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Enabling poor rural people
to overcome poverty

President's report

Proposed loan and grant to the Republic of Malawi for the

Rural Livelihoods and Economic Enhancement Programme

Executive Board — Ninety-second Session
Rome, 11-13 December 2007

For: **Approval**

Note to Executive Board Directors

This document is submitted for approval by the Executive Board.

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Abbreviations and acronyms

ACF	Agricultural Commercialization Fund
ADP	Agricultural Development Programme
KIT	Royal Tropical Institute of the Netherlands
MGDS	Malawi Growth and Development Strategy
MLGRD	Ministry of Local Government and Rural Development
PSU	Programme Support Unit

Recommendation for approval

The Executive Board is invited to approve the recommendation for the proposed loan and grant to the Republic of Malawi for the Rural Livelihoods and Economic Enhancement Programme, as contained in paragraph 36.

Republic of Malawi

Rural Livelihoods and Economic Enhancement Programme

Financing summary

Initiating institution:	IFAD
Borrower:	Republic of Malawi
Executing agency:	Ministry of Local Government and Rural Development
Total programme cost:	US\$19.24 million
Amount of IFAD loan:	SDR 5.35 million (equivalent to approximately US\$8.37 million)
Amount of IFAD grant:	SDR 5.3 million (equivalent to approximately US\$8.33 million) inclusive of a Programme Preparatory Facility of US\$0.35 million and US\$0.2 million for the agreement with the Royal Tropical Institute of the Netherlands
Terms of IFAD loan:	40 years, including a grace period of 10 years, with a service charge of three fourths of one per cent (0.75 per cent) per annum
Cofinancier(s):	Royal Tropical Institute of the Netherlands (KIT)
Amount of cofinancing:	US\$0.10 million
Terms of cofinancing:	Grant
Contribution of borrower:	US\$0.39 million
Contribution of beneficiaries:	US\$2.04 million
Appraising institution:	IFAD
Cooperating institution:	Directly supervised by IFAD

Proposed loan and grant to the Republic of Malawi for the Rural Livelihoods and Economic Enhancement Programme

I. The programme

A. Main development opportunity addressed by the programme

1. Malawi is undergoing a period of economic liberalization in which parastatal marketing institutions and market interventions are being restructured at the same time as exposure to market competition is increasing. However, the rural population is unprepared for the realities of a market-led world. Very high levels of rural poverty persist, but smallholder farmers struggle to be competitive in a situation where they are not well connected to markets and lack the knowledge, skills and financial resources to participate fully in commercial transactions. A more market-led approach is required which involves production decisions based on market needs rather than the traditional production-oriented approach. The Malawi Growth and Development Strategy (MGDS) recognizes that there are opportunities to improve agriculture-derived livelihoods of poor rural producers and enable smallholder producers to benefit from efficient markets and local-level value addition. Success in achieving these objectives depends on effective engagement of the private sector and special measures to include smallholder farmers in the process.

B. Proposed financing

Terms and conditions

2. It is proposed that IFAD provide to the Republic of Malawi a loan in the amount of SDR 5.35 million (equivalent to approximately US\$8.37 million), on highly concessional terms, and a grant in the amount of SDR 5.3 million (equivalent to approximately US\$8.33 million) to help finance the Rural Livelihoods and Economic Enhancement Programme. The loan will have a term of 40 years, including a grace period of 10 years, with a service charge of three fourths of one per cent (0.75 per cent) per annum.

Relationship to the IFAD performance-based allocation system (PBAS)

3. The allocation defined for Malawi under the PBAS is US\$16.76 million over the 2007-2009 allocation cycle.

Relationship to national sector-wide approaches or other joint funding instruments

4. The programme has been designed in cognizance of the MGDS and the emerging multi-donor Agricultural Development Programme (ADP), and contributes directly to the ADP agribusiness and market development pillar.

Country debt burden and absorptive capacity of the State

5. Malawi's recent attainment of irrevocable debt relief under the Heavily Indebted Poor Countries Debt Initiative signifies the return to macroeconomic stability that has been championed by the current administration. The country has managed to maintain budgetary and fiscal discipline and see improved exchange rate stability and reductions in inflation and interest rates. Improved macroeconomic management has restored the confidence of the international community, as demonstrated by the resumption of budget support by bilateral donors and a new International Monetary Fund (IMF) Poverty Reduction and Growth Facility.

Flow of funds

6. Funds will be channelled through a special account to be operated by the Ministry of Local Government and Rural Development (MLGRD) at the Reserve Bank of Malawi.

From this account, funds will be disbursed to the operational programme account in accordance with IFAD procedures and based on annual workplans and budgets.

Supervision arrangements

7. The programme will be supervised directly by IFAD.

Exceptions to IFAD General Conditions for Agricultural Development Financing and operational policies

8. No exceptions are foreseen.

Governance

9. A high standard of governance will be assured through stringent and transparent administrative and financial procedures. Formats for submitting financial statements and progress reports will be agreed with IFAD, and will be checked for compliance by supervision missions. Programme accounts will be subject to annual independent audit by auditors appointed by the Auditor General.

C. Target group and participation

Target group

10. In accordance with IFAD targeting policy, the principal target groups are the economically active rural poor and the transient poor who are at risk of slipping backwards into the ranks of the core poor, but also have the ability to move out of poverty. The programme will also extend its outreach to the core poor through employment opportunities generated by commercial development. It is expected that around 24,000 households will participate directly.

Targeting approach

11. Selection of priority commodities will be a key element of targeting strategy. Groundnuts and Irish potatoes are proposed as the initial priority commodities because they are primarily grown by smallholders, and have significant opportunities for value addition using technologies accessible to poor households. The second element of the strategy is selection of focal areas, taking into consideration the prevalence and severity of poverty as well as gender.

Participation

12. Value-chain mapping and analysis will be undertaken in a participatory manner to ensure that all value-chain actors have a say in the identification of constraints and opportunities and the preparation of action plans. Positive initiatives will be taken to engage smallholder farmers and other value-chain actors through publicity and awareness campaigns, sensitization and capacity-building for farmer groups.

D. Development objectives

Key programme objectives

13. The programme goal is to sustainably improve the incomes of economically active poor rural households engaged in the production, processing and marketing of selected agricultural, livestock and fisheries commodities (crops, livestock and fish) by advancing their integration with the emerging commercial sector. Objectives are to: (i) strengthen value chains and enhance the enabling environment to make it more conducive to rural commercial development; (ii) improve farmers' linkages to value chains by establishing more efficient production, transport, storage, processing and marketing systems for target commodities, thereby expanding economic activity and employment; and (iii) facilitate and manage the programme in an efficient and effective manner.

Policy and institutional objectives

14. The programme will inform the policy and institutional processes within the MGDS and the ADP. Knowledge generated will be used to support the development of rural commercialization policy. The programme will also provide resources to strengthen national and local institutions in agricultural commercialization.

IFAD policy and strategy alignment

15. The programme is in line with the IFAD Strategic Framework 2007-2010, which emphasizes strengthening the organizational capacity of the rural poor and increasing their access to markets. The 2005 country strategic opportunities paper targets the capable poor and the transient poor in rural areas and aims to strengthen livelihoods through agricultural development and economic diversification. This requires that IFAD work with its national partners to design programmes that support smallholders directly; provide mechanisms for them to better connect to markets; support private-sector intermediaries; and promote dialogue to generate the policy, institutional and regulatory context required for enhanced market linkages.

E. Harmonization and alignment

Alignment with national priorities

16. The proposed programme is consistent with national priorities as described in the MGDS.

Harmonization with development partners

17. The programme has been developed in full consultation with donor partners. IFAD maintains contact with the principal donors through the Donor Coordination Group on Agriculture and Food Security, which is participating actively in the development of the ADP.

F. Components and expenditure categories

Main components

18. The programme has three components: (i) value-chain mobilization and organization; (ii) agricultural productivity enhancement and commercialization; and (iii) programme facilitation and management.

Expenditure categories

19. There are five expenditure categories: (i) agricultural commercialization grant fund (51 per cent); (ii) technical assistance (19 per cent); (iii) training, workshops and studies (8 per cent); (iv) civil works (1 per cent); equipment and vehicles (4 per cent); and (v) recurrent costs (17 per cent).

G. Management, implementation responsibilities and partnerships

Key implementing partners

20. MLGRD is the lead programme agency and will contract other implementing agencies to perform most of the activities. The prime opportunities for partnership lie with government agencies and public-private partnerships (PPPs) between government institutions, parastatals, companies, individual entrepreneurs, research institutions, NGOs, farmer organizations, cooperatives, fair trade operators, etc.

Implementation responsibilities

21. The overall coordination and management functions will be performed by the programme support unit (PSU) in MLGRD, under the oversight of the programme steering committee. Most activities will be implemented by other ministries or through contracted private sector organizations and service providers.

Role of technical assistance

22. The Royal Tropical Institute of the Netherlands (KIT) will facilitate a collaborative learning network on value-chain development. KIT will work under a partnership arrangement with a Malawian institution and will provide technical assistance, training and linkages to international sources of knowledge on pro-poor value-chain development. An internationally recruited agribusiness adviser will also be attached to the PSU during the three-year pilot phase.

Status of key implementation agreements

23. A portion of debt sustainability framework (DSF) grant funding will be provided by IFAD to advance start-up activities in the form of a programme preparatory facility (PPF). To ensure availability upon signing of the financing agreement, there will be a separate grant governing the use of the PPF, as well as a separate agreement with KIT to cofinance and implement the knowledge management partnership. Agreements between the PSU/MLGRD and implementing agencies will be governed by contracts and/or memoranda of understanding. Grants funded by the Agricultural Commercialization Fund (ACF) will be subject to grant agreements between PSU/MLGRD and the grantees.

Key financing partners and amounts committed

24. The total programme cost is US\$19.24 million over eight years, comprising a three-year pilot phase and a five-year expansion phase. IFAD will finance US\$16.70 million (87 per cent); the Government US\$0.39 million (2 per cent); private sector and beneficiaries US\$2.04 million (10.5 per cent); and KIT US\$0.10 million (0.5 per cent).

H. Benefits and economic and financial justification

Main categories of benefits generated

25. The programme will assist the primary beneficiaries to (i) obtain the inputs and technologies necessary to obtain higher yields of better quality produce; (ii) add value to produce by processes including aggregation, sorting, grading, drying, and storage; (iii) make better commercial decisions on the basis of improved market information; (iv) obtain higher and more stable prices through participation in contract farming and/or outgrower arrangements; and (v) gain access to the financial and technical support services needed to make the transition from subsistence to small-scale commercial farming.

Economic and financial viability

26. The programme will generate economic and financial returns through: (i) increases in the quantity of agricultural production; (ii) higher farmgate prices due to aggregation, grading and quality enhancement; (iii) more stable prices due to the diversification of markets and products; (iv) further value adding post-farmgate through better storage, transport and processing; and (v) increased export revenue and/or reduced food imports. The economic rate of return is estimated to be 16 per cent.

I. Knowledge management, innovation and scaling up

Knowledge management arrangements

27. Creation of a knowledge management partnership on value chain development, with the support of KIT, will ensure that knowledge generated within the programme is captured and knowledge available from elsewhere is accessible.

Development innovations that the programme will promote

28. Engaging private-sector actors as the drivers of agricultural commercialization is a new approach in Malawi. The private sector will be engaged through participation in value chain mapping and analysis, formulation of action plans, and access to ACF grant windows. Private-sector participation in programme governance will be assured through representation on the programme steering committee. Other innovative features include (i) the commodity-based approach rather than the conventional area-based agricultural development programme; and (ii) the targeting strategies to be employed.

Scaling-up approach

29. The programme will begin with a pilot phase of three years. Following a comprehensive review – including reformulation, if necessary – the programme will be expanded to embrace up to six commodities. There will be many opportunities to

expand and replicate the initiative, both in Malawi and in surrounding countries, once key value-chain actors gain confidence in the approach.

J. Main risks

Main risks and mitigation measures

30. The innovative nature of the programme entails a number of risks including: (i) reluctance of the private sector to fully engage in the programme; (ii) limited implementation capacity; and (iii) barriers to the participation of the poor in agricultural commercialization. The most important mitigation strategy is the three-year pilot phase with provision for a comprehensive review.

Environmental classification

31. Pursuant to IFAD's environmental assessment procedures, the programme has been classified as a Category B operation in that it is not likely to have any significant negative environmental impact.

K. Sustainability

32. Commercial incentives and private-sector participation are the keys to sustainability. Support will be provided for farmer groups to build forward and backward commercial linkages with input suppliers, traders and agribusiness enterprises, and will not be phased out until it is clear that the arrangements will remain operational on the basis of commercial incentives. At the institutional level, consideration will be given after completion of the pilot phase to discontinuing the PSU and transferring its functions to the regular departments of MLGRD and the implementing agencies.

II. Legal instruments and authority

33. A programme financing agreement between the Republic of Malawi and IFAD will constitute the legal instrument for extending the proposed financing to the borrower. Important assurances included in the negotiated agreement are attached as an annex.
34. The Republic of Malawi is empowered under its laws to borrow from IFAD.
35. I am satisfied that the proposed financing will comply with the Agreement Establishing IFAD.

III. Recommendation

36. I recommend that the Executive Board approve the proposed financing in terms of the following resolution:

RESOLVED: that the Fund shall make a loan to the Republic of Malawi in various currencies in an amount equivalent to five million three hundred and fifty thousand special drawing rights (SDR 5,350,000) to mature on or prior to 1 October 2047 and to bear a service charge of three fourths of one per cent (0.75 per cent) per annum, and to be upon such terms and conditions as shall be substantially in accordance with the terms and conditions presented herein.

RESOLVED FURTHER: that the Fund shall provide a grant to the Republic of Malawi in various currencies in an amount equivalent to five million three hundred thousand special drawing rights (SDR 5,300,000) and upon such terms and conditions as shall be substantially in accordance with the terms and conditions presented herein.

Lennart Båge
President

Important assurances included in the negotiated programme financing agreement

(Negotiations concluded on 22 November 2007)

Women and youth

1. At all relevant time during the programme implementation period the Government will ensure that the Lead Programme Agency and other programme parties will strive to improve the participation of women and youth in the operations of the programme, develop targets and processes to achieve those targets, and present reports by the end of each programme year on the achievements towards this end.

Pest management

2. The Government will ensure that pesticides procured under the Programme do not include any pesticides banned by the FAO or classified as Extremely Hazardous or Highly Hazardous by the WHO.

Fraud and corruption

3. The Government will promptly bring to the attention of IFAD any allegations or concerns of fraud and/or corruption in relation to the implementation of the programme of which it has knowledge or becomes aware.

Commitment to private sector engagement

4. The Government confirms its commitment to engaging with the private sector under Public-Private Partnership arrangements in order to accelerate the development of rural commerce with the active participation of the programme's target group.

Commitment to the implementation of free market policies

5. The Government confirms its commitment to implement free market policies creating an enabling environment for rural commercial development.

Support for interactive processes

6. The Government confirms its commitment to support for the interactive processes of the programme designed to ensure that outputs truly reflect stakeholder needs in the target groups.

Support for knowledge management

7. The Government confirms its commitment to supporting the programme's knowledge management, with success and failures fully and transparently documented.

Use of programme vehicles and other equipment

8. The Government will ensure that:
 - (a) all vehicles and other equipment procured under the programme are allocated for programme implementation;
 - (b) the types of vehicles and other equipment procured under the programme are appropriate to the needs of the programme; and
 - (c) all vehicles and other equipment transferred to or procured under the programme are dedicated solely to programme use.

Suspension

9. (a) IFAD may suspend, in whole or in part, the right of the Government to request withdrawals from the loan and grant accounts if:
 - (i) IFAD, after consultation with the Government, has determined that the material benefits of the programme are not adequately reaching the

- Target Group, as defined in the Agreement, or are benefiting persons outside the Target Group to the detriment of Target Group members; or
- (ii) The Government has defaulted in the performance of any covenant set forth in the Agreement and such default shall have continued unremedied for a period of thirty (30) days, and IFAD has determined that such default has had, or is likely to have, a material adverse effect on the programme; or
 - (iii) IFAD has given notice to the Government that credible allegations of corrupt or fraudulent practices in connection with the programme have come to the attention of IFAD, and the Government had failed to take timely and appropriate action to address the matters to the satisfaction of IFAD; or
 - (iv) Procurement has not been or is not being carried out in accordance with the Agreement.
- (b) IFAD will suspend, in whole or in part, the right of the Government to request withdrawals from the loan and grant accounts if the required audit has not been satisfactorily concluded within twelve (12) months of the financial reporting date.

Conditions precedent to withdrawals and transfers

10. No withdrawals for the loan and grant accounts shall be made until the Government has (i) duly opened the special account; and (ii) implemented measures to allow taxes and duties to be waived for all programme activities; and until the Lead Programme Agency has submitted a draft programme implementation manual.

Conditions precedent to effectiveness

11. The Agreement will become effective subject to the fulfilment of the following conditions precedent:
- (a) the Programme Steering Committee has been duly constituted;
 - (b) the Programme Support Unit has been duly constituted and its key professional staff, consisting of the National Programme Director, the Financial Controller, the Procurement and Contracts Officer and the Monitoring and Evaluation Officer have been employed;
 - (c) the Agreement has been duly signed, and the signature and performance thereof by the Government has been duly authorized and ratified by all necessary administrative and governmental action; and
 - (d) a favourable legal opinion, issued by the Attorney General of the Government or other legal counsel authorized by the Government to issue such opinion, in respect of the matters set forth in the Agreement and in form and substance acceptable to IFAD, has been delivered by the Government to IFAD.

Key reference documents

Country reference documents

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Government of Malawi: Microfinance Needs Assessment Study Report

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National Statistical Office (2005): Integrated Household Survey 2004-2005

National Statistics Office (2000): 1998 Malawi Population and Housing Census. Report of Final Census Results

IFAD reference documents

IFAD (2005): Malawi COSOP - Main Report and Working Papers
 IFAD (2006): RLEEP Inception Memorandum - Main Report and Working Papers
 IFAD (2006): Key Issues for IFAD in Eastern and Southern Africa
 IFAD (2007): Portfolio Performance Report: Mid Year Review 2007: Eastern and Southern Africa Division
 IFAD (May 2007): Malawi Rural Livelihoods and Economic Enhancement Programme. Formulation Report: First Draft
 IFAD RLSP Supervision Reports: June 2001, December 2001, August 2002 and February 2003
 IFAD/IRLADP: Working Papers 4 & 5
 IFAD: Learning Notes
 IFAD: Strategic Framework 2007-2010 Enabling the Rural Poor to overcome Poverty
 IFAD: Targeting Policy Reaching the Rural Poor

Other miscellaneous reference documents

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 Bie SW, and Lang T. (2006): Evaluation of Norwegian Support to NASFAM's Strategic Development Programme
 Booth, D. et al (2006): Drivers of Change and Development in Malawi. ODI, London
 Bua Consulting Engineers/Norconsult (2006): Infrastructure Services Project: Feasibility Studies for Provision of Coordinated Infrastructure Services
 Byrceson DF, Fonseca J, and Kadzandira, J. (2004): Social Pathways from the HIV/AIDS Deadlock of Disease, Denial and Desperation in Rural Malawi, CARE Malawi.
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Prorustica (April 2007): A Public Private Partnership to Support the Development of the Fertiliser Supply Chain in Malawi: Draft Programme Concept Paper
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World Bank (April 2007): Project Appraisal Document, Business Environment Strengthening Technical Assistance (BESTAP)
World Bank (October 2005): Project Appraisal Report: Irrigation, Rural Livelihood and Agricultural Development Project (IRLADP)

Logical framework

Narrative Summary	Verifiable Indicators a/	Means of Verification	Assumptions and Risks
Goal: Sustainably improve the incomes of economically active poor rural households engaged in the production and marketing of selected commodities by advancing their integration with the emerging commercial sector	<ul style="list-style-type: none"> Reduced incidence and severity of rural poverty Number of households with improved incomes and assets Number of households with reduced hunger gaps, improved nutrition and higher welfare status 	<ul style="list-style-type: none"> National poverty monitoring studies Agricultural production and income data MTR and completion reports IFAD PBAS reviews 	<ul style="list-style-type: none"> Continued Government commitment to economic growth strategy Donors support complementary initiatives Sustained pursuit of decentralization
Objective 1: Strengthen value chains and enhance the enabling environment to make it more conducive to rural commercial development.	<ul style="list-style-type: none"> Number of value chains developed Volume of domestic and international trade Farmgate prices for priority commodities Amount of post-farmgate value addition 	As above, plus: <ul style="list-style-type: none"> M&E reports, surveys and case studies Supervision mission reports Impact assessment studies Trade and employment statistics Commercial and employment statistics M&E reports, surveys and case studies Supervision mission reports 	As above, plus: <ul style="list-style-type: none"> Macro-level economic liberalization and policy reform efforts continue Barriers to export markets do not become more onerous Development of input suppliers and agro-dealer networks are not disrupted by subsidized distribution of agricultural inputs
Objective 2: Improve farmers' linkages to value chains by establishing more efficient production, transport, storage, processing and marketing systems.	<ul style="list-style-type: none"> Number of households achieving sustainable improvements in incomes and living standards Increase in Number of micro and SME enterprises Number and type of jobs created 		
Outputs, Component 1: Value Chain Mobilization and Organization			
Value chain action plans for 2-3 target commodities (pilot phase only)	<ul style="list-style-type: none"> Number of value chain action plans prepared 	<ul style="list-style-type: none"> Documented action plans owned by stakeholders 	<ul style="list-style-type: none"> Commercial actors prepared to participate
Commodity-specific value chain networks formed and active	<ul style="list-style-type: none"> Number of farmers and other actors actively participating in networks 	<ul style="list-style-type: none"> Records of meetings and activities 	<ul style="list-style-type: none"> Distrust between actors can be gradually overcome
Key constraints in the enabling environment for priority commodities identified and addressed	<ul style="list-style-type: none"> Number and range of key constraints identified Number of ACF projects completed which address the constraints 	<ul style="list-style-type: none"> Reports, surveys and interviews with key value-chain actors ACF project reports 	<ul style="list-style-type: none"> Policy, legal and regulatory frameworks remain conducive to removing trade barriers
Learning alliance on value chain development formed and active	<ul style="list-style-type: none"> Number of participants in learning alliance Contribution to knowledge management and policy dialogue 	<ul style="list-style-type: none"> Reports from institution(s) engaged to coordinate learning alliance 	<ul style="list-style-type: none"> Research institutions, trainers, service providers and policy-makers willing to participate
Outputs, Component 2: Agricultural Productivity Enhancement and Commercialization			
Farmer groups in focal areas engaged by improving their connection to profitable market opportunities	<ul style="list-style-type: none"> Number of groups formed and/or strengthened Number of farmer groups and other value-chain actors' groups acquiring agribusiness skills 	<ul style="list-style-type: none"> Reports from service providers on number of persons and groups supported 	<ul style="list-style-type: none"> People willing to change from dependency to self-help culture Profitable markets identified Refresher training effective Poorer actors and women participate
Viable PPPs established linking private, government, parastatal and farmer actors, supported by ACF	<ul style="list-style-type: none"> Number and range of ACF projects completed successfully 	<ul style="list-style-type: none"> Reports on grant-funded activities 	<ul style="list-style-type: none"> Private enterprise prepared to engage ACF grant applications satisfactory Evaluation criteria adhered to Timely disbursement of grant funds
Demand-led and market-oriented research and extension services created	<ul style="list-style-type: none"> Research and extension activities undertaken Number of farmers participating in trials and demos Number of people accessing advisory services 	<ul style="list-style-type: none"> Research and extension reports Survey of stakeholders to assess satisfaction with services provided 	<ul style="list-style-type: none"> Research and extension services are prepared to adopt a demand-led approach Stakeholders able to articulate their research and extension needs

a/ All indicators to be gender disaggregated

