain its focus on poverty reduction in the disadvantaged areas of the eastern and south-eastern regions of the country. When the next two investment proposals have been completed (2006 and 2008), and as Turkey moves further down the path of EU accession, IFAD may enter into a dialogue with the Government concerning a possible exit strategy for the Fund in Turkey.

REPUBLIC OF TURKEY COUNTRY STRATEGIC OPPORTUNITIES PAPER

I. INTRODUCTION¹

1. Turkey is an original member of IFAD, having joined in December 1977. Its first loan was approved in 1982 and total loan assistance has since amounted to US\$99.4 million for six projects, all on IFAD's ordinary lending terms. The total cost of the projects is about US\$525 million. Earlier projects have closed and the Ordu-Giresun Rural Development Project was completed in December 2005, with loan closure set for 30 June 2006. The Sivas-Erzincan Development Project, approved in September 2003 and declared effective in January 2005, is now the only active IFAD-supported project in the country.

2. The previous country strategic opportunities paper (COSOP) for Turkey was prepared in 2000. Since then, the investment environment in Turkey has undergone substantial changes. The country faced an acute economic and financial crisis in 2001 with spiralling inflation and currency instability. With the advent of a new government in 2002, strong efforts were made in macroeconomic stabilization. These efforts have brought the formerly chronic inflation under control, fostered impressive economic growth, the appreciation of the Turkish lira – rescaled in January 2005 – and improved stability in the banking sector, which in turn have generated greater investor and consumer confidence. Additionally, the move towards European Union accession has intensified, and the associated policy shifts and convergence of legislation with the European Union *acquis communautaire* are providing new opportunities as well as new challenges for the agriculture sector and the wider aspects of rural development. The design of IFAD's investments, currently aimed at promoting sustained growth in the rural economy and improved living standards among the rural poor, would need to be consistent with the changing policy environment.

3. This COSOP updates the development context for IFAD-sponsored operations in Turkey and provides a guide for future IFAD investment within the framework of its performance-based allocation system (PBAS). It is based on wide-ranging discussions with numerous stakeholders in Ankara and south-eastern Anatolia (public- and private-sector actors, and farmer organizations), as well as reviews of the key strategies and policies of the Government and major development agencies affecting macroeconomic and rural development. The main features of this COSOP have also been discussed with key donors in Turkey, most notably the United Nations Development Programme (UNDP) and the World Bank. The Government endorses and strongly supports the proposed focus of IFAD activities in the very poor south-eastern part of the country.

II. ECONOMIC, SECTORAL AND RURAL POVERTY CONTEXT

A. Country Economic Background

4. Turkey is situated at the crossroads between Europe and Asia. It shares land borders with Bulgaria and Greece in the north-west, Georgia, Armenia and Azerbaijan in the north-east, The Islamic Republic of Iran in the east, and Iraq and the Syrian Arab Republic in the south-east. Turkey's sea borders comprise the Black Sea to the north and the Mediterranean and Aegean seas to the south-west. Its land area of 780,000 km² is about the same as that of France and the United Kingdom taken together. The population of 73 million (2005) has grown over the past five years at an average rate of 1.6% per year, down from 2.4% during the 1980s and 1.8% in the 1990s. Turkey has an annual

¹ See Appendix I for additional information.

urbanization rate of 4.5%, with about 67% of the population classified as urban. In the past two decades, the gross domestic product (GDP) has grown substantially, at an average annual rate of about 6% in United States dollar terms, and was estimated at US\$4,128 for 2005. As noted below, the regional differences in income and poverty levels are extreme.

5. High inflation and an unstable currency plagued Turkey in the five years prior to 2001. Annual inflation from 1996 to 2001 averaged 70% and the exchange rate against the dollar rose to 1.6 million lira in October 2001 at the height of the financial crisis. Since then, the currency has strengthened: in November 2005, the exchange rate was 1.36 lira to the dollar. However, inflation has continued, albeit at a reduced pace – the consumer price index increased by about 7% between 2004 and 2005. Wages have increased more or less in line with inflation, with no significant changes in their real levels. Furthermore, during this period of currency stabilization, interest rates have remained high in real terms. These factors have meant that over the past few years the terms of trade have moved sharply against those primary industries whose output prices are related to the world market.

6. The structure of the Turkish economy is changing as manufacturing and services outpace agricultural growth. In the 1980s, agriculture contributed about 25% of GDP. This fell to 20% in 1985, and between 1990 and 2000 it varied between 14% and 17%. The fall has continued since 2000. Nevertheless, the share of agriculture in the Turkish economy is still high, at about 11% in 2004, compared with 4%-5% in central and eastern European countries that joined the European Union in the same year.

7. Turkey has a labour force of about 24 million (2004) and overall unemployment is quite high at 10.3%, with urban unemployment at 12.5% and rural unemployment a reported 5.9% (although this figure masks considerable agricultural underemployment). Job creation for the relatively young and fast expanding labour force is clearly an important priority. Agriculture, which used to employ over half of the labour force in the early 1980s, now employs one third. It is clear from these figures (50% of labour producing 25% of GDP twenty years ago, but 33% of labour now producing only 11% of GDP) that labour productivity in agriculture has increased more slowly than in other sectors.

8. There is a considerable regional disparity in the levels of economic activity and income in Turkey. The State Planning Organization has classified provinces into five groups based on a composite index derived from 58 economic and social indicators. The wealthiest regions are around the coast and big cities in Marmara as well as Izmir and Ankara. Out of a total of 81 provinces, 19 provinces are in the relatively poor, underdeveloped category, and 16 provinces are in the poorest, severely underdeveloped category. The poorest areas are mostly located in the mountains and rangelands of the eastern and south-eastern Anatolia regions. The average GDP per capita of people living in the wealthier provinces in 1997 was 4.8 times higher than those of people living in the poorest provinces. In general, about 30% of the population living in wealthier areas is over three times richer than the 28% living in poorer areas.

B. Agricultural Sector

9. **Land use.** Turkey is largely an agricultural country. Total agricultural and forest area amounted to some 61.3 million hectares in 2003, comprising field crops (28.5%); fallow (8.2%); orchards, vineyards and olive groves (4.4%); vegetables (1.3%); pastures and meadows (23.8%); and forest (33.8%).

10. The 2001 agriculture census indicated that there were about 3.1 million agricultural holdings, that is one million less than in 1991. Holdings are typically fragmented with an average of five parcels per holding, indicating land consolidation to be a priority action area. Over 90% of all farm households and 60% of total land falls into the 0-20 hectare group. Average size is about six hectares and 66% of all holdings are of less than five hectares. This compares with a European Union average

of 16.5 hectares per farm household. Farm family members provide 70% of the agricultural labour and women constitute about three quarters of the total agricultural labour force.

11. Climate varies considerably over the country but, without irrigation, large tracts can only support low-yielding dryland crops utilizing residual moisture from winter rains. Presently, about 4.3 million hectares are served by irrigation; however, there is considerable scope to increase this to about double the present irrigated area. In general, irrigation has not been well managed, although attempts are being made to overcome this, for example, through the creation of water users' associations to operate and maintain large irrigation projects.

12. **Livestock.** Turkey has substantial but declining numbers of cattle and sheep, and a growing poultry sector. The number of grazing livestock units declined by about 44% between 1980 and 2004, while the number of poultry increased by 400% over the same period. The World Bank is assisting the Government in combating outbreaks of avian flu in Turkey. Cattle and sheep farming are generally undertaken by small-scale family enterprises. Climate and topography have an important impact on the location and type of animal husbandry. Regarding cattle, there has been a move away from local breeds over time; since 1990, the percentage of local breeds has decreased from 58% to 35%. In contrast, the vast majority of sheep and goats continues to comprise native breeds. The area under rangeland has also contracted and is now reported to be only one third of its level in the late 1930s. Despite the recent contraction in livestock numbers, there still appears to be an imbalance between the requirement for livestock feed and the potential to produce it from the rangeland. The result is overgrazing, which gives rise to poor performance of grazing livestock and degradation of pasture.

13. **Production and trade.** The main Turkish agricultural products include wheat and other cereals, pulses, oilseeds, cotton, tobacco, tea and a range of fruits and nuts, as well as Mediterranean fruits and vegetables. Turkey is in slight overall trade surplus with agricultural products. In 2004, agricultural exports were reported at US\$6.5 billion, of which, US\$6.0 billion were unprocessed; while agricultural imports were US\$6.1 billion, with US\$3.1 billion unprocessed. Principal unprocessed exports by value in 2004 were hazelnuts (US\$738 million), dried grapes and figs (US\$412 million), tobacco (US\$399 million) and olive oil (US\$133 million), while the main unprocessed agricultural imports were cereals, oilseeds and Virginia tobacco.

14. **Agriculture sector reforms.** Until 2000, the agricultural sector policy was both interventionist and protectionist. The intensification of land use was encouraged by public subsidies and other interventions to stimulate agricultural production and investment. State assistance comprised support prices for selected crops, subsidies on fertilizers, chemicals and farm credit, and loss compensation for agricultural sales cooperatives through Treasury transfers. The domestic market remained highly protected to encourage food self-sufficiency. Most commodity exports were regarded as a vent for surplus production, with public agencies extensively involved in the process. These policies pushed inflation up as a result of the unsustainable fiscal commitments involved, which cost about 3.1% of GDP in 1999, and benefits tended to accrue to rich landowners rather than poor farmers.

15. To remedy the situation, the Government undertook to phase out its commodity support and input subsidy policies and replace them with a direct income support (DIS) system targeted towards poorer farmers. Under the World Bank-financed Agricultural Reform Implementation Project (ARIP), a pilot programme of farmer registration and associated DIS payments was introduced for crop year 2000. Based on the results of this, DIS was expanded nationwide in 2001. Four years into the programme, the agricultural subsidy reforms contributed significantly to fiscal stabilization by reducing transfers to farmers to about 0.8% of GDP in 2004.

16. In December 2004, the High Council of Ministers approved the new Agriculture Strategy 2006-2010. The new strategy emphasizes the following objectives: (a) to ensure food security and higher income levels through increased agricultural production and income diversification; (b) to strengthen

farm competitiveness through improved access to markets and market linkages; (c) to develop processing initiatives and other agribusinesses; (d) to establish rural development projects based on participatory processes and the provision of finance directly to producers; and (e) to develop farmers' associations and cooperatives. The strategy recognizes the need for agriculture to modernize to be competitive within the European Union framework, but at the same time to remain as an important catalyst in mobilizing local resources and as a basis for increasing employment and incomes in rural areas.

17. A range of measures are proposed in order to meet these objectives, including: (a) compensatory payments to encourage a shift to more profitable crops; (b) insurance payments to guard against price and production fluctuations; (c) investment in specific development programmes, with particular emphasis on countering soil erosion; and (d) relevant research grants and loan supports. These measures are targeted to cost about 1% of gross national product, substantially less than the historical level of support, but an increase on the levels of the past two years. The new proposals do not go as far in decoupling support from production as had previously been implied and production-linked premiums are to be slightly increased, particularly for crops in which Turkey is not self-sufficient.

18. The European Union's Instrument for Pre-Accession Assistance (IPA) provides for (a) institution-building in alignment with the *acquis* in the areas of human resource development and regional development; (b) rural development; and (c) transportation, infrastructure and environment. Associated institutional arrangements are not yet complete, although it seems probable that a network of development agencies will be established on a regional basis to act as coordinating bodies. With respect to the rural development aspects under the IPA, the State Planning Organization and the Ministry of Agriculture and Rural Affairs (MARA) are preparing a national rural development strategy as the precursor to a rural development plan. It is expected that the Government and its various development partners will finance investment activities consistent with this plan and that MARA will be responsible for IPA rural development measures. MARA is undertaking a reorganization to accommodate its Instrument for Pre-Accession Assistance – Rural Development (IPARD) responsibilities. It appears likely that a general directorate for rural development will be created and a new IPARD payment agency established in the ministry. The European Union is to finance technical assistance to MARA during 2006 to help in setting up a European Union-accredited IPARD agency in time to permit IPA funds to flow as of 2007 – that is, in accordance with the pre-accession timetable.

19. **Rural finance.** The level of rural finance in Turkey is low compared with most other countries. A recent World Bank rural finance study indicated that for Turkey as a whole, only 37% of the rural households had ever borrowed, only 20% had borrowed in the past two years and only 11% had any outstanding debt. In the poorer regions of eastern and south-eastern Anatolia, the exposure was much lower – only 2%-4% of households had borrowed in the past two years and fewer than 2% had outstanding debt. Formal rural finance has been provided mainly by the state-owned Ziraat Bank and agricultural credit cooperatives (ACCs). These institutions have a wide cover of rural areas. Ziraat Bank has local branches that cover 95% of the rural population, while ACCs cover 92%; in contrast, the large private bank reviewed in the study covers only 4% of the rural population.

20. Currently, loans for agricultural purposes carry a standard annual interest rate of about 20%. This is close to a fair market rate, but would probably be too low for loans to higher-risk farmers to be profitable on average. Since early 2005, new agricultural loans have been subject to credit subsidies depending on their purpose. These subsidies have the effect of reducing the interest payable to 8%-15%. However, they are not explicitly provided for in the Agriculture Strategy, so there is a high possibility that they will need to be reduced or abandoned in 2006. They are also only available through Ziraat Bank or the ACCs, thus largely excluding private banks from agricultural lending. With the privatization of Ziraat Bank expected to take place within the next two years, and reform and restructuring of the ACCs likely to be supported by the World Bank, it must be anticipated that there

will be considerable changes in the rural credit system and the Government's support for it in the short to medium term.

C. Rural Poverty

21. Turkey is categorized as a middle-income country, and its development status is rated as middle ranking, with the United Nations Development Programme (UNDP) Human Development Report 2004 placing Turkey at 88 among 177 reported countries. Based on 2002 data, 27% of the Turkish population were assessed² as living below the national poverty line (at purchasing power parity exchange rates), with 9.2% having incomes of below US\$2.15³ per day and 38.9% incomes below US\$4.30 per day. Urban/rural differentials are less than might be expected, mainly because of high levels of migration among poor rural households that have swollen the numbers of urban poor. The overall poverty rate in urban households is 22% compared with 35% in rural households, but income and consumption inequalities are only slightly higher in urban areas, with comparative Gini coefficients for income at 0.44 (urban) and 0.42 (rural). Poverty rates are generally higher among self-employed and unpaid family workers, many of whom live in rural areas and are dependent upon the output of small-scale family farms or livestock holdings.

22. In a country of such topographical, climatic and economic diversity, generalizations concerning the root causes of rural poverty should be treated with caution, although certain common factors exist, namely: large family size and its corollary, small landholdings; long-term environmental problems such as overgrazing in rangelands and soil erosion in deforested areas; lack of infrastructure, especially roads and markets in remote locations; and the lack of an effective welfare safety net for the very poor. The structure of landholdings is highly fragmented in all regions with the exception of the prosperous and progressive areas of the Aegean and Marmara coastal regions. According to the 2001 agricultural census, around 90% of farms were owner-occupied, with the remaining 10% held by tenants and sharecroppers. Two thirds of all holdings were less than five hectares. It is generally accepted that there has been no significant shift in farm size, largely due to the complexities of the land tenure system and the principle of the division of inheritance.

23. The countrywide figures conceal striking regional disparities, with the worst of the poverty to be found in the eastern and south-eastern Anatolia regions, followed by certain areas of the Black Sea coastal region. According to the 2001 human development index (HDI) classification⁴ of Turkey's 80 provinces, 16 of the 20 least-developed provinces were located in either the eastern or south-eastern regions, and the remaining four in the Black Sea region. The average per capita GDP of the eight poorest provinces, all located in the east or south-east, was less than 30% of the national average. The relatively poorest and most underdeveloped provinces in Turkey, based on the HDI and State Planning Organization classifications, are summarized in the following table.

² *Turkey: Joint Poverty Assessment Report*. State Institute of Statistics (DIE)/World Bank, 2004.

³ The US\$2.15 and US\$4.30 poverty levels for middle-income countries are considered as comparable with the US\$1 and US\$2 levels used for cross-country comparisons between low income countries.

⁴ The HDI is based on life expectancy, educational attainment and per capita GDP.

Relatively Poorest and Most Underdeveloped Provinces in Turkey

Province	Region	HDI rank (/80)	SPO rank (/80)	GDP per capita (US\$)	GDI ^a
Sirnak	South-east Anatolia	80	79	1 816	0.543
Agri	East Anatolia	79	78	1 803	0.558
Mus	East Anatolia	78	80	1 587	0.556
Bitlis	East Anatolia	77	75	1 932	0.568
Bingol	East Anatolia	76	77	2 331	0.593
Hakkari	East Anatolia	75	74	2 455	0.590
Van	East Anatolia	74	71	2 447	0.596
Sanliurfa	South-east Anatolia	73	63	2 847	0.598
Igdir	East Anatolia	72	73	2 556	0.664
Siirt	South-east Anatolia	71	72	3 062	0.608
Mardin	South-east Anatolia	70	70	2 519	0.613
Batman	South-east Anatolia	69	69	3 410	0.628
Kars	East Anatolia	68	66	2 482	0.640
Adiaman	South-east Anatolia	67	65	2 736	0.643
Erzincan	East Anatolia	66	49	3 348	0.652
Ardahan	East Anatolia	65	76	2 315	0.652
Erzurum	East Anatolia	64	60	3 178	0.653
Yozgat	Central Anatolia	63	62	2 736	0.653
Diyarbakir	South-east Anatolia	62	61	3 701	0.640
Gumushane	Black Sea	61	67	3 263	0.657

Source: *UNDP Human Development Report, 2004*.

a/ For purposes of comparison, the 20 most-developed provinces in Turkey have gender-related development index (GDI) values of between 0.750 and 0.850.

24. All socio-economic factors that are positively correlated with poverty in Turkey are highest in the eastern and south-eastern regions. For example, in the south-east, the family size is nearly twice the national average; the adult literacy rate is 62%, compared with a national average of 83%; and the percentage of underweight children under five is 17%, compared with a national average of 10%. Furthermore, in that same region, there are 60% fewer doctors per 10,000 inhabitants, the rural per capita level of agricultural production is 22% lower and the proportion of women in employment is only 42% of the national average.

25. Compounding these difficult socio-economic conditions, many areas of the east and south-east encountered large-scale migration from the countryside to the towns both within and beyond those regions. This movement has left many villages depopulated and lacking the necessary labour capacity to revive devastated local economies. In addition, many of the poorest provinces are set in mountainous and rangeland areas with a limited natural resource base and restricted opportunities for income diversification. As noted in section D below, the Government is seeking to increase and consolidate support for the disadvantaged regions in the south-east.

26. Overall, poverty rates are higher among households headed by women (32%) than those headed by men (26.6%), although the estimated proportion of woman-headed households is low (6.5%). There is a low and possibly declining rate of female labour market participation; male labour force participation, at some 72% in 2002, is more than twice that of female. While female literacy rates are approaching those of men, income disparities continue to grow. Poverty rates in Turkey, as elsewhere, decrease as the number of years in education increases and men typically progress further through the education system. For both sexes, those who are illiterate or whose education is limited to primary school have higher poverty rates than average; rural households are disproportionately represented in these categories. According to 2001 gender-related development index⁵ figures, the 12 worst

⁵ The gender-related development index (GDI) is based on the same three variables as the human development index (HDI).

performing provinces in terms of gender equity are all located in the eastern and south-eastern regions.

27. The livelihood strategies of the poor households in these two regions include: engaging in agricultural and/or livestock production but with low levels of productivity; working as wage labourers in large-scale farms; or seeking off-farm employment. The combined effect of the abandonment of the traditional farm subsidies and the slow but sure replacement of the public sector oriented top-down approach for agricultural development towards a market-oriented scenario is to exert pressure on farmers to move away from their established farming patterns. In particular, because of the lower world market prices and the cancellation of crop-specific price-support subsidies, they will need to find alternatives to increasingly unprofitable cash crops such as wheat and cotton. The effects of this are already discernible in the grain-growing areas of central Anatolia, where attempts are being made to diversify into fruit- and vegetable-growing in areas where there is sufficient rainfall. In livestock-producing regions, including in eastern and south-eastern Anatolia, problems of overgrazing and marketing are severely affecting the already precarious livelihoods of small-scale producers (typically with no land and only 10-15 sheep or 2-3 cattle). Off-farm employment or migration, both permanent and seasonal, are other alternatives.

D. National Strategy for Rural Poverty Reduction

28. The Government's approach to solving Turkey's main economic and social problems is laid down in its Long-term Strategy 2001-2023.⁶ The Government is pursuing high-sustained growth, human resource development and employment in high technology industries, infrastructure advances and regional development, coupled with transfer payments to poorer segments of society. Within this framework, the Medium-term Programme 2006-2008 adopted by the Council of Ministers on 23 May 2005, represents a dynamic, three-year rolling programme linking objectives and priorities directly to the annual budgets of ministries and Government agencies. Its primary objective is "to improve the life quality of the Turkish people, caring for all segments of the society in an environment where Turkey's socio-economic development is accelerated on the road to European Union membership". The Government's approach to poverty alleviation thus relies on the complementary implementation of economic and social policies, for example, through measures for improving and restructuring income transfer systems and policies geared to increasing employment opportunity especially in less-developed regions. Small- and medium-sized enterprises are viewed as important future contributors to increasing the level of employment. The Agriculture Strategy, emphasizing increased competitiveness of farms, strengthening of farmer organizations and improved market linkages, is subsumed under this general framework.

29. The Government, through multifaceted rural development projects in economically less-favoured regions, has addressed regional disparities. These projects have provided financial and other direct and indirect incentives to encourage private investments; the establishment of the Social Aid and Solidarity Fund to assist the rural unemployed with discretionary grants; rehabilitation programmes to encourage immigrants from urban areas to return to their rural villages; and strengthening the legal framework to support these measures. Particular attention has focused on the three poorest regions through the South-eastern Anatolia Project (GAP), the Eastern Anatolia Development Project and the Eastern Black Sea Regional Development Plan. GAP is the most prominent of these and has attracted funding for several of its constituent elements from United Nations agencies, the World Bank, the European Union and some bilateral donors. Fundamental to GAP is the aim to utilize the substantial water resources of the upper Tigris and Euphrates rivers. The master plan envisages the construction of a network of dams, hydroelectric plants and canals, which would ultimately irrigate some 1.7 million hectares and generate an annual average of 20 billion kilowatt-hour of energy. Major dams and hydroelectric facilities are estimated to be more

⁶ *Long-Term Strategy and Eighth Five-Year Development Plan*. State Planning Organization, Ankara, 2001.

than 80% complete. Irrigation development has lagged behind with only about 14% completed. Besides this resource development, there are other pilot projects within GAP that deal variously with social service provision, gender equity, agricultural development, enterprise development, environmental sustainability, institutional and community capacity-building and civic participation.

III. LESSONS FROM IFAD'S EXPERIENCE IN THE COUNTRY

30. The track record of implementing IFAD projects in Turkey has been mixed. Difficulties have arisen from the highly centralized and bureaucratic nature of government administration and a supply-driven attitude towards development. In the past, these problems were compounded by unstable and adverse macroeconomic conditions. The stabilization of the economy in the past few years and curbing chronic inflation through fiscal and structural reforms have markedly improved the overall climate for investment and development. Nevertheless, lengthy and complex bureaucratic procedures continue to act as a constraint on the smooth and successful implementation of projects. Specific difficulties, experienced not only by IFAD but by other donors such as the World Bank, include: unacceptably long delays in declaring projects effective; slow rates of disbursement; and difficulties in maintaining the flow of funds – including counterpart funds. In some cases, portfolio restructuring, partial loan cancellation or resource reallocation has been necessary, resulting in adjustments to loan agreements and project administration arrangements during the course of project implementation.

31. The principal lessons learned from IFAD's total portfolio are as follows:

- (a) Future project designs should be explicit in specifying effective arrangements for the timely flow of funds for implementation as well as procedures for the procurement of goods and services. In a situation of budgetary austerity and strict control over the use of foreign loan funds, timely access to counterpart funding has proved difficult to achieve. The national budget process continues to preclude access to development funds in the first quarter of a calendar year – a feature that has had substantial adverse repercussions to date on disbursements.⁷ To facilitate the timely flow of funds and accelerate procurement activities, a pilot initiative was initiated in 2005 under which UNDP acts under contract as a third party to facilitate the administration of the IFAD-sponsored Sivas-Erzincan Development Project. The appropriateness and effectiveness of this approach should become clear within the next year, as the project becomes operational.
- (b) There is a need to avoid over-complexity in project design and hence institutional arrangements in order to minimize the need for inter-agency coordination. With the exception of the former Agricultural Extension and Applied Research Project, the development strategy for IFAD has emphasized an integrated, area-based approach, which has proved difficult to implement in the Turkish context. The strategy led to the involvement of multiple implementing organizations, each with its own responsibility and budget. Because of the difficulty of ensuring efficient inter-agency coordination or even interdepartmental collaboration within the same agency, implementation delays have occurred.⁸ In the future, it will therefore be important to entrust the oversight and management of project implementation to one department or branch within one ministry.
- (c) Objectives should be realistically set based on activities that can be influenced more or less directly by the executing authority without undue reliance on the performance of external agencies, unless such performance can be linked to clearly defined contractual

⁷ The Office of Evaluation mid-term evaluation of the Ordu-Giresun Rural Development Project estimated the "disbursement lag" to be at 35% relative to the typical IFAD disbursement model.

⁸ The appraisal report for the Sivas-Erzincan Development Project refers to "time overruns" of between 22% and 33% for IFAD-funded projects.

obligations as a service provider. With its mandate for involvement not only in agriculture but also in the wider aspects of rural affairs, the Ministry of Agriculture and Rural Affairs – and ideally one department within that ministry – remains the natural host for the IFAD-sponsored operations, acting where appropriate through its Provincial Directorates of Agriculture.

IV. STRATEGIC FRAMEWORK FOR IFAD

A. IFAD's Strategic Niche and Proposed Thrusts

32. In the nineties, IFAD's strategy in Turkey emphasized area-based, rural development projects, focusing principally on rural infrastructure such as roads and irrigation, together with support to farmers for extension, training and credit. The 2000 COSOP continued the focus on the three poorest regions (eastern Anatolia, south-eastern Anatolia and the eastern Black Sea), but also stressed the importance of participatory mechanisms and income diversification. In fact, this shift of emphasis had already been signalled in the Ordu-Giresun Rural Development Project, with village development committees set up for the development and implementation of village development plans and attempts made to diversify production and income sources. However, the mid-term evaluation carried by the Office of Evaluation of the Ordu-Giresun Rural Development Project found that the drive to achieve targets and the rigidity of fund allocation tended to override the process of setting priorities at the village level.

33. The Sivas-Erzincan Development Project, which became effective in January 2005, continues the emphasis on village-based planning. It also aims to support the development of community and cooperative initiatives through a fund offering a seed capital loan, but implementation of the project is still at an early stage. A recent GAP publication identified two specific obstacles to successful participation – the disparities in terms of gender, age and socio-economic levels; and the weak capacities of local people – the combined effect of which has reportedly been to leave most development initiatives in the hands of the public sector. The selection criteria for participating villages for the Sivas-Erzincan Development Project are specific, the intention being to include villages whose economy depended on local income sources but which also had sufficient labour capacities to exploit the opportunities offered.

34. As indicated above, Turkey's reforms in the agricultural sector mean that, in order to make a living, small producers have to adjust their production patterns to the demands of the market, locally, regionally, or internationally. Small producers can no longer rely on the state for protection from price instability or insufficient demand. With this in mind, IFAD's strategy in Turkey fully integrates the new policy directions outlined in the Government of Turkey's Medium-term Programme 2002-2008 and its Agriculture Strategy Paper. This entails a greater emphasis on (a) the profitability and marketability of the promoted activities; (b) the site-specific opportunities available in terms of natural resources, market linkages and private sector involvement; and (c) the support of small- and medium-sized enterprises to provide the market linkages and increase self-employment and job-creation opportunities. The broad aim would be to ensure that people who are able and interested could engage in economic activities that generate incremental income. The strategy fully matches the current trends in the agricultural sector, in particular the stated commitment to supporting farmers' organizations, improving market linkages and sustainable growth as well as the gradual spread of farm mechanization, processing plants, agricultural services enterprises, and other private sector initiatives into remoter areas. The approach would also be in line with the emphasis on institutional strengthening and market development as outlined in the current Strategic Framework for IFAD.

35. IFAD's targeting approach to reach out to the rural poor will be an integrated holistic approach whereby interventions are either directly aimed at the target group, or support those entities that can bring benefits to this group. This means, for example, that while there will still be a focus on improving the productivity of small grain-crop growers in the plateau areas and livestock producers in the highland forest villages, the inclusion of progressive farmers for the adoption of appropriate technology and as a model for more traditional growers will be pursued. Furthermore, producers' associations, traders and agro-processors that are a crucial source of market access for small producers will be supported. Private financial institutions that can finance the activities of both the target groups and their service providers will also be promoted. Young rural men and women, on the other hand, could be directly supported through vocational and skills training, and they would indirectly benefit from the promotion of small- and medium-sized enterprises that can either be a source of self-employment or jobs. This approach builds on the recognition that sustainable poverty reduction requires a combination of targeted interventions and broad-based sector growth.

36. IFAD should continue its focus on agricultural and institutional development in the very poor eastern and south-eastern regions, with more intensive efforts to support income diversification among the economically active poor. This is particularly important in view of the high levels of unemployment and out-migration in these regions. Income diversification is one of the planks of the Government's current agricultural policy, and new opportunities will emerge, at least in the plains, with the expansion of irrigation under the various schemes referred to above. Future investment programmes should aim at providing an improved, enabling environment for self-determined investment, with effective, flexible mechanisms for responding to often disparate circumstances and opportunities that are site-specific and demand-driven. In a country as large as Turkey, both in geographical and demographic terms, it is important that investment should not be spread too thinly if anticipated outcomes and impact are to be achieved.

37. The potential level of IFAD's funding commitment in Turkey is relatively modest. A greater proportion of these funds should henceforth be applied to: (a) create multiplier effects, attracting other, more substantial resources for rural development from the Government and the international community; (b) catalyse the inflow of private investment into the presently less-developed eastern parts of the country; (c) assist in fulfilling requirements of EU convergence; and (d) complement and support the initiatives and processes of key partners in development, notably the EU, the World Bank and UNDP. For IFAD, as well as for other donors, item (c) constitutes a particular opportunity for vigorous engagement in the country, with the Government under a great deal of pressure to address its severe disparities and to ensure a more even spread of the benefits of economic growth.

38. In summary, it is suggested that IFAD should:

- (a) maintain the focus on the reduction of poverty in the disadvantaged areas of the eastern and south-eastern regions of the country;
- (b) adopt an approach that pays greater attention to the income-generating potential of supported activities and to their sustainability, profitability and marketability, within the longer-term vision of rural economic development, consistent with the new strategic policy directions of the Government;
- (c) ensure that programme-related expenditures can be justified in terms of attracting and expanding private-sector involvement in such areas as the processing and marketing of agricultural produce;
- (d) maintain a clear and consistent focus on generating incremental income and employment and reducing income disparities in less-favoured areas;

- (e) recognize that, while support for productivity gains is important, sustainable poverty reduction initiatives should include a market-based sector-wide perspective; and
- (f) build effective partnerships with stakeholders in the public and private sector at the national and international levels.

B. Main Opportunities for Innovations and Project Interventions

39. To date, IFAD's projects have focused less on the implications of factors influencing the rural economy and more narrowly on the agricultural production and land productivity gains. Measures should now be introduced to address the challenges thrown up by the modernizing trends in agricultural development and the Government abandonment of subsidies in favour of direct income support, which will have the effect of pushing farmers beyond the traditional – and often unprofitable – farming systems. This will entail exploring and supporting alternative on-farm and off-farm sources of income, a development prefigured by the design of the ongoing Sivas-Erzincan Development Project. The entrepreneurial aptitude that is widely acknowledged to exist provides a sound basis for an IFAD investment focused on the sustainable exploitation of small-scale, private agricultural and agribusiness opportunities.

40. It is therefore proposed to introduce the concept of the strategic investment plan (SIP) already pioneered under other IFAD-financed projects. The SIP would provide the management framework for the design and operationalization of specific agrifood supply chain strategies within a market economy context. Alongside the analysis of supply chain actors' relationships, aimed at improving the efficiency of key agricultural commodity supply chains, the SIP entails the identification, in a participatory manner, of supply chains' market opportunities, growth prospects and potential to contribute to rural poverty reduction, as well as of the constraints that impede or limit the ability of the supply chain to exploit existing and forthcoming market opportunities. Following the design of the SIP, a series of relevant investment activities to improve and support the development of supply chains' competitive advantage should be put in place at each level of the supply chain. Depending on the commodity and constraints identified, such investments may vary in nature, ranging from financing, small-scale infrastructure, technology transfer, technical or vocational training of labour force, provision of business planning skills and improved methods for natural resource management. The SIP should be developed for commodities of particular relevance to poor people, including rural women, and involve producers, processors, traders and financial institutions. An obvious area for developing an SIP in the south-eastern part of the country would be livestock production. This will most likely involve investment in improved breeding activities and, most importantly, measures within the new Law for the Improvement of Pastures and Meadows.

41. The adoption of an analytical tool such as the SIP and subsequent implementation modalities further implies an initial IFAD investment in: (a) skills-enhancement and local capacity-building among Provincial Directorate of Agriculture staff, small- and medium-sized entrepreneurs and service providers in aspects of business planning and financial management; (b) enhancement of specialized technical skills in business; (c) a structured, consultative approach to supply chain analysis; (d) establishment and/or improved management and administration of relevant private primary associations and common interest groups (for example, specialist producers' associations, marketing associations); (e) capacity-building at a "community" level for the management of common resources linked to water users; (f) enhancement of local commercial opportunities; and (g) improved awareness of and access to financial resources and suitable financial products in order to respond to investment opportunity. The overarching objective of all such measures is obviously to assist the poorest economically-active people.

42. In terms of rural finance, a vital element in most commodity-based investment schemes, private commercial banks appear to be quite liquid in Turkey, indicating no absolute shortage of funds for rural area investment. However, there is still an issue concerning the availability of matching

resources for medium- and long-term investment. Despite the situation of improved inflation and lower interest rates – still high in real terms by international standards – continuing constraints exist for private banks lending to the rural sector, including (a) their lack of competitiveness in the face of currently-subsidized interest rates being made available through Ziraat Bank and agricultural credit cooperatives (ACCs); (b) the adverse effects of historical approaches to debt forgiveness; (c) levels of perceived/actual risks; and (d) the high administrative/operating costs involved in providing financial services in rural areas.

43. In spite of these challenges and noting that the interest subsidies may be phased out over the next one or two years, IFAD will explore the introduction of a number of innovative instruments in seeking to pioneer and fill the present vacuum in medium- and long-term financing in rural areas, including setting up refinancing mechanisms at the local province level and awarding competitive contributory grants, in line with the approach currently being piloted under the Agricultural Reform Implementation Project (ARIP). Although microfinance remains almost entirely undeveloped in Turkey, the situation may change if the draft microfinance law is adopted and appropriate institutional mechanisms for the delivery of microfinance services can be identified. In collaboration with UNDP, IFAD will therefore enter into a dialogue with the Government of Turkey with the aim of supporting short-term microfinance lending.

C. Outreach and Partnership Possibilities with NGOs and the Private Sector

44. The dominance of the public sector in the management of regional and rural development programmes has continued to act as a disincentive to the emergence of national or local initiatives outside the public domain. No foreign NGOs operate in agricultural and rural development programmes. There are very few local NGOs, and their implementation capacity, geographical coverage and areas of specialization are limited. Civil society organizations are not available to act as major sources of broad-based service provision in Turkey, so alternative approaches involving private sector contracts and/or public-private partnerships are required.

45. More promising opportunities lie with farmer and other representative organizations. These include chambers of commerce and industry, chambers of agriculture and chambers of commodity exchanges, all of which would be interested parties during the analysis of supply chains and possible stakeholders in subsequent investment responses. The chambers are member-based organizations, but typically retain many characteristics of a top-down management style and remain highly responsive to government directives. Under new government regulations, chambers of agriculture, which also include small farmers, are now authorized to employ agriculture/veterinary specialists and may therefore be able to offer advisory services to their members. Specialist producers' associations, established under cooperative laws, are gradually emerging; for example, fruit growers' associations, vegetable growers' associations and breeders' associations. Again, these may become engaged as involved stakeholders during consultative supply chain analyses, the resulting strategic investment plan (SIP), and as partners in subsequent actions.

46. Agricultural Credit Cooperatives (ACCs) have national coverage and could become key players in improving financial and other service access among their members in rural areas. ACCs currently function as suppliers of inputs, semi-public marketing agencies and credit delivery agencies, although there is wide local differentiation in the degree of emphasis placed on these functions and on the competence and viability of individual ACCs. Historically, ACCs have been subject to political and administrative influence rather than being run as autonomous, fully member-controlled bodies. Their role and functions are currently under review as part of the ongoing World Bank support under ARIP and it is possible that future restructuring will permit close affiliations with commercial banks. It may then be possible to consider a refinancing arrangement for medium- and longer-term financing via ACCs through correspondent commercial banks. It may also become possible over the medium-term for ACCs to engage in microfinance lending, depending on the provisions of pending legislation.

47. District centres and small towns in predominantly rural areas act as important service and marketing centres. Existing and upcoming processing enterprises, trading businesses and specialized service providers are increasingly available in these centres and will be important potential partners in linking poor farmers to the market, following the supply chain analysis and development of SIPs.

D. Opportunities for Linkages with Other Donors and Institutions

48. Turkey does not have a significant bilateral donor presence. Major sources of development assistance include the EU and the World Bank, which together will provide resources to Turkey of approximately US\$2.5 billion to US\$3.0 billion per year. IFAD's investment, which is likely to be minor in comparative terms, should be viewed within the wider framework of their ongoing operations and the Government's commitment to adopting measures that contribute towards EU accession. Through close relationships in implementation with in-country partners, notably the World Bank and UNDP, IFAD will be in a stronger position to contribute to the ongoing dialogue on issues relevant to IFAD's mandate and the application of its corporate and regional strategies. In the context of programme design under a new COSOP framework, possibilities should be explored for parallel and/or joint financing with the World Bank, especially in measures related to provision of rural financial services, possible refinancing of ACCs and wider aspects of rural economic development. These and other opportunities for cofinancing (for example, for construction of small-scale public infrastructure that may be critical to efficient supply chain management and growth in local economic activity) can be further explored by IFAD and the Government during detailed country programme design.

49. The EU is perhaps the most influential external institution in view of the pre-eminence of EU accession on the Turkish agenda. The EU opened accession negotiations with Turkey on 3 October 2005. The European Commission continues to seek a high degree of complementarity between the pre-accession financial assistance programme and ongoing reforms supported by international financial institutions, notably the World Bank, in areas such as education, environment, health, agriculture, transport, regulatory reform and public procurement. A critical area for progress on accession is the establishment of institutions necessary for implementation of the Instrument for Pre-Accession Assistance, scheduled for 2007, in order to avoid limitations on future absorption capacity. IFAD's support would be consistent with the Instrument for Pre-Accession Assistance Rural Development (IPARD) measures, would help to build the platform for convergence with the common agricultural policy (CAP) and could help to inform the Government on possible future adjustments in agricultural strategy and policies to improve their alignment with the CAP.

50. The World Bank's main focus is on structural, economic and financial reforms, but it is also heavily engaged in poverty alleviation projects. In the area of rural development, the World Bank is piloting a number of initiatives linked to the wider, rural affairs responsibilities of the Ministry of Agriculture and Rural Affairs (MARA). A major portion of the earlier investment under ARIP has recently been restructured. New elements introduced include: (a) the provision of grants and advice aiming to replace environmentally harmful agricultural techniques; (b) participatory rural development to provide for the rehabilitation of selected public infrastructure strategic investments in small rural businesses through a system of competitive contributory grants to individuals and organizations; (c) participatory land consolidation to support demand-driven adjustment in the pattern of landholdings and contribute towards more competitive agricultural production; and (d) institutional reinforcement of farmers' organizations. The experience gained from the implementation of these activities will be of the utmost relevance and will provide an input to the formulation of investment programmes for the proposed new programme in the south-eastern part of the country. Items (b), (c) and (d) above closely match IFAD's priorities both in terms of its current and proposed strategic direction.

51. UNDP continues to be an important in-country partner for IFAD. Together with its associated agencies, UNDP is heavily engaged in dialogue with the Government, the provision and coordination

of development aid and other aspects of donor coordination. The United Nations Development Assistance Framework 2006-2010 focuses on the challenges of EU accession and Turkey's commitment to achieving the Millennium Development Goals. Priority areas are the improvement of democratic governance, the reduction of poverty disparities including access to quality basic services and improvement in the status of women, children and youth. IFAD will engage in these initiatives through the support to the integration of small- and medium-sized enterprises in local and global chains by means of clustering, entrepreneurship and business development services.

E. Areas for Policy Dialogue

52. The performance indicators (lower scores) of the performance-based allocation system (PBAS) are helpful in identifying the weak sectoral policy areas of the Government. In the past, these weaknesses also affected the full realization of programme impact, and include (a) the weakness of rural organizations; (b) the limited degree of rural organizations' representation in executive and advisory government bodies; (c) the heavily centralized decision-making processes; (d) the low levels of accountability at the local level; and (e) the role of publicly-owned banks and credit organizations in the rural financial sector.

53. Through its existing and future programmes in Turkey, and in partnership with the EU, UNDP and the World Bank, IFAD will contribute in providing its knowledge and experience in these various issues, and in engaging in policy dialogue with the Government and its partners when appropriate. For example, based on its experiences in the central and eastern Europe and the newly independent states region, IFAD can contribute to the debate on the financial sector reform to avoid distortions and promote healthy competition among providers of commercial financial service to rural areas. IFAD can also be involved in pushing for the development of the microfinance sector, as mentioned in section D above.

F. Action Areas for Improving Portfolio Management

54. Building on the lessons learned from the implementation of previous projects financed by IFAD in Turkey, as well as the mid-term evaluation of the Ordu-Giresun Rural Development Project, a number of measures could be introduced to improve portfolio management. First, project design should be simplified in terms of implementation responsibility. Activities should fit within the broad mandate of MARA and the responsibilities of the appropriate general directorate and designated provincial directorates of agriculture. Second, investment should be defined in the context of the Agriculture Strategy Paper 2006-2010 and IPARD measures, and must be included in the national and provincial budgets for public investment. Third, clearly defined arrangements must be in place for the efficient management of project affairs, in particular for timely procurement and flow of funds for implementation. Emerging experience with the engagement of UNDP as an administrative intermediary will be an important guide in identifying an appropriate mechanism. Fourth, project design should incorporate improved systems for measuring results and impact as practical aids to the ongoing management of projects. Fifth, consultative approaches should be used in developing project activities with concerned stakeholders. Sixth, close in-country partnerships should be maintained with the World Bank, UNDP and the EU to facilitate IFAD's engagement in policy dialogue and ensure a focus on the interests of the rural poor. Seventh, when introducing innovations – especially in the areas of financial service provision and investment planning based on enhanced market analysis – the Fund should aim at assuming the role of direct supervisor and provide specialized technical back-up. This will also facilitate the knowledge management process, a fundamental function in a renewal process.

G. Tentative Lending Framework and Rolling Programme of Work

55. The country's current PBAS rating is quite positive with respect to the macroeconomic and sectoral indicators, whereas the portfolio performance still calls for improvement. Based on current

PBAS projections, Turkey qualifies for loans of about US\$6 million to US\$7 million a year. A low-case scenario, which could be triggered by the worsening of the policy and institutional framework and lack of improvement in the portfolio performance, could push the PBAS projection lower. However, this is highly unlikely given Turkey's strong policy and institutional performance over the past few years. On the contrary, and in view of the move towards EU accession, it is expected that the policy and institutional framework will improve further. It is also expected that, with the new partnership with UNDP and the restructuring of MARA, portfolio performance will improve. This calls for a scenario of about US\$7.5 million to US\$8 million per year with no more than three years' allocation committed under any one project. External cofinancing will be explored: in addition to the World Bank, this will include the Organization of the Petroleum Exporting Countries and the Islamic Development Bank, noting that these institutions have already been engaged with IFAD in Turkey.

56. A number of key strategy/policy directions and institutional adjustments affecting rural development are either unconfirmed or are at a transitional stage. Therefore, IFAD's support in the period to 2010 would be best viewed as a single programme within which two successive investment projects can be developed. The first project would be designed in 2006. Design work for the second project could then be carried out in 2008, by which time a number of outstanding sectoral reform and institutional issues in rural development may have been resolved. Other elements of the programme, including partnerships and policy dialogue, have been noted above.

57. The first project would include pilot/preparatory activities to be built upon or expanded in the second project, should they prove successful or when further adjustments in policy and regulatory frameworks permit. The first project should be implemented under the auspices of MARA, which is represented both centrally and in all provinces. Details of the institutional arrangements may need to be reconsidered in designing the second project in light of future developments, particularly in the relationships between the IPARD agency in MARA, the anticipated development agencies in the regions and province-level structures. When these investment proposals have been completed, and as Turkey moves further down the path of EU accession, IFAD should enter into a dialogue with the Government concerning a possible exit strategy for the Fund in Turkey.

APPENDIX I

COUNTRY DATA

TURKEY

Land area (km² thousand) 2003 1/	770	GNI per capita (USD) 2003 1/	2 800
Total population (million) 2003 1/	71	GDP per capita growth (annual %) 2003 1/	4.2
Population density (people per km²) 2003 1/	92	Inflation, consumer prices (annual %) 2003 1/	25.3
Local currency	Turkish Lira (TRL)	Exchange rate: USD 1 =	TRL 1.35
Social Indicators		Economic Indicators	
Population (average annual population growth rate) 1997-2003 1/	1.7	GDP (USD million) 2003 1/	240 376
Crude birth rate (per thousand people) 2003 1/	21	Average annual rate of growth of GDP 2/ 1983-1993	5.0
Crude death rate (per thousand people) 2003 1/	7	1993-2003	2.7
Infant mortality rate (per thousand live births) 2003 1/	33	Sectoral distribution of GDP 2003 1/	
Life expectancy at birth (years) 2003 1/	69	% agriculture	13
Number of rural poor (million) (approximate) 1/	n/a	% industry	22
Poor as % of total rural population 1/	n/a	% manufacturing	13
Total labour force (million) 2003 1/	33.72	% services	65
Female labour force as % of total 2003 1/	39	Consumption 2003 1/	
Education		General government final consumption expenditure (as % of GDP)	14
School enrolment, primary (% gross) 2003 1/	95 a/	Household final consumption expenditure, etc. (as % of GDP)	66
Adult illiteracy rate (% age 15 and above) 2003 1/	13 a/	Gross domestic savings (as % of GDP)	20
Nutrition		Balance of Payments (USD million)	
Daily calorie supply per capita	n/a	Merchandise exports 2003 1/	46 576
Malnutrition prevalence, height for age (% of children under 5) 2003 2/	16 a/	Merchandise imports 2003 1/	69 340
Malnutrition prevalence, weight for age (% of children under 5) 2003 2/	8 a/	Balance of merchandise trade	-22 764
Health		Current account balances (USD million)	
Health expenditure, total (as % of GDP) 2003 1/	7 a/	before official transfers 2003 1/	-8 993
Physicians (per thousand people) 1/	1 a/	after official transfers 2003 1/	-7 905
Population using improved water sources (%) 2002 2/	93	Foreign direct investment, net 2003 1/	1 562
Population with access to essential drugs (%) 2/	n/a	Government Finance	
Population using adequate sanitation facilities (%) 2002 2/	83	Cash surplus/deficit (as % of GDP) 2003 1/	n/a
Agriculture and Food		Total expenditure (% of GDP) 2003 1/	n/a
Food imports (% of merchandise imports) 2003 1/	4	Total external debt (USD million) 2003 1/	145 662
Fertilizer consumption (hundreds of grams per ha of arable land) 2003 1/	672 a/	Present value of debt (as % of GNI) 2003 1/	81
Food production index (1999-01=100) 2003 1/	103	Total debt service (% of exports of goods and services) 2003 1/	39
Cereal yield (kg per ha) 2003 1/	2 231	Lending interest rate (%) 2003 1/	n/a
Land Use		Deposit interest rate (%) 2003 1/	38
Arable land as % of land area 2003 1/	34 a/		
Forest area as % of total land area 2003 1/	13 a/		
Irrigated land as % of cropland 2003 1/	18 a/		

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

1/ World Bank, *World Development Indicators* CD ROM 2005

2/ UNDP, *Human Development Report*, 2005

LOGICAL FRAMEWORK

Narrative Summary	Verifiable Indicators	Means of Verification	Assumptions/Risks
Goal			
Sustainable improvement of the standard of living of rural people in poorest regions, in line with Turkey's national strategy for poverty reduction	<ul style="list-style-type: none"> • Improvement in the composite index of poverty • Increase in household asset ownership • Reduction in the prevalence of malnutrition among children below five years of age 	<ul style="list-style-type: none"> • State Planning Organization composite poverty index rankings • Household surveys • Ministry of Health records • Impact assessment surveys • UNDP poverty and HDI reports 	<ul style="list-style-type: none"> • Continued macroeconomic stability, Government commitment to private sector development • Institutional reforms consistent with EU convergence
Purpose/Objectives			
Establishment of new and expansion of existing profitable rural businesses, both on- and off-farm	<ul style="list-style-type: none"> • Numbers of businesses engaging with project and volume of incremental investment • Incremental profitability of such businesses • Diversity of rural investment achieved 	<ul style="list-style-type: none"> • Business registration records • Chamber of Commerce • Project documentation • Initial and follow-up project surveys 	<ul style="list-style-type: none"> • Security situation conducive to private investment • Availability of potential investors willing to take entrepreneurial risks
Income diversification and increased employment	<ul style="list-style-type: none"> • N° of new full-time equivalent jobs created • Crop production strategy 	<ul style="list-style-type: none"> • Project surveys – Ministry of Agriculture and Rural Affairs (MARA) • Local Government records 	
Improved business, financial and marketing environment and entrepreneurship skills at the local level	<ul style="list-style-type: none"> • Improved access to finance • Small businesses profitable • Increased rate of small business start-ups • Reduced rate of small business failures • Increase of local farm gate price in relation to prices at major consumption centres 	<ul style="list-style-type: none"> • Chamber of Commerce • MARA price surveys 	

STRENGTHS, WEAKNESSES, OPPORTUNITIES AND THREATS (SWOT) ANALYSIS

Institution	Strengths	Weaknesses	Opportunities	Threats
Ministry of Agriculture and Rural Affairs (MARA)	<ul style="list-style-type: none"> • Comprehensive coverage (offices in 803 districts and 81 provinces) • The major Government agency that has always dealt with food and agriculture • From the beginning of 2005 full agricultural subsidies/support budget transferred to MARA from Treasury • Skilled staff (agronomists, livestock experts, etc.) with knowledge of the rural situation and technical production potential for the different agricultural zones • Wealth of experience of multilateral project implementation including over 20 years with IFAD • MARA expects to handle EU resources under the proposed IPARD funding and is receiving technical assistance from EU to prepare itself for this and to be come the “payment agency” for these resources 	<ul style="list-style-type: none"> • Centralized and bureaucratic approach • Reluctance of staff to relocate to rural areas • Limited operating budget and management capacity • Coordination problems between different departments • Regulation and legislation problems concerned with procurement and disbursing loan proceeds in part due to heavily centralized financial procedures 	<ul style="list-style-type: none"> • Through the harmonization and alignment process with the EU, the entire spectrum of public agencies including MARA can be expected to have a more dynamic approach to rural development policy and be better funded in its implementation • It is planned that MARA will undergo restructuring shortly. In the new framework, the establishment of a General Directorate of Rural Development and Infrastructure (GDRDI) is planned. Its main responsibilities will be to determine rural development policies and strategies nationwide, to guide preparation and implementation of suitable projects, and to monitor and evaluate their performance • Regulation and implementation of income-generating activities to improve the opportunities for rural employment and alleviation of rural poverty outside agriculture itself are likely to fall under the responsibility of GDRDI 	<ul style="list-style-type: none"> • MARA may find it difficult to cope with the expanded responsibilities and workload, given the level of training of its core staff
Rural financial institutions	<ul style="list-style-type: none"> • ACCs have wide coverage, with nearly 2,000 primary level cooperatives, with the potential to cover 92% of the rural population • The aggregate ACC balance sheet is very strong and its equity could be leveraged to expand its rural lending substantially, if it were profitable • Ziraat Bank covers 95% of the rural population • Ziraat Bank is highly liquid 	<ul style="list-style-type: none"> • Most of ACCs’ and Ziraat’s non-equity resources are of a short-term nature • Government policies favourable to ACCs and Ziraat have largely precluded formal private financial institutions entering the rural finance market • Despite benefiting from a strong equity base, ACCs have been unprofitable in recent years, due to poor debt collection performance and high operating costs • Present legal constraints and regulations virtually preclude microfinance 	<ul style="list-style-type: none"> • The massive investment that needs to take place in rural Turkey to modernize and transform agriculture and to generate vital additional rural employment means that there is a potentially huge market for developing rural financial services, in particular the provision of medium- and long-term resources 	<ul style="list-style-type: none"> • Unclear signals from Government, for example the reintroduction of subsidized agricultural credit available only to ACCs and Ziraat • Political instability in some regions may frighten off investors and encourage a non-repayment culture

Institution	Strengths	Weaknesses	Opportunities	Threats
Agricultural support institutions				
<ul style="list-style-type: none"> Chambers of Agriculture 	<ul style="list-style-type: none"> Wide coverage of all agricultural areas 	<ul style="list-style-type: none"> At present possess limited financial and human resources 	<ul style="list-style-type: none"> Farmers must register with and pay fees to the Chambers in order to collect DIS payments; therefore, Chambers have an income source. Legislation has been enacted to allow them to widen their activities, to provide extension services and make investments. 	<ul style="list-style-type: none"> With no history of being other than a registration agency and farmers' interface with Government, there is a major risk that if they try to expand their activities too fast, they will fail commercially.
<ul style="list-style-type: none"> Chambers of Trade and Industry 	<ul style="list-style-type: none"> Wide coverage within provinces Some experience in training and technical support for members, particularly in business and entrepreneurship 	<ul style="list-style-type: none"> Mainly urban, rather than rural 	<ul style="list-style-type: none"> Could be an important resource for training and providing a forum for market linkages 	
<ul style="list-style-type: none"> Commodity Exchanges 	<ul style="list-style-type: none"> Wide coverage at trade centres Considerable financial resources Technical skills in product analysis and classification 	<ul style="list-style-type: none"> Have a narrowly based role, largely concerned with regularizing trade to enable product-related support payments to be made and value-added tax to be collected Possibly they are over-staffed and invested due to their effective monopoly position 	<ul style="list-style-type: none"> In view of their specialized role, opportunities are confined to helping to regularize markets and improving market information 	<ul style="list-style-type: none"> Removal of commodity-based support payments may take away their attractiveness to traders/farmers
<ul style="list-style-type: none"> Farmers' Organizations 	<ul style="list-style-type: none"> Have access to land Have considerable livestock assets Experienced in agriculture relevant to their local environment Abundant family labour 	<ul style="list-style-type: none"> Lack irrigation in low rainfall areas High proportion of low-yielding livestock Fragmented landholdings Rangeland resources have become degraded Tenure arrangements may not be favourable to those who actually work the land Lack capital for desirable on-farm development Distrust financial institutions 	<ul style="list-style-type: none"> Consolidate landholdings Upgrade livestock quality through AI Focus farming systems on optimizing income, subject to existing constraints Utilize grants/credit to make profitable on-farm investments, e.g. making more effective use of irrigation in newly irrigated areas Develop non-farm enterprises to add value to products or utilize off-peak labour availability Link with companies and markets to add more value to farm produce and take advantage of market opportunities 	<ul style="list-style-type: none"> Farmers remain uncertain of the future, adopt risk-minimizing strategies, and so are unprepared to invest The young continue to move out of rural areas, thus depleting the labour force and skill base

IFAD'S CORPORATE THRUSTS AS RELATED TO THE COUNTRY PROGRAMME

As documented throughout the text of the main report, the thrusts of the COSOP are in line with IFAD's strategic framework objectives of enhancing the capacity of the poor and their organisations (support for farmer organisations and producer groups for improved market integration), increasing the access of the poor to productive natural resources and technology (contributory grants for technology transfer) and improving the access of the poor to financial services and markets (supply chain improvement, SIPs and the establishment of sustainable rural financial services for the poor). The thrusts of the COSOP do also adhere with the regional strategy for NENA most notably in terms of the emphasis on capacity building at the community level for common resource management.

In line with the mandate of the Fund, the COSOP proposes to target the communities situated in the most disadvantaged part of the country, with the highest concentration of rural poor. The strategy of the Fund is to target both poorest mostly subsistence oriented farmers as well as those who are striving to enter the market within a new policy environment. Through the support for SME development, within pro-poor supply chains the COSOP seeks to improve employment opportunities for both men and women, thereby potentially contributing to reduce inter-regional migration.

In terms of innovative approaches the introduction of improved supply chain management measures targeted towards the economic active segments of the rural poor represents a new development in Turkey. When successfully tested, such measures which are consistent with the new policy framework currently being implemented in Turkey can be up-scaled and replicated in partnership with other donors and the private sector. The COSOP advocates that such innovations require new implementation arrangements as well as a direct supervisory and supporting role by the Fund to enhance efficiency and facilitate knowledge management.

ACTIVITIES OF OTHER PARTNERS IN DEVELOPMENT – ONGOING AND PLANNED

Development Partner	Nature of Project/Programme	Project/Programme Coverage	Status	Complementarity/Synergy Potential
The World Bank	<p>ARIP – 2001 (US\$600 m)</p> <p>Adjustment portion (US\$200 million); initial investments (US\$400 million) included support for DIS payments, farmers transition grants, Agricultural Sales Cooperative Union (ASCU) restructuring and project support services. This disbursed slowly and the balance of US\$280 million World Bank funding has been reallocated in 2005 as follows:</p> <ul style="list-style-type: none"> - DIS Support Component (US\$69 million) - Farmers Transition Component (US\$137 million) - ACSU restructuring (US\$68 million) - Project support (US\$6 million) <p>Country Economic Memorandum and other sector work leading up to a Country Assistance Strategy (2007-2009)</p>	<p>The restructured ARIP introduced four new subcomponents under farmer transition: environmentally based land utilization (US\$9 million in 4 pilot regions); village-based participatory investments (US\$30 million in 16 provinces); participatory land consolidation (US\$20 million in selected villages in 7 provinces); and institutional reinforcement of farmers' organizations (US\$11 million).</p> <p>A warehouse receipts programme (US\$41 million) was introduced under ASCU restructuring.</p> <p>Major review of rural financial sector ongoing as precursor to a future rural finance project</p>	<p>Ongoing</p> <p>Being introduced</p> <p>Under preparation</p>	<p>Review of ACCs (November 2005) carried out under ARIP might provide the basis for IFAD support to selected ACCs possibly jointly with the World Bank.</p> <p>IFAD may pick up on competitive grants mechanism used under village-based participatory investments within its next project.</p> <p>Institutional reinforcement of farmers' organizations and marketing (through warehouse receipts programme), would complement the support an IFAD project would give to small farmers and entrepreneurs.</p> <p>IFAD/World Bank collaboration in piloting activities concerned with improved rural finance services on a provincial basis</p>
European Union (EU)	<p>SAPARD Programme</p> <p>IPA Programme expected to provide major funds from 2007 (approximately EUR 1 billion per year)</p>	<p>National. Pre-negotiation stage of EU funding Deals with <i>acquis</i> alignment including political criteria, human rights, judiciary reform and institutional reform needed to handle CAP.</p> <p>IPA funding on a national basis following opening of negotiations (in October 2005) on Turkey's accession to EU membership focusing on:</p> <ul style="list-style-type: none"> - institution building for <i>acquis</i> alignment - human resource development - regional development - rural development (IPARD) - transport, infrastructure and environment <p>This supports convergence processes, political dialogue and further liberalization of trade.</p>	<p>Closing</p> <p>Measures being undertaken by Government to meet preconditions for access to IPA funds by 2007</p>	<p>Strengthening of MARA: support under this funding will enhance its ability to handle future IFAD projects more effectively</p> <p>Anticipated development of regional agencies under IPA may affect design options for second IFAD project</p> <p>IPARD will establish payment agency in MARA.</p> <p>Measures supported under IPARD relate to investment, diversification, processing and market linkages, capacity building and environmental/animal welfare within rural areas, and associated technical assistance and training. IFAD's proposed programme will provide complementary support in many of these areas.</p>

Development Partner	Nature of Project/Programme	Project/Programme Coverage	Status	Complementarity/Synergy Potential
United Nations Development Programme (UNDP)	United Nations Development Assistance Framework 2006-2010	National framework for United Nations agencies provides support for meeting Millenium Development Goals through three development themes: democratic governance; reduction of poverty and income disparity; and protection of rights of women, children and youth.	Pending	UNDP may continue its close relationship with IFAD through involvement in project administration. UNDP's technical awareness of the Turkish microfinance situation will be an important resource if a microfinance subcomponent can be introduced in IFADs future programme.