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Enabling the rural poor  
to overcome poverty

## **President's report**

### **Proposed grant to the Federation of Production Cooperatives for the**

### **Programme for the Development of Rural Finance Networks in the Republic of Paraguay**

Executive Board — Ninetieth Session  
Rome, 17-18 April 2007

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For: **Approval**

## **Note to Executive Board Directors**

This document is submitted for approval by the Executive Board.

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## **Abbreviations and acronyms**

AFD	Development Finance Agency
FDC	Peasant Development Fund
FECOPROD	Federation of Production Cooperatives
INCOOP	National Institute of Cooperatives

## **Recommendation for approval**

The Executive Board is invited to approve the recommendation for the proposed grant to the Federation of Production Cooperatives for the Programme for the Development of Rural Finance Networks in the Republic of Paraguay, as contained in paragraph 20.



# Proposed grant to the Federation of Production Cooperatives for the Programme for the Development of Rural Finance Networks in the Republic of Paraguay

## I. Background

1. Rural finance policy in Paraguay has traditionally been characterized by, among others, subsidized interest rates, poor monitoring, inadequate handling of arrears and collection, concentration of investments on a small number of crops, debt forgiveness and indiscriminate selection of beneficiaries. This has hampered the development of an efficient and sustainable rural finance system, while generating high deficits at public banks such as the National Development Bank, the Agricultural Credit Agency and other financial institutions.
2. During the 1990s, IFAD recognized that weaknesses in the rural financial system were a structural constraint on sustainable rural development. It therefore supported the creation of a second-tier bank (the Peasant Development Fund [FDC]) and the development of a rural financial system based on rural savings and credit cooperatives. FDC was created in 1991, and IFAD approved two loans (one in 1992 and the other in 1995), for a total of SDR 15.15 million, to strengthen informal rural financial institutions mainly through funding and support to the FDC.<sup>1</sup>
3. In 2005, the National Congress passed a law consolidating and restructuring the public banking sector. Four second-tier public financial institutions – including the FDC – merged into one, second-tier institution, the Development Finance Agency (AFD), to which all funds and lending portfolios from the institutions affected by the reform were transferred. Access to AFD resources is limited to formal institutions supervised by the Central Bank of Paraguay and to cooperatives given the highest credit rating (“Class A”) by the National Institute of Cooperatives (INCOOP), the supervisory body for cooperatives.
4. Of the 70 cooperatives and other organizations assisted by the former FDC, only 17 currently meet the eligibility requirements for AFD loans. As a consequence, a large number of rural institutions and rural poor families have no access to formal credit. This seriously affects the maintenance of technologies adopted for the most common crops, previously financed with formal credit, and interrupts institutional processes, formalized during the 1990s at the initiative of FDC, that had ensured greater access by the rural poor to sources of institutional credit.

## II. Rationale/relevance to IFAD

5. The proposed programme is highly relevant to IFAD in that it will strengthen poor farmers’ organizations and the rural financial system’s capacity to ensure their access to financial services. The programme links strategically with the IFAD-financed Empowerment of Rural Poor Organizations and Harmonization of Investments (Paraguay Rural) Project, which – because FDC funding was available when it was designed – does not include a financial services component. While former FDC funding is still in principle earmarked for the organizations targeted by the Paraguay Rural Project and once assisted by the FDC, it is inaccessible to most of these financial organizations – at least in the short and medium term – because of the stiff eligibility requirements set by AFD. This situation places a constraint on the project’s implementation, which the proposed programme will help overcome.

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<sup>1</sup> Inter-American Development Bank also funded the FDC.

6. The programme is expected to have a broad impact on the country's rural financial system. To facilitate access to both public and private funds, it will create a network of organizations, comprising both well-established cooperatives and smaller and weaker organizations representing the poorest rural beneficiaries. It will pay special attention to the weakest organizations and to well-established cooperatives that use their institutional platforms to help these organizations gain access to credit, markets and rural services for technical and financial assistance. An initial assessment, on a case-by-case basis, will enable the Federation of Production Cooperatives (FECOPROD) to prevent resources being allocated to organizations that fail to comply with basic governance conditions and show no commitment to improving their performance.
7. The programme's strategic objective is to encourage, through awareness-raising campaigns and other communication efforts, consolidated cooperatives to form partnerships with weaker cooperatives for mutual benefit. Larger cooperatives would gradually include smaller ones in their development plans, intermediate credit and other services. Prior replicable experiences exist (for example, the Nikkei cooperatives initiative in the San Pedro area, supported by the Japan International Cooperative Agency).
8. Some 65 cooperatives come within the Paraguay Rural Project's target group. Their 44,000 members are mainly low-income small farmers producing subsistence and market-based (mainly cotton) crops on traditional plots. These strategic objectives are therefore consistent with the current Government's public policy guidelines for combating rural poverty, inequality and social exclusion.
9. The proposed programme is in line with the IFAD Policy for Grant Financing and responds to both strategic objectives of the Fund's grant programme: (i) it aims to facilitate access to rural financial services by small farmers and other poor rural people, promoting innovative approaches to channel rural financial services to IFAD's target group; and (ii) it supports and strengthens the capacity of pro-poor financial institutions to provide efficient services to empower rural cooperatives and organizations, and to test, develop and implement innovative approaches to rural finance. The programme is also well placed to contribute to the successful implementation of the Paraguay Rural Project by facilitating access to public or private financial resources by small cooperatives and rural organizations that are currently excluded from the formal financial system.

### III. The proposed programme

10. The overall goal of the three-year programme is to create mechanisms to facilitate access by small-scale producers to financial services, by promoting and developing networks of organizations to channel resources efficiently and effectively. The purpose is to ensure access by cooperatives and organizations and their members to institutionalized credit systems and support institution-building for the weakest institutions to enable them, in as short a time as possible, to fulfill conditions for accessing resources from AFD and other public or private financial market funds.<sup>2</sup>
11. The programme will have three interlinked components:

**Promoting and developing networks.** Under this component, the programme will promote the development of networks or partnerships between well-established ("Class A") cooperatives and newly formed ("incipient") and intermediate ones, through proposals that allow partners to derive mutual benefits. It will include

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<sup>2</sup> These activities will be carried out in close collaboration with and with support from the Paraguay Rural Project.



activities for: (i) the design of an operating strategy and methodology; (ii) network development; and (iii) the institutionalization of networks.

**Training.** This is a priority activity and calls for a methodology that will lay the groundwork for operation of the system. Training and capacity-building are instrumental in helping cooperatives graduate to higher credit-risk categories as defined by INCOOP. The programme will provide training to: (i) programme staff, to inform and train producers' organizations; (ii) executives and technical and administrative staff of cooperatives, to manage efficiently the credit system to be implemented; and (iii) producers and their organizations, to generate viable investment proposals for submission to the various financing facilities.

**A management information system on financial markets.** A database will be created containing all available information about the supply of financial services, particularly in rural areas, in order to close the information gap on financial services. It will include a description of each financial institution, type of financial products, terms and conditions, collateral requirements, security and other costs.

#### **IV. Expected outputs/expected benefits**

12. The programme's expected impact and benefits will include:
  - Networks, partnerships and mergers between well-established and weaker organizations formalized and strengthened.
  - Effective instruments adopted and implemented for managing financial intermediation operations in assisted organizations, to complement organization-building by the Paraguay Rural Project.
  - Staff of organizations trained in drawing up technically, economically and financially viable investment proposals for submission to financing facilities.
  - A management information system developed and accepted by AFD to assess the administrative and financial position of each assisted entity and to evaluate requests for financial services.
  - A system of mutual guarantees implemented, to facilitate access to credit by undercapitalized producers.
13. During the life of the programme, an estimated 110 organizations currently classified as incipient and intermediate are expected to join cooperative networks set up to facilitate access by the cooperative sector to financial services and to public or private-sector financial resources. It is estimated that, by programme end, at least 5,000 beneficiaries will have had access to financial services.

#### **V. Implementation arrangements**

14. The grant recipient and agency responsible for administering and implementing the programme will be the Federation of Production Cooperatives (FECOPROD), selected by IFAD following a comprehensive, nationwide institutional analysis. The Federation is a second-tier cooperative, legally recognized since 1976 and registered with INCOOP since 1998. It has 30 member cooperatives to which it provides a wide range of services, including technical assistance, auditing, investment project preparation, feasibility studies and market research, management of credit lines, promotion of market linkages, and natural resource management. Under agreements with various bilateral cooperation agencies, NGOs and private-sector actors<sup>3</sup>, FECOPROD has several projects under way and has substantial experience and a

<sup>3</sup> The Canadian International Development Agency; the Japan International Cooperation Agency; the Swedish Cooperative Centre; SOCODEVI, a Canadian non-profit corporation; and AGROPUR, a Canadian dairy cooperative.

demonstrated capacity for constructive dialogue. Its other assets include credibility, prestige and a strong presence among small, medium and large cooperatives.

15. The Federation will set up a small cooperative networking unit within its headquarters in Asunción, to be supervised by a programme coordinator and consisting of experts in credit risk, development of rural associations, training and information technology. Technical staff will also provide support at the provincial level. A monitoring and evaluation system will be set up as part of the unit's functions.
16. Oversight and guidance will be provided by a steering committee, chaired by a member of the Federation's executive board. It will comprise the programme coordinator, representatives of INCOOP, representatives of the IFAD-funded Southern Cone Common Market's Commission on Family Farming (FIDAREAF) regional programme and selected representatives of the organizations supported. The committee will meet annually to review implementation progress, approve workplans and budgets, and provide guidance on key implementation and management issues.
17. The Federation will establish and develop institutional contacts, linkages and partnerships to take advantage of synergies and exchange experiences and methodologies with other institutions in the sector, such as the Ministry of Crops and Livestock's National Directorate of Project Coordination and Administration, the Paraguay Rural Project implementation unit, AFD, INCOOP and the Agricultural Credit Institute. A special relationship will be established with the FIDAREAF programme to take advantage of the sector and subsector policy dialogue promoted in Paraguay through this programme.
18. The United Nations Office for Project Services will supervise the programme, in its capacity as IFAD's cooperating institution for the Paraguay Rural Project.

## VI. Indicative programme costs and financing

19. The total programme budget is estimated at US\$743,000 over three years, of which IFAD will provide US\$680,000.

### Programme costs by component (United States dollars)

<i>Component</i>	<i>IFAD grant</i>	<i>Percentage</i>	<i>FECOPROD</i>	<i>Total</i>
1. Promoting and developing networks	360 000	46		360 000
2. Training	150 000	32		150 000
3. Information system	50 000	5		50 000
4. Management unit	120 000	17	63 000	183 000
<b>Total</b>	<b>680 000</b>	<b>100</b>	<b>63 000</b>	<b>743 000</b>

## **VII. Recommendation**

20. I recommend that the Executive Board approve the proposed grant in terms of the following resolution:

RESOLVED: that the Fund, in order to finance in part, the Programme for the Development of Rural Finance Networks in the Republic of Paraguay for three years, shall make a grant not exceeding six hundred and eighty thousand United States dollars (US\$680,000) to the Federation of Production Cooperatives upon such terms and conditions as shall be substantially in accordance with the terms and conditions presented herein.

Lennart Båge  
President



## Logical framework

<i>Objective hierarchy</i>	<i>Key performance indicators and targets</i>	<i>Monitoring mechanisms and information sources</i>	<i>Assumptions and risks</i>
<b>Goal</b> Poor small - scale producers have improved their financial and non-financial assets	<ul style="list-style-type: none"> <li>• % of small – scale producer with higher monetary income</li> <li>• % of small – scale producer with improved non-financial assets</li> </ul>	<ul style="list-style-type: none"> <li>• Survey on assets</li> </ul>	
<b>Project Purpose</b> Small scale producer organized in cooperatives have better access to public or private financial services by an efficient and effective resource channelling system focusing the rural poor.	<ul style="list-style-type: none"> <li>• % of the first class cooperatives organized in the network function as credit intermediaries</li> <li>• % of 80 inc./interm. organizations organized in the network presented their projects with credit plans for financing</li> <li>• Approx. US\$4 million channelled to 6800 beneficiaries</li> </ul>	<ul style="list-style-type: none"> <li>• Financial agreements</li> <li>• Credit plans</li> <li>• Records of the cooperatives/organizations</li> </ul>	
<b>Outputs</b>			
<b>Output 1:</b> A network and merger of first class cooperatives with well trained leaders/managers and non-cooperatives organisations for financing production projects in operation	<ul style="list-style-type: none"> <li>• 10 first class cooperatives/organizations organized in the network</li> <li>• 80 incipient or intermediate organizations assisted by PRP have joint the network</li> <li>• 80 managers trained in financial instruments and mechanism</li> <li>• No of cooperatives trained in business and credit plans</li> </ul>	<ul style="list-style-type: none"> <li>• Minutes of the network meetings</li> <li>• Training records</li> <li>• Records of the cooperatives/organizations</li> <li>• Annual reports of cooperatives/ organizations sent to Mix Market network</li> </ul>	Managers assess positively the creation of networks and take it as a surplus
<b>Output 2:</b> Efficient credit management instruments including a system of mutual guarantee to facilitate credit access by undercapitalized producer installed	<ul style="list-style-type: none"> <li>• 80 financing plans for the execution of productive projects prepared</li> <li>• Guarantee system available</li> <li>• Credit criteria with positive discrimination of rural women and young entrepreneurs designed and implemented</li> <li>• Risk management instruments designed and implemented</li> </ul>	<ul style="list-style-type: none"> <li>• Documentation of financial plans</li> <li>• Documentation of guarantee system</li> <li>• Documentation of credit criteria</li> <li>• Documentation of risk management</li> </ul>	Credit management instruments are specially designed to be used by small scale producer
<b>Output 3:</b> Efficient and effective resource channelling system between AFD, first class cooperatives/organizations and small scale producer organised in non-cooperative organisations established	<ul style="list-style-type: none"> <li>• No of credit official trained as trainer in management of credit coop.</li> <li>• No of non cooperative organisations acquainted with credit modalities/requirements and financial models</li> <li>• Lending operations between first class cooperatives and smaller and weaker organisations signed</li> <li>• Tutorship of first class organisations to weaker organisations established for accessing formal credit lines</li> </ul>	<ul style="list-style-type: none"> <li>• Training records</li> <li>• Records of the cooperatives/organizations</li> <li>• Documentation of common meetings</li> <li>• Documents of lending operations</li> </ul>	Participation of INCOOP to validate the mechanisms of resource channelling system
<b>Activities:</b> <ul style="list-style-type: none"> <li>- Organize sector meetings, events, seminars for building up networks where high potential benefits are identified</li> <li>- Conducting training programmes at different level (credit plans, business plans, risk management)</li> <li>- Design and installation of credit management instruments/mechanism</li> <li>- Assistance in the elaboration of credit plans</li> <li>- Establishment of coordination and communication mechanisms between AFD , first grade cooperatives/organizations and non-cooperative organizations</li> <li>- Organize exchange of experiences among stakeholders</li> </ul>			