

Document: EB 2009/98/R.34/Rev.1
Agenda: 17(c)(iv)
Date: 17 December 2009
Distribution: Public
Original: English

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Enabling poor rural people
to overcome poverty

President's report

Proposed loan and grant to the Government of Nepal for the

High-Value Agriculture Project in Hill and Mountain Areas

Executive Board — Ninety-eighth Session
Rome, 15-17 December 2009

For: **Approval**

Note to Executive Board Directors

This document is submitted for approval by the Executive Board.

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Contents

Abbreviations and acronyms	ii
Recommendation for approval	iii
Map of the project area	iv
Financing summary	v
I. The project	1
A. Main development opportunity addressed by the project	1
B. Proposed financing	1
C. Target group and participation	2
D. Development objectives	2
E. Harmonization and alignment	2
F. Components and expenditure categories	3
G. Management, implementation responsibilities and partnerships	3
H. Benefits and economic and financial justification	4
I. Knowledge management, innovation and scaling up	4
J. Main risks	4
K. Sustainability	5
II. Legal instruments and authority	5
III. Recommendation	5
Annex	
Negotiated financing agreement	6
Appendices	
I. Key reference documents	
II. Logical framework	

Abbreviations and acronyms

AEC	Agro Enterprise Centre
MAPs	medicinal and aromatic plants
NTFP	non-timber forest products
SNV	SNV Netherlands Development Organisation

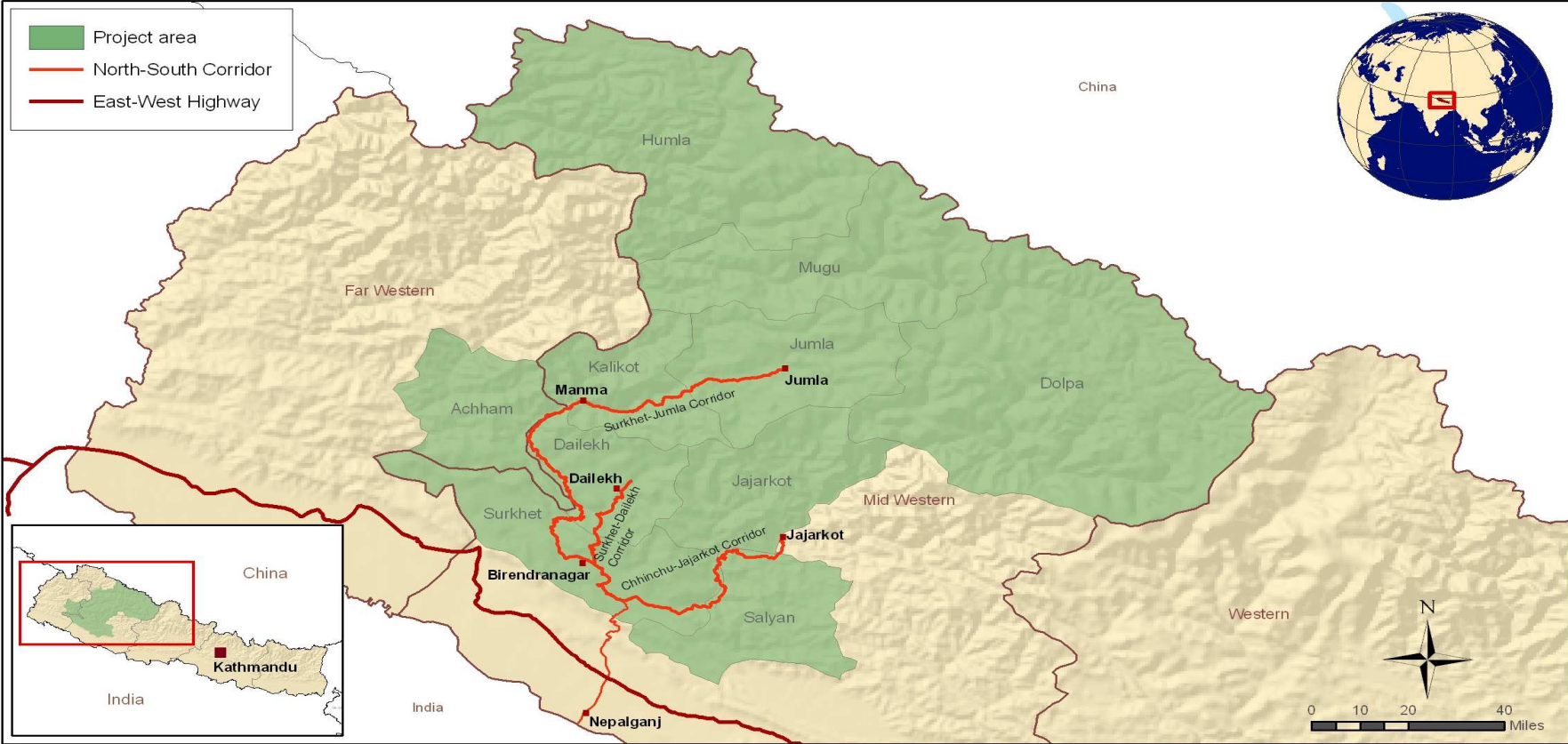
Recommendation for approval

The Executive Board is invited to approve the recommendation for the proposed financing to the Government of Nepal for the High-Value Agriculture Project in Hill and Mountain Areas, as contained in paragraph 36.

Map of the project area

Nepal

High-Value Agriculture Project in Hill and Mountain Areas



The designations employed and the presentation of the material in this map do not imply the expression of any opinion whatsoever on the part of IFAD concerning the delimitation of the frontiers or boundaries, or the authorities thereof.

Map compiled by IFAD

Government of Nepal

High-Value Agriculture Project in Hill and Mountain Areas

Financing summary

Initiating institution:	IFAD
Borrower:	Government of Nepal
Executing agency:	Ministry of Agriculture and Cooperatives
Total project cost:	US\$18.8 million
Amount of IFAD loan:	SDR 4.75 million (equivalent to approximately US\$7.6 million)
Amount of IFAD grant:	SDR 4.75 million (equivalent to approximately US\$7.6 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
Cofinanciers:	SNV Netherlands Development Organisation (SNV) Agribusinesses
Amount of cofinancing:	SNV: US\$0.7 million Agribusinesses: US\$0.6 million
Contribution of borrower:	US\$1.7 million
Contribution of beneficiaries:	US\$560,000
Appraising institution:	IFAD
Cooperating institution:	Directly supervised by IFAD

Proposed loan and grant to the Government of Nepal for the High-Value Agriculture Project in Hill and Mountain Areas

I. The project

A. Main development opportunity addressed by the project

1. To reduce poverty and social disharmony in hill and mountain areas, experience has shown that the issue of economic isolation needs to be addressed. Poverty persists in these areas because of poor infrastructure and access to services and markets. This has been exacerbated by conflict and economic exclusion linked to gender, ethnicity and caste. Stronger connectivity among farmers, input suppliers, traders/agribusinesses and downstream markets is fundamental to increasing agricultural diversification, productivity and incomes. Such increases can be achieved through initiatives focused on high-value crops, non-timber forest products (NTFPs), medicinal and aromatic plants (MAPs) and livestock. Appropriate pro-poor value chains and market systems for these high-value commodities can be developed through better access to technical services, finance, input supplies and market information, and improved infrastructure. The project is designed to exploit the unsatisfied demand for these commodities from the private sector and the opportunities for export and import substitution.

B. Proposed financing

Terms and conditions

2. It is proposed that IFAD provide to the Government of Nepal a loan in the amount of SDR 4.75 million (equivalent to approximately US\$7.6 million), on highly concessional terms, and a grant in the amount of SDR 4.75 million (equivalent to approximately US\$7.6 million) to help finance the High-Value Agriculture Project in Hill and Mountain Areas. 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 the Government of Nepal under the PBAS is US\$21.9 million over the 2007-2009 allocation cycle. The remaining US\$15.3 million for the current 2007-2009 PBAS cycle will be committed in full under this project.

Country debt burden and absorptive capacity of the State

4. Under IFAD's Debt Sustainability Framework, Nepal is categorized as being at medium risk of debt vulnerability and is therefore eligible for 50 per cent grant financing in 2009.

Flow of funds

5. The IFAD financing will be channelled to a designated account for the loan and grant, managed by the project management unit. Funds will flow to an operating account, also managed by the project management unit. IFAD funds may also be paid directly to service providers in accordance with established IFAD procedures.

Supervision arrangements

6. The project will be directly supervised by IFAD.

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

7. No exceptions are foreseen.

Governance

8. The following planned measures are intended to enhance the governance aspects of the IFAD financing: (i) establishment of social auditing and public audit groups; (ii) internal and external auditing; (iii) transparent dissemination of information and awareness-building among project stakeholders and beneficiaries; and (iv) strict selection and eligibility criteria for project activities.

C. Target group and participation

Target group

9. The overall target group consists of the members of poor and vulnerable households that lack access to resources and opportunities. The most vulnerable among this group are women and members of socially disadvantaged groups such as *dalits* and indigenous groups (*janajatis*).

Targeting approach

10. In accordance with the IFAD Policy on Targeting, the project will target poor and vulnerable households living in the ten project districts. It will follow a social inclusion approach, with an emphasis on women's participation. A combination of targeting and monitoring strategies will be used to involve poor people and facilitate social inclusion, including geographical targeting, social/community targeting, proactive involvement of risk-averse households and spatial inclusion of poor remote communities.

Participation

11. A key feature of the project is the participation of all market actors in the pro-poor value chain development, which will be facilitated by an interactive planning and implementation process led by local and national NGOs.

D. Development objectives

Key project objectives

12. The goal of the project is to reduce the poverty and vulnerability of women and men in hill and mountain areas of the Mid-Western Development Region. The purpose of the project is the integration of rural poor people, especially women and marginal groups, into high-value agriculture and NTFP/MAP value chains and markets, better income and employment opportunities as a result of marketing agreements with private agribusiness, and greater ability to respond to market demand and opportunities.

Policy and institutional objectives

13. Influencing the policies affecting access to economic opportunities by poor farmers and producers in hill and mountain areas is a key objective. The project's institutional strategy is to work directly with the agribusinesses and market players to strengthen value chains and the position of poor producers to actively participate in the market on a fair and equitable basis.

IFAD policy and strategy alignment

14. The project is fully aligned with the objectives of the IFAD country strategic opportunities programme (COSOP) 2007-2012 for Nepal and the IFAD Strategic Framework 2007-2010.

E. Harmonization and alignment

Alignment with national priorities

15. The project has been designed within the context of the COSOP and responds directly to the key government policy initiatives of Nepal's poverty reduction strategy (PRS). Both the COSOP and the PRS stress the importance of (i) increasing the economic opportunities of poor farmers and producers in hill and mountain areas, (ii) supporting private-sector development through public/private partnerships, and

(iii) reducing gender, ethnic and caste-related disparities through greater inclusion of disadvantaged groups in development.

Harmonization with development partners

16. An extensive consultation process led by the Government has been undertaken with development partners in Nepal. The project will work with other ongoing agriculture commercialization projects and participate in a national value chain working group.

F. Components and expenditure categories

Main components

17. The project has three components: (i) pro-poor value chain development; (ii) inclusion and support for value chain initiatives; and (iii) project management. The second component has the following subcomponents: (a) group formation and strengthening; (b) social and gender inclusion; (c) production/post-harvest support; (d) a value chain fund; and (e) district participation and spatial inclusion.

Expenditure categories

18. There are five expenditure categories: (i) vehicles and equipment (1.1 per cent); (ii) studies, surveys, training and workshops (18.7 per cent); (iii) service provider contracts (31.1 per cent); (iv) funds (38.2 per cent); (v) recurrent costs: salaries (6.4 per cent) and operation and maintenance (4.5 per cent).

G. Management, implementation responsibilities and partnerships

Key implementing partners

19. The lead project agency is the Ministry of Agriculture and Cooperatives (MOAC). Other key project partners are the SNV Netherlands Development Organisation (SNV); the Agro Enterprise Centre (AEC); selected national/local NGOs; district agricultural development offices (DADOs); agribusinesses; producers' groups; and cooperatives.

Implementation responsibilities

20. This project will be implemented under the responsibility of MOAC. The Government's role focuses on financial and institutional oversight, technical support and guidance, monitoring and coordination. The SNV will assume overall responsibility for the implementation of the first component and provide support, technical advice and backstopping for development initiatives in the second. The SNV will work with AEC to mentor and develop its capacity to assume part of the responsibility for implementation as SNV phases out in project year (PY) 3/PY 4. SNV will also support the project in monitoring and evaluation, knowledge management and learning exchange, and policy initiatives. National and local NGOs will be responsible for implementing activities in the participating communities. DADOs will coordinate the work of the project in the districts, facilitate the harmonization of the project with district development plans and help organize technical support by crop/forestry/livestock officers.

Role of technical assistance

21. Predominantly local technical assistance will be used to supplement project staff and will form part of the project management framework to ensure that the established value chains function effectively.

Status of key implementation agreements

22. The key implementation agreements include partnership/implementation agreements and memorandums of understanding between key implementation partners.

Key financing partners and amounts committed

23. The total project cost is US\$18.8 million over six years. The sources of financing are: IFAD, with a loan (40.5 per cent) and a grant (40.5 per cent); the Government

(9.1 per cent); the SNV (3.7 per cent), agribusinesses (3.2 per cent), and the beneficiaries (3 per cent).

H. Benefits and economic and financial justification

Main categories of benefits generated

24. Within the project area, the project is expected to benefit directly and indirectly about 52,000 households (285,000 people), or about 20 per cent of the population of 1.4 million people. Some 15,000 households will benefit directly from participation in the project's value chains.
25. The project will generate a range of benefits both from the value chain development itself and from the supporting activities: (i) more efficient and profitable value chain systems for high-value commodities for producers in the Mid-Western Region; (ii) poor producers able to increase their income and sustain those increases by engaging profitably in high-value commodity production and marketing; (iii) women's status and incomes improve and the gender balance in rural households is enhanced; (iv) the landless and quasi-landless find employment through project vocational training/job placement and thus are able to increase their incomes; (v) very remote communities more accessible and better able to market high-value, low-volume commodities; (vi) increased number and capacity of pro-poor rural institutions enabling poor people and minority groups to participate in markets; and (vii) lessons learned from the innovative approaches developed under the project captured and disseminated for the benefit of the Government, projects and development practitioners.

Economic and financial viability

26. The economic rate of return for the project is estimated at 25 per cent.

I. Knowledge management, innovation and scaling up

Knowledge management arrangements

27. To facilitate the effective management of knowledge and learning, the project will focus on: (i) strengthening knowledge-sharing and learning processes; (ii) developing a knowledge-sharing and learning infrastructure; and (iii) fostering partnerships for broader knowledge-sharing and learning. SNV will use its specialized competence in this area to support project knowledge management processes.

Development innovations that the project will promote

28. The main project innovation is its approach to market-led value chain development, which uses the entrepreneur as the starting point, rather than the producer. The project's focus on supporting the development of pro-poor, high-value agriculture deviates from the usual concentration on staples and bulk markets. The project represents a move away from a geographically driven implementation approach by seeking to scale up and replicate an implementation strategy based on road corridors, production potential and improved market access.

Scaling-up approach

29. The project scales up various pilot approaches and integrates lessons learned from the country programme. A multiplier effect will be produced by the sharing and dissemination of ideas, approaches and lessons. This will also promote the scaling up and replication of activities in the target districts during the project period.

J. Main risks

Main risks and mitigation measures

30. The project faces three main risks: (i) Nepal is currently in a difficult political transition period, which could have an adverse impact on the project; (ii) possible shortfall in private-sector demand for high-value commodities from poor small producers; and (iii) high turnover of project staff and the quality of government officers willing to work in the more remote areas. For the first risk, while there are

substantial changes occurring in the country, no major changes are expected to the policies on which the project is based. For the second risk, it is considered that the interest expressed by agroenterprises, traders and wholesalers in the project and the local and international demand for the high-value commodities that can be produced in the project area justify the project's focus on developing pro-poor value chains of this kind. If demand proves lower than expected or slower to develop, the project has the flexibility to adapt. The third risk is addressed through competitive recruitment processes. Most of the project management unit positions will be filled by contracted experts whose terms and conditions will create the incentive to find and maintain suitable candidates.

Environmental classification

31. Pursuant to IFAD's environmental assessment procedures, the project has been classified as a Category C operation in that it is unlikely to have any environmental impact.

K. Sustainability

32. The approach of developing value chains with private-sector partners should enable the main project activities to continue after the project as long as the value chains developed continue to generate profits for both the producers and the agribusinesses. As there are no subsidies provided by the project that would distort the ongoing production of the commodities, project closure should not result in the withdrawal of agribusinesses from the project's value chains.

II. Legal instruments and authority

33. A financing agreement between the Government of Nepal and IFAD will constitute the legal instrument for extending the proposed financing to the borrower/recipient. A copy of the negotiated financing agreement is attached as an annex.
34. The Government of Nepal is empowered under its laws to receive financing from IFAD.
35. I am satisfied that the proposed financing will comply with the Agreement Establishing IFAD and the Lending Policies and Criteria.

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 on highly concessional terms to the Government of Nepal in an amount equivalent to four million seven hundred and fifty thousand special drawing rights (SDR 4,750,000), and 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 Government of Nepal in an amount equivalent to four million seven hundred and fifty thousand special drawing rights (SDR 4,750,000) and upon such terms and conditions as shall be substantially in accordance with the terms and conditions presented herein.

Kanayo F. Nwanze
President

Negotiated financing agreement:

"High Value Agriculture Project in Hill and Mountain Areas"

(Negotiations concluded on 9 December 2009)

Loan Number: _____

Grant Number: _____

Project Title: High Value Agriculture Project in Hill and Mountain Areas (HVAP) (the "Project")

The International Fund for Agricultural Development (the "Fund" or "IFAD")

and

the Government of Nepal (the "Borrower/Recipient")

(each a "Party" and both of them collectively the "Parties")

hereby agree as follows:

Section A

1. The following documents collectively form this Agreement: this document, the Project Description and Implementation Arrangements (Schedule 1), the Allocation Table (Schedule 2), and the Special Covenants (Schedule 3).
2. The Fund's General Conditions for Agricultural Development Financing dated 29 April 2009, as may be amended from time to time (the "General Conditions") are annexed to this Agreement, and all provisions thereof shall apply to this Agreement. For the purposes of this Agreement the terms defined in the General Conditions shall have the meanings set forth therein.
3. The Fund shall provide a Loan and a Grant to the Borrower/Recipient (the "Financing"), which the Borrower/Recipient shall use to implement the Project in accordance with the terms and conditions of this Agreement.

Section B

1. The amount of the Loan is four million seven hundred and fifty thousand Special Drawing Rights (SDR 4 750 000).
2. The amount of the Grant is four million seven hundred and fifty thousand Special Drawing Rights (SDR 4 750 000).
3. The Loan is granted on highly concessional terms as provided for in Section 5.01 (a) of the General Conditions.
4. The Loan Service Payment Currency shall be the US dollar.

5. Payments of principal and service charge shall be payable on each 1 June and 1 December, with payments of principle commencing on 1 June 2020.
6. There shall be a Project Account for the benefit of the Lead Project Agency in a bank acceptable to the Fund.
7. The first day of the applicable Fiscal Year shall be 16 July.
8. The Borrower/Recipient shall provide counterpart financing to the Project for the amount of one million seven hundred and twenty four thousand United States Dollars (1 724 000 USD) to reimburse taxes paid by the Project and for other purposes.

Section C

1. The Lead Project Agency shall be the Ministry of Agriculture and Cooperatives of the Borrower/Recipient.
2. Additional Project Parties include but are not limited to service providers and institutions mentioned in Schedule 1.
3. The Project Completion Date shall be the seventh anniversary of the date of entry into force of this Agreement.

Section D

The Loan and Grant will be administered and the Project supervised by the Fund.

Section E

1. The following is designated as an additional ground for suspension of this Agreement: the Project Manager shall have been appointed or removed from the Project without the prior concurrence of the Fund.
2. (a) The following are designated as additional general conditions precedent to withdrawal:
 - (i) the Project Steering Committee (PSC) and Project Consultative and Coordination Committee shall have been established and the members selected;
 - (ii) the Project Manager for the Project Management Unit shall have been selected and appointed, through a competitive selection process, and shall be acceptable to the Fund;
 - (iii) the Accounts Officer and the Administrative Officer for the Project Management Unit shall have been designated and shall be acceptable to the Fund;
 - (iv) the members of the Project Management Unit shall have been contracted within 9 months of entry into force of this Agreement and shall be acceptable to the Fund; and
 - (v) a final draft version of the Project Implementation Manual shall have been approved by the Borrower/Recipient and by the Fund.
- (b) The following is designated as an additional specific condition precedent to withdrawal: disbursement under Category IV will commence only once Eligibility

Guidelines and Procedures for the funds satisfactory to the Fund, have been prepared, and contracting of NGO service providers has been completed.

3. The following are the designated representatives and addresses to be used for any communication related to this Agreement:

For the Fund:

President
International Fund for Agricultural Development
Via Paolo di Dono 44
00142 Rome, Italy

For the Borrower/Recipient:

Secretary
Ministry of Finance
Singhdurbar, Kathmandu
Nepal

This agreement, dated _____, has been prepared in the (English) language in six (6) original copies, three (3) for the Fund and three (3) for the Borrower/Recipient.

For the Fund
(Name and Title)

For the Borrower/Recipient
(Name and Title)

Schedule 1

Project Description and Implementation Arrangements

I. Project Description

1. *Target Population.* The Project shall benefit about 52 000 poor and vulnerable households living in the Project Area in the Mid-Western Development Region. The overall target group shall consist of the members of poor and vulnerable households that lack access to resources and opportunities. The most vulnerable among this group are women and members of socially disadvantaged groups such as dalits and indigenous groups (*janajatis*).

2. *Goal.* The Project shall contribute to the reduction of poverty and vulnerability of women and men in hill and mountain areas of the Mid-Western Development Region.

3. *Purpose.* The Project purpose shall be that the rural poor, especially women and marginal groups, are integrated in high value agriculture and Non-timber forest products (NTFPs), medicinal and aromatic plants (MAPs) value chains and markets and have improved income, employment opportunities and ability to respond to market demand and opportunities based on marketing agreements with private agribusinesses.

4. *Outcomes.* Four key outcomes are expected from the Project:

- (a) improved commercial linkages and partnerships between agricultural/NTFP/MAP market operators and producers result in profitable, efficient, market-oriented production of high value commodities for 13 500 beneficiary households;
- (b) increased participation and access of poor marginal producers in high value commodity value chains and agricultural/NTFP markets;
- (c) small poor farmers and other rural producers benefit from sustainable increases in volume and value of production as a result of improved production/collection, value addition and sales of high value niche market products; and
- (d) enhanced environment and strengthened local capacity to support market driven/value chain initiatives.

5. *Components.* The Project shall consist of the following Components:

5.1 Component 1. - Pro-Poor Value Chain Development. The objective of this component shall be to facilitate mutually beneficial and profitable production and marketing arrangements between producers of high value commodities and agribusinesses.

5.2 Component 2. - Inclusion and Support for Value Chain Initiatives. The objective of the component shall be that small poor farmers and other rural producers benefit from sustainable increases in volume and value of production as a result of improved production/collection, value addition and sales of high value niche market products and strengthened local capacity for market-driven initiatives. The component shall consist of the following subcomponents: (a) group formation and strengthening; (b) social and gender inclusion; (c) production/post-harvest support; (d) a value chain fund; and (e) district participation and spatial inclusion.

5.3. Component 3. - Project Management. The objective shall be to provide effective implementation through technical, financial and contract management of the Project

within the context of gender and poverty targeted value chain development. The Project Management Unit will also ensure the effective monitoring and evaluation of Project activities.

II. Implementation Arrangements

1. The Ministry of Agriculture and Cooperatives (MOAC) shall be the Lead Project Agency. In this capacity, the MOAC shall have overall responsibility for the Project and for the establishment and chairmanship of the PSC and the area-based Project Consultative and Coordination Group. To ensure effective delivery of the Project and achievement of development objectives, a major part of the Project shall be implemented through service providers such as local and national NGOs, which shall be selected through a competitive selection process. The government's role shall be focused on financial and institutional oversight, technical support and guidance, monitoring and coordination.
2. The Project's collaborative framework comprises three main bodies: the PSC, the High Value Agriculture Project in Hill and Mountain Areas (HVAP) Agribusiness Working Group, and an Area-Based Project Consultative and Coordination Group.
 - (a) The PSC shall be chaired by the Secretary of the MOAC. It shall review Project progress against targets, assess its effectiveness in achieving its poverty/social inclusion and gender objectives, review lessons learned, assess management effectiveness and each year review and approve Annual Work Plans and Budgets. It shall have a balanced membership representing government, the private sector and NGOs.
 - (b) The HVAP Agribusiness Working Group shall be a forum for agribusinesses to discuss topics that are of particular concern to them, raise issues and present ideas and proposals to the Project team. It is foreseen to grow into a body to serve the high value agricultural/NTFP/MAP sector as a whole and work with other value chain projects and programmes.
 - (c) The Consultative and Coordination Group shall act as a forum to discuss issues and review opportunities and progress and to facilitate coordination with government bodies, agribusinesses and other related projects/development initiatives operating in the Project area.
3. In addition, social audits, using district-based Public Audit Groups shall be instituted to make Project implementation more transparent, accountable and locally manageable. They shall monitor, supervise and evaluate Project activities within the value chain groups and communities and provide a forum for raising issues and concerns.
4. The Project Management Unit (PMU), to be based in the district of Surkhet, shall be headed by a competent Project Manager competitively selected from MOAC, subject to prior approval by IFAD. The majority of experts from the PMU shall be contracted. The Project Manager shall have been selected and appointed, through a competitive selection process, and shall be acceptable to the Fund, and the Accounts Officer and the Administrative Officer for the Project Management Unit shall have been designated and seconded from MOAC and shall be acceptable to the Fund. The Netherlands Development Organisation (SNV) team, which shall be responsible for the implementation of Component 1, shall assist in the coordination of activities in Component 2 and support knowledge management, and shall be part of the PMU and be based in the Project offices. The senior SNV expert shall be the senior technical project management expert in the PMU and the chief advisor to the Project Manager.

5. *Main Implementing Agencies and Roles:*

- (a) MOAC – shall assume overall management responsibility for the Project, chair the PSC, the area-based Project Consultative and Coordination Group and guide the PMU.
- (b) SNV – shall be the main partner with MOAC in Project implementation. It shall assume overall responsibility for the implementation of Component 1 (Pro-Poor Value Chain Development), and provide support, technical advice and backstopping for the Project's other development initiatives contained in Component 2 (Inclusion and Support for Value Chain Initiatives). It shall also assume direct responsibility for implementation of the following two activities under Sub-component 2(b), (Gender and Social Inclusion): (i) Service Provider Awareness and Training; and (ii) Gender/Social Inclusion Strategy/Tools Development. It shall also assume the lead role in guiding knowledge management activities under the Project and facilitate learning exchange and policy dialogue/response. As part of its responsibility for Component 1, it shall work with Agro Enterprise Centre (AEC) and act as a mentor to develop capacity of the organization to assume part of the responsibility for implementation as SNV phases out between the third and fourth Project Year.
- (c) AEC – is the institution charged with facilitating business development in the agricultural sector nationally, linked to the Federation of Nepalese Chambers of Commerce and Industry (FNCCI). It shall also fulfil this role in the Project. The two officers seconded to the Project shall progressively assume responsibility for the business side of the value chain development. They shall work jointly with the SNV experts for the first three years and take over from them by 2012/13. By working with SNV, AEC shall build an understanding and capacity within the organization to manage the 'inclusive business' approach and become an active player in supporting value chain development.
- (d) Local NGOs/service providers – shall be responsible for a major part of Project implementation and be the main Project-designated experts implementing Project activities in the participating communities.
- (e) National NGO – shall provide higher level expertise and fulfil a supervision, oversight and capacity building function in relation to the local NGOs/service providers.
- (f) District Agriculture Development Offices (DADOs) – shall be the main point of contact within the participating Project districts. They shall play a major role in coordinating the work of the Project in the districts, facilitate the harmonization of the Project with the district development plans and help organize technical support from their crop and livestock officers. The district forest officers and district livestock officers shall fulfil a similar role for NTFP/MAPs and livestock respectively. The DADO shall also assume prime responsibility for implementing the District-based Farming Systems/Food Security Facility under Sub-component 2(c) and work with the PMU in determining the priority areas and infrastructure projects to be financed by the Project under the District Spatial Inclusion Fund.

6. *Project Funds.* The Project shall create under Component 2, three separate funds for supporting the development of value chains established under Component 1. Eligibility Guidelines and Procedures will be included in the Project Implementation Manual.

- (a) Production Inputs Fund. As many of the farmers are too poor to be able to pre-finance the inputs needed for production of the high value commodities, the Project shall provide support to value chain groups in the form of a grant.

This funding shall in turn be revolved at the group level in each value chain group to sustain a mechanism for supporting the supply of inputs. The local NGOs shall assume responsibility for providing assistance to value chain groups in establishing and managing the revolving funds. Additional guidance and oversight shall be provided by the Funds and Contracts Manager based in the PMU and the selected national NGO. The funding, to be released directly from the PMU to the group once the local NGO gives its approval, shall be made available based on the proposed production plan as contained in the value chain business plan (agreed with the PMU and the participating agribusiness(es)). Each group shall set up an account in an approved bank to hold the revolving fund.

- (b) Value Chain Fund. The purpose of the Value Chain Fund shall be to allow value chain groups to make essential investments to facilitate the production and subsequent primary processing/storage of the selected high value commodities. Based on the business plans developed under Component 1, the range of investments from this Fund could include small-scale infrastructure required to produce, store and carry out primary processing and simple conversion. The plans shall include: a full technical and financial assessment and justification for the investment; the constraints and/or opportunities that the investment addresses; the integration of the investment into the value chain and the value added; the contribution to be made by the value chain group members (at least 10% shall be required) and the agribusiness; and the ownership, operation and maintenance arrangements for the infrastructure/equipment once in place. The Value Chain Fund shall be under the responsibility of the Funds and Contract Manager within the PMU. The support to groups involved in a value chain investment project (infrastructure, equipment, or a combination) shall rest with the local NGOs. A funds consultative committee shall be set up to review all submissions for utilization of the funds – this committee shall also fulfil the same function for the District/Spatial Inclusion Fund. The members of the committee shall be proposed by the PMU, in consultation with MOAC and IFAD, to be submitted to the PSC for approval.
- (c) District Spatial Inclusion Fund. To facilitate the participation of more remote communities in value chain activities, and promote spatial equity, a matching grant fund shall be established to finance infrastructure to improve accessibility to those areas that have been identified as having high potential for high value commodities, particularly NTFPs/MAPs. The types of infrastructure foreseen include simple bridges, pulley traversing systems, and ropeways. The establishment of the District Spatial Inclusion Fund shall be initiated through a series of working sessions held between the regional offices (agriculture, forestry and livestock) and participating districts with the PMU to assess which of each district's remote communities shall have the best potential for producing high value products if their access were to be improved through the construction of simple bridges or other structures. The funds shall be provided by the Project on a matching grant basis with the communities guaranteeing 10% and the districts/Village Development Committees providing another 10% from their development funds.

7. *Project Implementation Manual*. The PMU shall finalise the Project Implementation Manual (PIM) and shall submit the PIM to IFAD for no objection and to the PSC for approval.

Schedule 2

Allocation Table

1. *Allocation of Loan and Grant Proceeds.* (a) The Table below sets forth the Categories of Eligible Expenditures to be financed by the Loan and Grant and the allocation of the amounts of the Loan and Grant to each Category and the percentages of expenditures for items to be financed in each Category:

Category	Loan Amount Allocated (expressed in SDR)	Grant Amount Allocated (expressed in SDR)	Percentage of Eligible Expenditures to be financed
I. Vehicles and Equipment	50 000	50 000	85% or 100% net of tax for imported vehicles
II. Studies, Surveys, Training, and Workshops	850 000	850 000	85%
III. Service Provider Contracts	1 250 000	1 250 000	75%
IV. Funds	1 650 000	1 650 000	100%, excluding Government and beneficiary contribution where applicable
V. Recurrent Costs			
a. Salaries	270 000	270 000	100% net of Government staff positions
b. Operation and Maintenance	200 000	200 000	85%
VI. Unallocated	480 000	480 000	
TOTAL	4 750 000	4 750 000	

(b) Expenditures from the Loan and Grant are to be shared pari-passu at the ratio of 50:50

Schedule 3

Special Covenants

In accordance with Section 12.01(a) (xxiii) of the General Conditions, the Fund may suspend, in whole or in part, the right of the Borrower/Recipient to request withdrawals from the Loan and/or Grant Account if the Borrower/Recipient has defaulted in the performance of any covenant set forth below, and the Fund has determined that such default has had, or is likely to have, a material adverse effect on the Project:

1. *Gender.* The Borrower/Recipient shall ensure that women beneficiaries shall be represented in all Project activities and that they receive appropriate benefits from the Project outputs.
2. *Tax Exemption.* The Borrower/Recipient shall, to the fullest extent possible, exempt the proceeds of the Loan and the Grant from all taxes. Any taxes which the Project is nonetheless obliged to pay shall be promptly reimbursed by the Borrower/Recipient.

Key reference documents

Country reference documents

Tenth Year Plan and Interim Three Year Plan

National Agricultural Policy

IFAD reference documents

Project Design Document, Appendices and Annexes

COSOP

Administrative Procedures on Environmental Assessment

Logical framework

Objectives-hierarchy	Objectively verifiable indicators	Means of verification	Assumptions
<p>Goal The overall goal is the reduction of poverty and vulnerability of women and men in hill and mountain areas of the Mid-Western Development Region</p>	<ul style="list-style-type: none"> * No of hhs with improvement in household assets ownership index [RIMS indicator] * % reduction in prevalence of child malnutrition (weight for age) [RIMS indicator] 	<p>RIMS Impact Assessments Outcome Surveys including Household Income and Expenditure Surveys</p>	<p>Nepal has a stable social and economic climate that is conducive to value chain development Larger policy and institutional environment remains favourable</p>
<p>Purpose Rural poor, especially women and marginal groups, are integrated in high value agriculture and NTFP/MAP value chains and markets and have improved income, employment opportunities and ability to respond to market demand and opportunities based on marketing agreements with private agribusiness</p>	<ul style="list-style-type: none"> * % and number of producers in the project area reporting increased incomes by gender, social group, district (target 13 500 hh or 81,000 direct beneficiaries) * Change in % and volume of surplus agricultural production and NTFP/MAPs marketed profitably by participating producers and traders 	<p>Project baseline, Mid-term and impact surveys Annual Outcome level assessments Government and FNCCI statistics at district, regional and national level</p>	<p>Demand for high value commodities is sufficient to realize the projected development of pro-poor value chains and the subsequent productive and profitable partnerships Continued commitment of Government of Nepal to facilitate commercialization of agriculture through market led approaches</p>
<p>Objectives Component 1. To facilitate mutually beneficial and profitable production and marketing arrangements between poor and marginal producers of high value commodities and agri-businesses Component 2. Small poor farmers and other rural producers benefit from sustainable increases in volume and value of production of as a result of improved production/collection, value addition and sales of high value niche market products and strengthened local capacity for market driven initiatives</p>	<ul style="list-style-type: none"> * 60% of contractual relationships between producer groups and agribusinesses/market operators operating after two years (based on 1000 contracts supported by business plans, assuming 2 contracts per producer group) * % of poor and marginal producers entering into high value commodity contractual arrangements with agribusinesses each year (target 750 hhs per VC) * Number of farmers reporting production/yield increases in high value niche market commodities 	<p>Project baseline and impact surveys Annual Outcome Assessments Value Chain Baseline and completion Assessments Qualitative post-intervention assessments (case studies), Special Studies/ assessments Government and AEC/FNCCI statistics</p>	<p>Agribusinesses, traders and agro-processors expand activities in a manner that benefits the project's poor producers Agribusinesses are and continue to be interested in developing and entering into contracts with poor producers from Mid-Western Region The terms of trade for producers of agricultural, NTFP/MAPs commodities remain favourable and increase their returns from high value products</p>
<p>Outputs Output 1.1 Contractual arrangements between producers groups and agribusinesses functioning effectively, sustainably and benefiting both parties in targeted value chains Output 1.2 Strengthened institutional capacity for delivery and facilitation of market opportunities, information and support services Output 1.3 Women, <i>dalits</i>, <i>janajatis</i> and other poor and vulnerable groups well represented, actively involved and benefiting from participation in project value chains Output 2.1 Small scale producers organized in groups, with a high proportion of women and vulnerable groups, are better able to respond to market demand and opportunities Output 2.2 High portion of risk adverse persons/households and landless in project communities participate in the project Output 2.3 volumes of agricultural commodities and NTFPs/MAPs are being produced in the quantities and qualities specified in contracts with agribusinesses</p>	<ul style="list-style-type: none"> * 750 contractual agreements established and sustained for three years for a subset of about 18 value chains (on basis of 18 VC assessments & analysis and 1 000 VC contracts) * 60% women participate and benefit from the project * At least 25% <i>Dalits</i>, <i>Janajatis</i> and other minorities participate and benefit from the project * At least 500 producer marketing groups formed/ strengthened and operational * No of people trained in post production, processing and marketing. (minimum of 1,450 lead farmers) * 10% of producers in value chain groups amalgamate into cooperatives * 800-900 risk averse persons/households have joined value chain groups and participate in the project * At least 2 500 people receiving vocational training consisting of at least 60% women * 500 value chain groups report incremental sales of high value commodities as stipulated in contracts with agribusinesses 	<p>Annual Outcome Assessments Baseline and completion Value Chain Studies Qualitative post-intervention assessments (case studies), Special Studies/ assessments Project progress reports, Government, AEC reports</p>	<p>Farmers groups identified and selected are willing to participate in project activities. Assumes that private sector will be able to make available the inputs needed for these commodities There is sufficient demand for the high value commodities that can be produced in the project area Road network development allows reaching out remote communities</p>

