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President's memorandum

Modifications to the loan and financing agreements for:

**(1) Project for Enhancing the Rural
Economic Competitiveness of Yoro
(loan no. 743-HN) in the Republic of
Honduras; and**

**(2) Inclusion of Small-scale Producers
in Value Chains and Market Access
Project (loan no. 729-NI and grant
no. DSF-8009-NI) in the Republic of
Nicaragua**

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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Recommendation for approval

The Executive Board is invited to approve the modifications to the loan and financing agreements for:

(1) the Project for Enhancing the Rural Economic Competitiveness of Yoro (loan no. 743-HN) in the Republic of Honduras; and

(2) the Inclusion of Small-scale Producers in Value Chains and Market Access Project (loan no. 729-NI and grant no. DSF-8009-NI) in the Republic of Nicaragua

as contained respectively in paragraphs 8 and 16.

President's memorandum

Modifications to the loan and financing agreements for: (1) Project for Enhancing the Rural Economic Competitiveness of Yoro (loan no. 743-HN) in the Republic of Honduras; and (2) Inclusion of Small-scale Producers in Value Chains and Market Access Project (loan no. 729-NI and grant no. DSF-8009-NI) in the Republic of Nicaragua

I. Republic of Honduras

A. Background

1. At its ninety-second session in December 2007, the Executive Board approved a loan of SDR 4.55 million (equivalent to approximately US\$7.13 million) to the Republic of Honduras, on highly concessional terms, to help finance the Project for Enhancing the Rural Economic Competitiveness of Yoro (PROMECOM). This amount was within the performance-based allocation system (PBAS) allocation for Honduras for 2007-2009. Cofinancing of the US\$13.88 million project consists of a US\$4.00 million loan from the Central American Bank for Economic Integration (CABEI), and contributions of US\$1.05 million from the Government and US\$1.69 million from beneficiaries. The loan agreement was signed on March 2008 and ratified by the National Congress of Honduras on June 2008. In view of the progress made in fulfilling the conditions for loan effectiveness, the project is scheduled to start up in November 2008.

Food crisis impact and response

2. The Honduran economy has been hard hit by the rapid rise in global food prices as evidenced by increased poverty levels. This trend is expected to continue in the short and medium term. Most Hondurans, including rural populations, are net buyers of food and thus negatively affected by the soaring prices and the variability of national food production. On the other hand, higher food demand and prices, as well as the consolidating process of Central American economic integration, provide opportunities for smallholder farmers to participate in the kind of dynamic markets that will be promoted under PROMECOM.

Key project objectives

3. The project's development objective is to significantly reduce rural poverty in the department of Yoro. Its purpose is to improve the organizational capacities and territorial management practices of the rural poor, including indigenous groups, and to achieve better market positioning for their products. The project is expected to strengthen rural organizations, achieve sustainable territorial management and ensure that small-scale farmers are better served by technical assistance providers and financial institutions. The project as originally designed would have benefited directly 9,000 small-scale producers (45,000 rural inhabitants), including 2,000 indigenous households.

B. Proposed modifications to the loan agreement

4. Given the increased PBAS allocation to Honduras in the last PBAS revision,¹ the Government of Honduras formally requested in May 2008 that IFAD increase the loan for PROMECOM by about US\$2.25 million. This supplementary loan will enable

¹ The country scores of all "active" countries are updated annually to reflect changes in rural population, GNI and performance variables. They are then provided to the Executive Board at its December session for information as part of the annual report to the Board on the PBAS.

the project to reach 1,700 additional smallholders, helping them to improve grain, milk and vegetable production and marketing, and thus contributing to the increased availability of food in national and Central American markets.

5. The proposed increased loan amount will be borrowed by the Republic of Honduras substantially under the same terms and conditions as approved by the Executive Board in December 2007. The project objectives, components and strategy remain as described in the project design report and the loan agreement. The proposed modifications to the loan agreement are as follows:
 - (a) Allocation of an additional US\$1.52 million to the market insertion and positioning component, under the commercial initiatives fund expenditure category;
 - (b) Allocation of an additional US\$0.36 million to the organizational development and territorial management component, under the contracted services expenditure category; and
 - (c) Allocation of an additional US\$0.37 million for administration and management, under the salaries expenditure category.

Total project cost

6. With these additional resources, together with increased resources from the Government and beneficiaries (see next paragraph), the total project cost will increase from US\$13.88 million to US\$16.7 million. This will result in the following allocation increases: (i) market insertion and positioning component, from US\$5.0 million to US\$6.9 million; (ii) the organizational development and territorial management component, from US\$5.3 million to US\$6.4 million; and (iii) management and administration, from US\$2.6 million to US\$3.4 million.

Project financing

7. Project financing will be revised as follows: (i) the IFAD loan will increase from SDR 4.55 million to SDR 5.98 million (or from about US\$7.13 million to US\$9.4 million); (ii) the Government's contribution will increase from US\$1.05 million to US\$1.18 million; and (iii) the beneficiaries' contribution will increase from US\$1.69 million to US\$2.16 million. The CABEI loan will remain the same (US\$4.0 million).

C. Recommendation

8. I recommend that the Executive Board approve the proposed loan in terms of the following resolution:

RESOLVED: that the Fund shall make a supplementary loan to the Republic of Honduras in various currencies in an amount equivalent to one million four hundred and thirty thousand special drawing rights (SDR 1,430,000) to mature on or prior to 15 November 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 approved by the Executive Board at its ninety-second session in December 2007.

II. Republic of Nicaragua

A. Background

9. At its ninety-first session in September 2007, the Executive Board approved a loan and a grant to the Republic of Nicaragua to finance the Inclusion of Small-scale Producers in Value Chains and Market Access Project (PROCAVAL). The IFAD loan of SDR 2.55 million (equivalent to approximately US\$3.9 million) was extended on highly concessional terms, and was matched by a grant, within the Debt Sustainability Framework, of SDR 2.55 million. The total financing amount was within the PBAS allocation for Nicaragua for 2007-2009. Cofinancing of the

US\$21.7 million project consisted of a US\$2.0 million loan from CABEI, a US\$6.0 million loan from the OPEC Fund for International Development, and contributions of US\$4.4 million from the Government and US\$1.4 million from beneficiaries. The financing agreement was signed in January 2008 and ratified by the Nicaraguan Congress in May 2008. Progress has been made in fulfilling the conditions for loan effectiveness, and the project is scheduled to start up in November 2008.

Food crisis impact and response

10. Facing the crisis brought about by soaring food and input prices, the Government of Nicaragua formulated the National Food Production Strategy to ensure that basic grains (beans, corn and rice) were available domestically and for export to neighbouring countries. The strategy seeks to bring 67,000 smallholders into basic grain production nationwide. The official note sent by the Ministry of Agriculture to IFAD in this regard emphasizes that the strategy's target group, rural poor people, is the same as IFAD's, and that, like PROCAVAL, the strategy will address the food price crisis.

Key project objectives

11. The project's goal is to enable the targeted population to take part in local and national social and economic processes in order to improve their income and employment opportunities. In particular, the project will: (i) promote the participation of small-scale producers in strategic value chains; (ii) contribute to income diversification; and (iii) help achieve the objectives and results frameworks set by the Institute for Rural Development by aligning project activities with its institutional objectives. The project, as originally designed, would have benefited 8,000 households of small-scale producers, most of whom are organized in cooperatives and other rural organizations; 8,400 households of labourers, who will be contracted to implement the project's rural roads component; and 2,500 vulnerable households.

B. Proposed modifications to the financing agreement

12. Given the increased PBAS allocation to Nicaragua in the last revision,² the Government formally requested in April 2008 that IFAD increase the financing approved under PROCAVAL. Specifically, it sought supplementary financing of SDR 0.78 million (equivalent to approximately US\$1.22 million) in the form of a loan and a grant, both of SDR 0.39 million (or about US\$0.61 million). The supplementary financing will allow 1,200 additional smallholders to improve their production capabilities and incomes, and will also ensure that their produce reaches national and Central American markets.
13. The proposed increased loan and grant amounts will be extended to the Republic of Nicaragua substantially under the same terms and conditions as approved by the Executive Board in September 2007. The project objectives, components and strategy will remain as described in the project design report and the financing agreement. Proposed modifications to the financing agreement are as follows:
 - (a) Expand the value chain participation through the strategic alliances component, by supporting the National Food Production Strategy Fund;
 - (b) Create a new expenditure category under the heading of Support to the National Food Production Strategy Fund, with an allocation of about US\$1.0 million; and
 - (c) Allocate US\$0.22 million to strengthening technical assistance services, under the local initiatives fund expenditure category

² See footnote 1.

Total project cost

14. With these additional resources, together with increased resources from beneficiaries (see next paragraph), the total project cost will increase from US\$21.6 million to about US\$22.9 million. As a result, the allocation to the value chain component will increase from US\$10.3 million to US\$11.6 million; the allocation to the local initiatives fund expenditure category will increase from US\$3.24 million to US\$3.46 million; and an allocation of US\$1.0 million will be made to the new National Food Production Strategy Fund.

Project financing

15. Project financing will be revised as follows: (i) the IFAD loan will increase from SDR 2.55 million to SDR 2.94 million (or from about US\$3.9 million to US\$4.5 million); (ii) the grant amount will also increase from SDR 2.55 million to SDR 2.94 million (or from about US\$3.9 million to US\$4.5 million); and (iii) the beneficiaries' contribution will increase from US\$1.4 million to US\$1.5 million. The contributions of cofinanciers and the Government will remain unchanged.

C. Recommendation

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

RESOLVED: that the Fund shall make a supplementary loan to the Republic of Nicaragua in various currencies in an amount equivalent to three hundred and ninety thousand special drawing rights (SDR 390,000) to mature on or prior to 1 August 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 approved by the Executive Board at its ninety-first session in September 2007.

RESOLVED FURTHER: that the Fund shall provide a supplementary grant to the Republic of Nicaragua in various currencies in an amount equivalent to three hundred and ninety thousand special drawing rights (SDR 390,000) and upon such terms and conditions as shall be substantially in accordance with the terms and conditions approved by the Executive Board at its ninety-first session in September 2007.

Lennart Båge
President

