Document:	EB 2014/LOT/P.11
Date:	1 August 2014
Distribution:	Public
Original:	English

E

Investing in rural people

President's memorandum

Proposal for additional financing to Papua New Guinea for the Productive Partnerships in Agriculture Project

Note to Executive Board representatives

Focal points:

Technical questions:	Dispatch of documentation:
Ronald Hartman Country Programme Manager Tel.: +39 06 5459 2184 e-mail: r.hartman@ifad.org	**Deirdre McGrenra** Head, Governing Bodies Office Tel.: +39 06 5459 2374 e-mail: gb_office@ifad.org

For: **Approval**

Recommendation for approval

The Executive Board is invited to approve the recommendation for the proposed additional financing in the form of a loan to Papua New Guinea for the Productive Partnerships in Agriculture Project as contained in paragraph 23

President's memorandum

Proposal for additional financing to Papua New Guinea for the Productive Partnerships in Agriculture Project

I. Background

1. This memorandum seeks approval for additional financing in the form of a loan of approximately US$22 million (equivalent to SDR 14.23 million) for the Productive Partnerships in Agriculture Project (PPAP) approved by the Executive Board in April 2010 (EB 2010/99/R.22). With the additional financing, IFAD will cofinance – together with the Government of Papua New Guinea, the World Bank, the European Union and project beneficiaries – the costs of scaling up the project nationally to target an additional 36,000 direct beneficiary households.

2. The PPAP was originally designed in partnership with the World Bank and the Government of Papua New Guinea. The project became effective in September 2010 and its completion date is June 2016. Its main objective is to improve the livelihoods of smallholder cocoa and coffee producers by improving the performance and sustainability of value chains in cocoa- and coffee-producing areas. The original project has three components: (i) institutional strengthening and industry coordination; (ii) productive partnerships; and (iii) market access infrastructure. The project supports improvement in rural livelihoods through strengthening industry coordination and institutions; facilitating linkages between smallholder farmers and agribusiness to provide market access, technologies and services; and providing critical infrastructure for market access. The original design envisaged scaling up the project to new areas and expanding existing partnerships.

3. Based on the performance of the PPAP, both the World Bank and the European Union have already approved additional financing for scaling up the project nationally. IFAD and the Government of Papua New Guinea (GOPNG) have agreed that US$22 million from the 2013-2015 performance-based allocation system (PBAS) cycle should also be used to scale up the project.

Table 1
Total project financing, by financier
(Thousands of United States dollars)

	Original financing		*Additional financing*		*Total financing*	
Source	*Amount*	*Share of total (%)*	*Amount*	*Share of total (%)*	*Amount*	*Share of total (%)*
World Bank	25 000	54	30 000	41	55 000	46
IFAD	14 000	30.2	22 000	30	36 000	30.1
European Union	-	-	6 400	9	6 400	5.4
GOPNG	1 500	3.2	4 500	6	6 000	5.2
Beneficiaries	5 800	12.5	10 100	14	15 900	13.3
Total	**46 300**	**100**	**73 000**	**100**	**119 300**	**100**

II. Justification and rationale

4. Most of the rural population in Papua New Guinea rely on coffee and cocoa for their livelihoods. In recent years, both the coffee and the cocoa sectors in the country have faced threats to their competitiveness and overall sustainability. This has had a significant negative impact on the rural populations for whom coffee and cocoa are a main source of income.

5. The PPAP provides predictable and continued support to implement the structural changes necessary to improve the performance and sustainability of Papua New Guinea's coffee and cocoa value chains and to increase their contribution to rural livelihoods. The PPAP has been successful in strengthening industry coordination; facilitating linkages between cocoa and coffee smallholder farmers and agribusiness to provide market access, technologies and services; and supporting the development of critical market infrastructure. The project has generated strong demand from smallholder cocoa and coffee farmers, many of whom are receiving support and services for the first time. Linking farmers to lead partners, most of which are key private-sector actors in the cocoa and coffee sectors, has proved to be an effective and innovative approach for delivering needed services to farmers and for strengthening value chain linkages.

6. The provision of additional financing presents IFAD with an opportunity to scale up its impact, strengthen its partnerships and expand its future engagement in Papua New Guinea. With additional financing, the number of potential direct beneficiary households more than doubles, from 24,000 to 60,000; the expected internal rates of financial and economic returns on the project's investment improve; and IFAD can strengthen support to policy development, promote further linkages between smallholder farmers and agribusiness, and strengthen support to farmers' organizations, women and other disadvantaged groups.

7. The PPAP is widely recognized as an innovative and effective model for agricultural development. The provision of additional financing enables IFAD to consolidate its co-leadership of the project after the approval of additional financing for the project from both the World Bank and the European Union. It also enables IFAD to reduce substantially project preparation time and administrative and transaction costs.

III. Details of the scaling up proposal

8. The Government of Papua New Guinea has formally requested the scaling up of the PPAP to support smallholder coffee and cocoa farmers nationally. As envisaged in the original project design, there is demand and opportunity for scaling up the productive partnership model by expanding the number of partnerships, intensifying coverage in existing project provinces, and extending the project's coverage to new areas across the country.

9. The additional financing will enable expansion of the PPAP to all cocoa- and coffee-growing provinces. Partnerships will remain demand-driven and consistent with the priorities identified in each subsector. The first call for proposals under the additional financing (the third overall call for the PPAP) will exclude the original provinces covered by the ongoing project. The next call will be open to all cocoa- and coffee-growing provinces across the country, in line with the established operational procedures for the project.

10. The project will continue to employ a combination of targeting and monitoring strategies aimed at ensuring an equitable distribution of project benefits. It will continue its inclusive targeting approach based on demand-driven partnerships with smallholders. Principal targeting mechanisms will continue to include geographical and commodity-based targeting, enabling and empowering

approaches, and procedural measures to promote the involvement of disadvantaged households and women and the inclusion of remote communities.

11. The additional financing will be fully in line with the original project design and will support the scaling up of the three original project components: (i) institutional strengthening and industry coordination; (ii) productive partnerships; and (iii) market access infrastructure.

12. Efforts under component 1 – institutional strengthening and industry coordination – will seek to improve the performance of sector institutions and enhance industry coordination in the cocoa and coffee sectors. The additional financing will reinforce the capacity of these institutions to coordinate industry activities, and facilitate the sustainability of their operations.

13. The objective under component 2 – productive partnerships – will be to foster the integration of more smallholder producers into well-performing and remunerative value chains by developing and implementing public-private alliances in the project areas, with the aim of improving market linkages. Partnerships will continue to be demand-driven and consistent with the priorities identified in each subsector. This component will maintain the two subcomponents of the original project: (a) productive partnerships in cocoa-growing areas; and (b) productive partnerships in coffee-growing areas.

14. As in the original project, the objective of component 3 – market access infrastructure – will be to improve smallholders' market access in the areas targeted by the project. The two subcomponents will remain unchanged: (a) preparation of market access infrastructure investments; and (b) market access infrastructure development. The expansion of the project into new areas will be expected to increase the demand for infrastructure. A critical element of component 3 is the requirement that subprojects have commitments in place for sustainable maintenance arrangements as an eligibility condition for project funding. With the additional financing, new modalities for securing maintenance funding will be introduced on a pilot basis.

15. The additional financing will be implemented over a five-year period from about September 2014 to 30 June 2019. The longer implementation period provides sufficient time for the completion of critical market access infrastructure under component 3, the completion and consolidation of partnership activities, and sustained support to sector coordination institutions. New partnerships financed by the additional financing will be implemented over a three-year period; project implementation will therefore have to continue for a minimum of three years after the last partnerships are approved. For greater implementation efficiency, the approval of new partnerships will be sequenced, with the last partnerships expected to be approved in 2016 and completed in 2019. An extension of the closing date of the original financing agreement will be required to align it with the new closing date for the additional financing.

IV. Project costs and financing

16. The total project cost is US$119.3 million, of which US$73.0 million is included as additional financing. The additional financing contributors are IFAD US$22.0 million, World Bank US$30 million, European Union US$6.4 million, Government of Papua New Guinea US$4.5 million, and beneficiaries' contributions US$10.1 million. Details are presented in the following tables.

Table 2
Additional financing, by component and financier
(Thousands of United States dollars)

	IFAD loan		World Bank		European Union		Beneficiaries		Borrower/ counterpart		Total	
Expenditure category	*Amount*	*%*	*Amount*	*%*	*Amount*	*%*	*Amount*	*%*	*Amount*	*%*	*Amount*	*%*
1. Institutional strengthening and industry coordination	6 000	27	8 000	26	400	6			1 430	32	15 830	22
2. Productive partnerships	8 700	40	11 900	40	3 600	56	10 100	100	1 050	23	35 350	48
3. Market access infrastructure	7 300	33	10 100	34	2 400	38			2 020	45	21 820	30
Total	**22 000**		**30 000**		**6 400**		**10 100**		**4 500**		**73 000**	

Table 3
Revised total costs, by component
(Thousands of United States dollars)

Component	*Original cost*	*Additional financing*	*Total*
1. Institutional strengthening and industry coordination	9.600	15 400	25 000
2. Productive partnerships	20 100	35 600	55 700
3. Market access infrastructure	16 600	22 000	38 600
Total	**46 300**	**73 000**	**119 300**

Table 4
Additional financing, by expenditure category and financier
(Thousands of United States dollars)

	IFAD loan		World Bank		European Union		Beneficiaries		Borrower/ counterpart		Total
Expenditure category	*Amount*	*%*	*Amount*	*%*	*Amount*	*%*	*Amount*	*%*	*Amount*	*%*	*Amount*
1. Consultancies	4 500	20	6 200	21	-		-		-		10 700
2. Goods, services and inputs	6 700	30	9 200	31	2 300	36	-		1 600	35	19 800
3. Training[1]	2 300	10	3 100	10	500	8	-		1 850	41	7 750
4. Grants and subsidies[2]	8 500	40	11 500	38	3 600	56	10 100	100	1 050	24	34 750
Total	**22 000**		**30 000**		**6 400**		**10 100**		**4 500**		**73 000**

[1] Includes additional operating costs.
[2] Productive partnership grants.

17. As was the case with the original project financing, the IFAD additional financing will be allocated across all project components and will finance a percentage of all project activities. The IFAD loan for additional financing will be extended to the Government of Papua New Guinea on blend financing terms and conditions. An extension of the completion and closing dates of the existing project will be required. The revised project completion date will be 30 June 2019.

V. Financial management

18. Financial management of the ongoing project was rated moderately satisfactory in the latest IFAD internal portfolio review exercise.

19. The overall fiduciary function is outsourced to the World Bank as the cooperating institution responsible for loan administration. Harmonized financial reporting to all donors financing the project will continue. The original financing for PPAP is 28 per cent disbursed, but 70 per cent of the original project loan funds have been committed for approved partnerships and will be disbursed incrementally based on performance. In addition, the infrastructure component, which accounts for 40 per cent of total project financing, has commenced and is expected to reach full

disbursement in late 2014. The financial management arrangements of the original project will continue for the additional financing, and the finance structure will be reinforced with the hiring of additional accountants to manage the increased workload.

VI. Flow of funds and withdrawal applications

20. A new designated account will be opened in a bank acceptable to IFAD, through which the additional financing will be channelled. Management of withdrawal applications (WAs) has improved since the start of the project, when many WAs of minimal value were submitted to IFAD for disbursement. Efficiencies have reduced the number of WAs submitted and increased their value.

VII. Audit

21. The annual financial statements of the project will be audited by the Office of the Auditor General. PPAP audits undertaken in recent years have been assessed as moderately satisfactory.

VIII. Proposed modifications to the project financing agreement

22. Upon the approval of the Executive Board, the project financing agreement will be amended to reflect the additional IFAD financing. Additional financing will be fully aligned with the original design. Activities will be intensified in existing areas and scaled up in the new coffee- and cocoa-growing areas, where new partnerships will be created.

IX. Recommendation

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

> RESOLVED: that the Fund shall make an additional loan to Papua New Guinea on blend terms in an amount equivalent to US$22 million (SDR 14.23 million) upon such terms and conditions as shall be substantially in accordance with the terms and conditions presented herein.

Kanayo F. Nwanze
President