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IFAD

Enabling poor rural people to overcome poverty

President's report

Proposed loan and grant to the Republic of Moldova for the

Rural Financial Services and Marketing Programme

Executive Board — Ninety-fourth Session
Rome, 10-11 September 2008

For: **Approval**

Note to Executive Board Directors

This document is submitted for approval 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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Contents

Abbreviations and acronyms

CPIU	consolidated programmes implementation unit
PFIs	participating financial institutions
VCD	value chain development

Recommendation for approval

The Executive Board is invited to approve the recommendation for the proposed loan and grant to the Republic of Moldova for the Rural Financial Services and Marketing Programme, as contained in paragraph 36.

Map of the programme area

Republic of Moldova

Rural Financial Services and Marketing Programme

Financing summary

Initiating institution:	IFAD
Borrower:	Republic of Moldova
Executing agency:	Consolidated programmes implementation unit - IFAD
Total programme cost:	US$18.95 million
Amount of IFAD loan:	SDR 8.10 million (equivalent to approximately US$12.70 million)
Amount of IFAD grant:	SDR 0.34 million (equivalent to approximately US$0.53 million)
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
Contribution of borrower:	US$1.43 million
Participating financial institutions:	US$1.54 million
Contribution of beneficiaries:	US$2.74 million
Appraising institution:	IFAD
Cooperating institution:	Directly supervised by IFAD

Proposed loan and grant to the Republic of Moldova for the Rural Financial Services and Marketing Programme

I. The programme

A. Main development opportunity addressed by the programme

1. The programme will improve the participation and employment of the poor in income-increasing activities related directly and indirectly to the development of the Moldovan horticultural value chain. This will be achieved by addressing gaps and weaknesses in the overall chain – input supply, production, processing, marketing, regulations and legislation – through the provision of targeted rural financial services, the development of rural commercial infrastructure, and capacity-building for beneficiaries in terms of the knowledge and technical expertise required to participate more profitably in national and international markets.

B. Proposed financing

Terms and conditions

2. It is proposed that IFAD provide to the Republic of Moldova a loan in the amount of SDR 8.10 million (equivalent to approximately US$12.70 million) on highly concessional terms, and a grant in the amount of SDR 0.34 million (equivalent to approximately US$0.53 million) to help finance the Rural Financial Services and Marketing 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. The grant will mainly finance programme technical assistance and start-up activities.

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

3. The allocation defined for Moldova under the PBAS is approximately US$13.51 million over a three-year allocation cycle (2007-2009).

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

4. The programme is in line with the current medium-term expenditure framework. There is no joint funding instrument in Moldova at present.

Country debt burden and absorptive capacity of the State

5. Moldova is at low risk of debt distress with all indicators below the relevant country-specific debt burden threshold. External debt stands at 56 per cent of GDP (2005), down from 124 per cent in 2000. Macroeconomic management is sound and annual real GDP growth is 5 per cent. The implementation record for the IFAD-financed operations in Moldova is excellent.

Flow of funds

6. The proceeds of the IFAD loan and grant will be channelled through a standard financing agreement between IFAD and the Government. A special account for the loan and a grant bank account will be opened by the Ministry of Finance for the IFAD share of programme expenditures.

Supervision arrangements

7. IFAD will directly supervise this programme.

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

8. No exceptions are foreseen.

Governance

9. The following planned measures are intended to enhance the governance aspects of the IFAD financing: (i) annual audit of programme accounts and financial statements; (ii) supervision and implementation support; (iii) emphasis on high-

quality management information systems; and (iv) provision of high-calibre technical assistance for institutional development and support.

C. Target group and participation

Target group

10. The programme will benefit rural people who are or could potentially become economically active. Three main subgroups of possible programme beneficiaries have been identified: (i) commercially active poor people, who are oriented towards commercial agriculture; (ii) economically active poor people, who produce a surplus that is sold in local markets; and (iii) very poor people, who are often landless and whose main sources of income are unskilled labour and social insurance.

Targeting approach

11. In accordance with the IFAD Policy on Targeting, the programme will use direct, indirect, value chain and geographic targeting. A significant portion of rural financial services and access to infrastructure support will be directly targeted, while value chain analysis will be used to target programme benefits indirectly by supporting rural goods and services assessed as having a substantial actual or potential linkage to the target group. Although the programme will have national coverage, its investments will be prioritized to reflect the distribution of areas with the highest concentrations of rural poor people, using national poverty data. Significant efforts will be made to ensure that women and young people have equitable access to programme benefits.

Participation

12. The programme's design strongly emphasizes systematic participation processes throughout implementation, from start-up to completion. Its approach encourages potential beneficiaries to seek access to rural financial services, technical assistance and employment generated through the programme. More socially driven opportunities in terms of improved access to roads, small-scale irrigation and potable water systems, and village natural gas supplies are also an important part of the programme. Beneficiaries will contribute a minimum of 15 per cent in cash or in kind to overall infrastructure costs, and participate in infrastructure design, supervision, operation and maintenance.

D. Development objectives

Key programme objectives

13. The programme's goal is to reduce rural poverty in Moldova by creating enabling conditions for the poorer and poorest members of rural society to increase their incomes through greater access to markets and employment. The specific objective is to improve the participation and employment of rural poor people in income-increasing activities related to the development of a horticulture value chain in Moldova.

Policy and institutional objectives

14. Key areas of policy dialogue under the programme include: (i) use of a closely targeted and appropriately scaled system of market-oriented financial, organizational and technical support to achieve poverty reduction through sustainable economic growth; (ii) clarification of the respective responsibilities of commercial banks and microfinance institutions; and (iii) development of a positive enabling environment for economic growth.

IFAD policy and strategy alignment

15. The programme conforms to the key thrusts in IFAD's 2007 country strategic opportunities programme: (i) establishment of pro-poor market linkages through support to competitive commodity value chains; and (ii) promotion of access to a full range of financial services. Furthermore, it is aligned with various objectives in the IFAD Strategic Framework 2007–2010, namely enhancing poor rural people's access to natural resources, improved agricultural technologies and a range of financial

services, and increasing their opportunities for taking advantage of rural off-farm employment and enterprise development.

E. Harmonization and alignment

Alignment with national priorities

16. The programme will help put into operation important elements of Moldova's 2004 economic growth and poverty reduction strategy paper, which highlights economic growth and private-sector development along with subsequent employment generation as the most important tools for poverty reduction. It will also align itself with the Government's 2006 agricultural strategy in terms of: (i) boosting value-added production; (ii) increasing the production of processed agricultural products; (iii) improving the quality and competitiveness of agricultural production; (iv) enabling Moldovan agricultural products to reach international markets; and (v) endeavouring to maintain agricultural incomes at or above 85 per cent of average national income.

Harmonization with development partners

17. The programme has been fully integrated into the United Nations Development Assistance Framework, and it has been carefully reviewed by the Office of the First Deputy Prime Minister. Moreover, it has benefited from the close operational partnerships established with the United States Agency for International Development, the World Bank, and the European Bank for Reconstruction and Development. The programme's organization and management is harmonized with government systems and with the procedures used by other relevant donor-supported development initiatives.

F. Components and expenditure categories

Main components

18. The programme has four components: (i) value chain development (VCD) for rural poverty reduction; (ii) rural financial services; (iii) pro-poor market-derived infrastructure; and (iv) programme management.

Expenditure categories

19. There are three main expenditure categories, which together account for 93 per cent of base costs: (i) refinancing/investment capital; (ii) civil works; and (iii) recurrent costs, including salaries, operation and maintenance, and other operating costs. Five other categories together account for the remaining 7 per cent of base costs: (i) equipment and supplies; (ii) vehicles; (iii) technical assistance (national and international); (iv) training and studies; and (v) contracts and unallocated.

G. Management, implementation responsibilities and partnerships

Key implementing partners

20. The Ministry of Agriculture and Food Industry will be the lead institution for the programme as a whole. Under the Ministry's overall responsibility, a programme coordination committee will ensure compliance with programme policies and criteria as negotiated and agreed with IFAD.

Implementation responsibilities

21. IFAD's existing Consolidated Programmes Implementation Unit (CPIU) will have overall day-to-day responsibility for planning, management, coordination, and monitoring and evaluation of programme outputs and effectiveness, and for administrative and financial reporting. It will also have administrative and financial autonomy to enter into contracts with third parties for programme implementation requirements. Rural financial services activities will be implemented by participating financial institutions (PFIs), and infrastructure works will be contracted out to national engineering and design firms as necessary.

Role of technical assistance

22. IFAD financing includes approximately US$0.97 million for national and international technical assistance, training and studies (from both the IFAD loan and grant). Given the innovative nature of the VCD approach, international technical assistance will be provided initially by a grant from IFAD. Local and international experts will also support other programme elements, including monitoring and evaluation, strengthening of linkages with PFIs, development of business development services, and provision of technical assistance for the introduction of modern agricultural technologies and the achievement of national standards.

Status of key implementation agreements

23. As is current practice in other ongoing programmes, arrangements made by the Ministry of Finance and/or the CPIU with implementing agencies that are acceptable to IFAD will be established as necessary through specific agreements.

Key financing partners and amounts committed

24. The total programme cost is US$18.95 million over five years. IFAD will contribute about US$13.24 million, including a US$0.53 million grant (70 per cent of total cost). PFIs will contribute US$1.54 million (8 per cent), the Government about US$1.43 million (8 per cent) and beneficiaries US$2.74 million (14 per cent).

H. Benefits and economic and financial justification

Main categories of benefits generated

25. Benefits include increased: (i) returns and income from agricultural production; (ii) numbers of farmers engaged in commercial agriculture; (iii) ability of the target group to access employment thanks to value chain and infrastructure development; (iv) levels of investments and incomes in the non-farm rural economy; (v) capacity of PFIs to provide sustainable financial services; and (vi) capacities of providers of business development services to ensure sustainable services to the target group.

Economic and financial viability

26. Since programme activities will be mostly demand-driven, an overall economic and financial analysis is unfeasible. Enterprise and farm models prepared during programme design do, however, show satisfactory returns.

I. Knowledge management, innovation and scaling up

Knowledge management arrangements

27. The entire VCD approach is about collecting and sharing knowledge. Consequently, the VCD experience will be closely documented and results disseminated. In addition to a management information system, IFAD will finance regular technical support missions and related workshops to follow up and guide progress. The CPIU will also maintain a website, linked to the Hortivar database[1] set up by the Food and Agriculture Organization of the United Nations (FAO) and to MIX Market.[2]

Development innovations that the programme will promote

28. The programme's two main innovations will be the establishment of a VCD platform – a working group bringing together all stakeholders in the horticultural value chain – and the requirement that PFIs contribute a proportion of the programme's lending portfolio from their own resources, thereby laying the basis for their ongoing involvement in rural poverty-reducing financial services.

Scaling-up approach

29. The validation and scaling up of technological and institutional innovations is a specific part of the VCD platform's mandate. Should the VCD implementation experience be positive, it could be replicated in other countries in the region.

[1] Hortivar: Horticulture Cultivars Performance Database. See www.fao.org/hortivar.

[2] Mix Market: a global microfinance information platform maintained by the Microfinance Information eXchange (MIX), a not-for-profit private organization. See http://www.mixmarket.org.

J. Main risks

Main risks and mitigation measures

30. The programme faces three main risks: (i) difficulties in establishing and operating the VCD platform; (ii) the conservative nature of the financial sector and its wariness of investing in the agricultural sector; and (iii) the vulnerability of the Moldovan economy to external shocks. The programme will seek to mitigate these risks by respectively: (i) providing strong implementation support to help ensure Government buy-in to the VCD platform; (ii) supporting PFI training and the inclusion of savings and credit associations in the rural finance component to channel finance for rural poor people; and (iii) developing more efficient vertically integrated commodity and service chains to achieve import substitution and greater access to export markets.

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. The sustainability of programme investments will be assured by: (i) requiring that investments be market-driven and subject to value chain assessments; (ii) requiring that infrastructure investments be conditional upon operation and maintenance agreements; and (iii) organizing regular stakeholder workshops to identify success factors and implementation issues.

II. Legal instruments and authority

33. A programme financing agreement between the Republic of Moldova 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 Moldova 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 Moldova in various currencies in an amount equivalent to eight million one hundred thousand special drawing rights (SDR 8,100,000) to mature on or prior to 1 June 2048 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 Moldova in various currencies in an amount equivalent to three hundred and forty thousand special drawing rights (SDR 340,000) 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 3 September 2008)

Gender

1. At all relevant times during the programme implementation period the Government will ensure that the Consolidated Programme Implementation Unit (CPIU)-IFAD and other programme parties will strive to improve the gender balance in the operations of the programme, develop targets and processes to achieve those targets as part of a gender strategy, and present reports by the end of each programme year on the achievements towards this end.

Pest management

2. The Government will comply with the International Code of Conduct on the Distribution and Use of Pesticides and ensure that pesticides procured under the programme do not include any pesticides classified as Extremely Hazardous or Highly Hazardous by the World Health Organization (WHO).

Fraud and corruption

3. The Government and any other programme party 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.

Suspension

4. (a) IFAD may suspend, in whole or in part, the right of the Government to request withdrawals from the Loan and Grant Accounts in accordance with Section 12.01 (Suspension by IFAD) of the General Conditions upon the occurrence of any of the events set forth therein, or 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 Schedule 1 paragraph 1, 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 Section II of Schedule 3 hereto and such default will 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) The Components Operations Manual, as defined in Paragraph B 12 of Schedule 3, or any provision thereof has been waived, suspended, terminated, amended or modified without prior consent of IFAD, and IFAD has determined that such waiver, suspension, termination, amendment or modification has had, or is likely to have, a material adverse effect on the programme; or

   (iv) Any of the Subsidiary Financing Agreements described in Schedule II, Section 5(a) or 5(b), or any provision of any of them, has been waived, suspended, terminated, amended or modified without the prior consent of IFAD, and IFAD has determined that such waiver, suspension, termination, amendment or modification has had, or is likely to have, a material adverse effect on the programme; or

(v) 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 has failed to take timely and appropriate action to address the matters to the satisfaction of IFAD; or

(vi) Procurement has not been or is not being carried out in accordance with Schedule 4 of this 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 audit required by Section 5.02(b) has not been satisfactorily concluded within twelve (12) months of the financial reporting date.

Conditions precedent to withdrawals

5. No withdrawals from the Loan or Grant Accounts will be made in respect of the following Categories until the following conditions have been satisfied:

(a) For withdrawals under Category I ("Refinancing and Investment Capital") related to subcomponents II(a) or II(c), a Subsidiary Financing Agreement acceptable to IFAD has been signed with at least one Participating Financial Institution for the relevant subcomponent.

(b) For withdrawals under Category I ("Refinancing and Investment Capital") related to subcomponent II (b), a Subsidiary Financing Agreement acceptable to IFAD has been signed with the Rural Finance Corporation.

(c) For withdrawals under Category II ("Civil Works") related to Component III, the existing Component Operations Manual (COM) has been revised and accepted by IFAD.

(d) For withdrawals under Grant Category I ("Refinancing and Investment Capital") related to subcomponent II(d), funds to be used for the seed capital for the establishment of a Credit Guarantee Fund for Savings and Credit Associations may only be disbursed subject to acceptance by IFAD of the proposed modalities.

Conditions precedent to effectiveness

6. The Agreement will become effective in accordance with Article XIII of the General Conditions (Effectiveness and Termination) subject to the fulfilment of the following conditions precedent:

(a) the Government will have confirmed that the IFAD programme Steering Committee established under the IFAD-funded Agricultural Revitalisation Project has been authorised to oversee the programme, and confirming that the CPIU-IFAD, with composition acceptable to IFAD will have been given authority with respect to the programme in accordance with Section A, paragraphs 3 and 4 of Schedule 3;

(b) the Agreement will have been duly signed, and the signature and performance thereof by the Government will have been duly authorised and ratified by all necessary administrative and governmental action; and

(c) a favourable legal opinion, issued by the Ministry of Justice or other legal counsel acceptable to IFAD, in respect of the matters set forth in Section 7.02 hereof and in form and substance acceptable to IFAD, will have been delivered by the Government to IFAD.

Key reference documents

Country reference documents
Economic Growth and Poverty Reduction Strategy Paper (2004)
MAFI Agricultural Development Strategy (2006)

IFAD reference documents
Project design document (PDD) and Key Files
COSOP (2007)
Administrative Procedures on Environmental Assessment
IFAD Strategic Framework 2007-2010
Private-Sector Partnerships and Development Strategy

Other miscellaneous reference documents
Gorton, M., and White, J./2004/Vertical Coordination in Transition Countries: A comparative study of agri-food chains in Moldova, Armenia, Georgia, Russia, Ukraine
International Development Association & International Monetary Fund: Debt Sustainability Analysis, February 2008.

Logical framework

Narrative Summary	Verifiable Indicators	Means of Verification	Assumptions / Risks
Goal:			
Reduced rural poverty in Moldova	▪ Increase in household asset ownership ▪ Reduction in prevalence of malnutrition among children below 5 years of age	▪ HBS and DSS and national data ▪ Project M&E and impact surveys, baselines and completion report	▪ Absence of external economic shocks
Purpose / Objectives:			
Participation and employment of the rural poor in income increasing activities arising directly and indirectly from an improved horticulture supply chain.	▪ 1175 full time equivalent jobs created (20% for women – 20% for youth); 300 full time equivalent jobs created through B1; 675 full time equivalent jobs created through B2; 200 full time equivalent jobs created through B3; N° of agribusiness enterprises with improved profitability; N° of smallholders reporting improved farm profitability; N° of supply chain contracts/agreements established; N° enterprises/legal entities operating under own brand/label; N° of new technologies adopted by enterprises; N° of beneficiaries reported provided with sustainable access to improved infrastructure; N° of smallholders reported improved market access; Value of marketed rural produce; Horticulture Value Chain Platform functioning	▪ Export/import statistics ▪ Programme M&E database ▪ Supervision and MTR reports ▪ Technical studies/assessments ▪ Annual performance reports ▪ PFI client records ▪ BDS client records	▪ Liberal economic policies continue ▪ No deterioration in external trade routes
Outputs:			
A: Value Chain Development for Rural Poverty Reduction **B1:** Financing of PFIs for small loans to poorer small-scale farmers. **B2:** Financing of PFIs for small loans to off-farm rural entrepreneurs. **B3:** Financing of PFIs for medium loans to rural processors. **B4:** Capacity-building of PFIs and SCAs **C:** Pro-poor market derived infrastructure	▪ **A:** Awareness Raising Campaign undertaken; N° of seminars & orientation workshops organised; N° and type of rural product quality standards met; Horticulture Value Chain Platform established ▪ **B1:** N° smallholder loans/legal entities (up to $50 000); 150 beneficiaries (USD 40 000 average loan size) ▪ **B2:** N° rural enterprises (income generating activities - up to $7 000); 450 beneficiaries (USD 5 000 average loan size) ▪ **B3:** N° rural processors/wholesalers loans (up to $150 000); 40 beneficiaries (USD 75 000 average loan size); N° of new rural businesses established/strengthened ▪ **B1, B2 & B3:** % of portfolio at risk; type of loans; N° of repeater loans; 50% of PFIs will have made provisions for start-up loans ▪ **B4:** PFIs and SCAs branches trained, Up to 150 business plans prepared for B1, Established seed Capital Guarantee Fund for SCA; Fee contribution from SVA borrowers to SCA Credit Guarantee Fund ▪ **C1:** N° of infrastructure beneficiaries; N° and type of infrastructure built; N° and amount of awarded competitive grants; Amount of co-financing leveraged for each infrastructure sub-investment; N° of groups managing infrastructure formed and/or strengthened; N° of groups managing infrastructure with women in leadership positions; N° of people in groups managing infrastructure	▪ Programme M&E database ▪ Progress reports ▪ PFI client records ▪ BDS client records ▪ Business plans and subsequent records ▪ Public sales records and enterprise records ▪ Evaluation report of Awareness Campaign and training programmes conducted by CPIU	▪ Political situation conducive to private investment ▪ Availability of potential investors to take entrepreneurial risks ▪ Financial institutions willing and able to address the intended target groups ▪ Financial institutions willing and able to develop remittance-based products

* All results measured to be disaggregated by gender where possible.