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Investing in rural people

## President's memorandum

Republic of Honduras: Proposed allocation to the Project for Competitiveness and Sustainable Development in the South-Western Border Region (PRO-LENCA) of funds deriving from cancellation of the Horizontes del Norte project

### Note to Executive Board representatives

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For: Approval

## Recommendation for approval

The Executive Board is invited to approve the recommendation for the proposed allocation to PRO-LENCA of funds deriving from the cancellation of loan 839-HN as contained in paragraph 38. The financing will be extended through a loan on blend terms for the amount of approximately SDR 4.51 million.

## President's memorandum

### Proposed allocation to the Project for Competitiveness and Sustainable Development in the South-Western Border Region (PRO-LENCA) of funds deriving from cancellation of the Horizontes del Norte project

#### I. Background and justification

1. The Project for Competitiveness and Sustainable Development in the South-Western Border Region (PRO-LENCA) was approved by the Executive Board through lapse-of-time procedures in September 2013.<sup>1</sup>
2. In 2014 the Government of Honduras decided to replace the United Nations Development Programme (UNDP) Honduras with a newly created government-led project management unit (UAP - Unidad Administradora de Proyectos) within the Ministry of Agriculture and Livestock as the service provider for management of the project's fiduciary aspects.
3. IFAD welcomed this initiative because it offered a more effective institutional arrangement for implementation of the IFAD portfolio in Honduras. IFAD approved and issued the necessary amendment letters to loan agreements to reflect the role and responsibilities of the UAP.
4. At the end of 2014, applying the limits agreed with the International Monetary Fund on the contracting of further external debt, the Government of Honduras carried out a thorough assessment of the approved financing agreements to be implemented in the framework of country development initiatives. This assessment covered not only the IFAD financing but also the Central American Bank for Economic Integration (CABEI) and OPEC Fund for International Development (OFID) cofinancing for the Horizontes del Norte project and PRO-LENCA respectively. The Government decided to maintain both as IFAD-funded projects – in line with the high priority given to poverty reduction in the new Government Plan (2014-2018) and the National Strategy for Food Security and Nutrition (2010-2022) – but not to proceed with formalization of the cofinancing agreements.
5. The Government has renewed its commitment to poverty reduction. In an effort to develop new debt ceilings and a more centralized approach to programme implementation – and in line with IFAD's revised approach to reallocating the cancelled funds of approved loans and grants to existing or new programmes<sup>2</sup> – in March 2015, the Government of Honduras (through the Ministry of Finance, its authorized representative) officially requested IFAD to concentrate financing efforts on PRO-LENCA, cancelling the remaining funds of Horizontes del Norte and allocating them to PRO-LENCA. The overall objectives and approach of PRO-LENCA

<sup>1</sup> EB 2013/LOT/P.7.

<sup>2</sup> EB/2014/111/R.12/Rev.

would remain unchanged. The Ministry of Finance also requested IFAD to initiate the process for realigning the two projects in response to the financing gap that now constrains their original structures. Cofinancing for Horizontes del Norte from CABEL represented 38 per cent of the total project cost, and the planned contribution from OFID was about 42 per cent of the total cost of PRO-LENCA.

6. In light of this request, IFAD and the Government agreed to take the following actions for submitting to the Executive Board a proposal for reallocating funds from Horizontes del Norte to PRO-LENCA:
  - Revise the PRO-LENCA design document to allow the project to absorb the residual IFAD financial resources of the cancelled 839-HN loan balance previously allocated to Horizontes del Norte, for an amount of approximately SDR 4.51 million. The realigned design will allow PRO-LENCA to take up – in addition to its original plan – ongoing activities to which Horizontes del Norte was already committed.
  - In addition, IFAD and the Government are working with the Global Environment Facility (GEF) to allow GEF funds originally assigned to Horizontes del Norte to be reallocated to PRO-LENCA.
7. Based on these reallocations, the external financing to PRO-LENCA is now estimated at US\$23.48 million, compared with the US\$28.79 million of the previous design. This represents an overall reduction of 18 per cent in total financing for the project.

## II. Performance of the IFAD portfolio in Honduras

8. As of 30 June 2015, the level of disbursement of the Honduras portfolio was as follows: Sustainable Rural Development Programme for the Southern Region (EMPRENDESUR) 30 per cent; Project for Enhancing the Rural Economic Competitiveness of Yoro (PROMECOM) 72 per cent; and Horizontes del Norte 17 per cent. PRO-LENCA has not yet started disbursing. In 2014, the disbursement rate was affected by the Government's decision to replace UNDP Honduras with the new UAP within the Ministry of Agriculture and Livestock. Throughout 2014, little progress was made in the implementation of existing projects and in the start-up of PRO-LENCA, which entered into force on 3 March 2014. In September, all external resources available under the three projects were frozen while the Government undertook its assessment.
9. Since its consolidation in 2015, the Ministry of Agriculture and Livestock's UAP has worked intensively on streamlining processes and accelerating implementation of the portfolio. Since July 2015, implementation of the three projects has been under way and new withdrawal applications will be received as implementation progresses.

## III. Progress towards results and impact

10. PROMECOM has made significant progress towards achievement of the development goals set forth in its logical framework. The project is currently running 214 investment plans, 26 business plans, 83 organizational development plans and 105 community management plans, representing 85 per cent of the final goal. It benefits 7,631 families and ensures the participation of youth (16 per cent) and women (35 per cent). Of the business groups involved in the project, 37 per cent currently have access to formal markets or better marketing conditions, 76 per cent apply best environmental practices, and 81 per cent have better infrastructure and productive technology. Improvements in food security have been recorded for 1,603 families, including 1,200 indigenous families of Tolupan ethnicity – well above the original goal. Through implementation of the project's integrated investment plans, 2,306 people have received direct support and tailored management and production training programmes. The work of the project management committee has resulted in improved social infrastructure for many

families through the installation of 1,034 latrines, 914 biomass stoves, 1,062 roofs, 239 water batteries, and 496 silos for storing grain. Investments have favoured vulnerable groups by enabling improved productivity that results in better access to food, employment and services that guarantee better living conditions.

11. EMPRENDESUR has been affected by external factors, which slowed its implementation over the last year. Delays were mainly because the programme was unable to access external resources, including those of CABEI, as explained in paragraph 8. However, the implementation strategies adopted achieved the following results: seven organizations benefited from improved access to markets and financial resources; 4,181 producers received specialized technical assistance; 16 local savings and credit cooperatives were strengthened, resulting in 1,442 people obtaining access to their services; and human capital was enhanced, with 931 people participating in capacity-building programmes and training on the promotion of gender equality and the inclusion of youth organizations, environmental conservation and sustainable management of natural resources, and other themes related to programme development goals. Remarkable results have been achieved through the rehabilitation and maintenance of 90 km of tertiary roads. When the programme could not count on receiving the expected resources, preparatory activities were undertaken.

#### IV. Continued support from the IFAD country office in Guatemala

12. The IFAD country office (ICO) in Guatemala will provide direct support by monitoring and supporting implementation of the Honduras country programme, with the main objective of strengthening the administrative and financial performance of the Ministry of Agriculture and Livestock's UAP and the management units of each project. As part of these implementation support activities, a training programme covering monitoring and evaluation (M&E), youth and human development issues was delivered in mid-July 2015. Tailored guidance tools have been developed for each project, to facilitate execution and implementation. In addition, ongoing dialogue with national counterparts will facilitate the provision of their support in specific areas as required. These measures will result in higher performance and impact.
13. Once PRO-LENCA is realigned, it will have sufficient capacity to expedite implementation and thereby achieve the expected results.

#### V. Rationale for the realigned project

14. The rationale of the project has not changed. The project will continue to focus its strategy on contributing to rural development in an area of Honduras that has not received much attention in recent years and that shows signs of reduced development compared with other areas of the country. PRO-LENCA will also maintain its focus on improving the living standards of rural populations that face higher levels of poverty and have traditionally been excluded from development operations.
15. As one of its basic pillars, the project strategy will continue to promote valuable cultural features and practices of the Lenca ethnicity, most of whom live in the rural areas targeted by the project (the region is called "Lenca Zone" or "Lenca Axis").
16. Based on this strategy, and on the positive experiences of EMPRENDESUR, PRO-LENCA proposes a financing approach based on community demand (community-driven development), with participatory investments that aim to enhance communities' autonomy. This mechanism entails full delegation of the implementation of investment plans to beneficiary organizations.
17. Horizontes del Norte interventions that have already been approved will be implemented through the realigned PRO-LENCA.

## VI. Realigned project description

### A. Project area and target group

18. The PRO-LENCA project area will remain the same as in the project design approved by IFAD in 2013, covering a slightly reduced total area of approximately 6,000 km<sup>2</sup> in the departments of La Paz, Intibucá and Lempira. The only difference is that now it will cover 36 municipalities instead of the 42 previously selected, because of the reduced resources available. Following the realignment, PRO-LENCA will also work in 11 municipalities that were previously covered by Horizontes del Norte and for which there are outstanding commitments with organizations in the departments of Atlántida (four municipalities), Cortés (two) and Santa Barbara (five).
19. The target group for the project has not changed and includes: (i) smallholder farmers with limited access to productive resources and varying degrees of organizational skill and market openness; (ii) rural artisans and their organizations, which are weakly associated with emerging markets; and (iii) rural and small-scale entrepreneurs. The project will pay particular attention to vulnerable groups such as women, youth and indigenous people.
20. The number of direct beneficiaries of the project has been revised to an estimated 11,000 poor rural households (down from 13,500), including 826 rural families in the departments of Atlantida, Cortes and Santa Barbara previously associated with Horizontes del Norte. The number of indirect beneficiaries is now estimated at 22,000 households, compared with the previous target of 31,500.
21. The revised number of total beneficiaries is estimated at 264,000 people (down from 360,000), including 4,130 in the Horizontes del Norte project area.

### B. Development objective and impact indicators

22. The development objective of PRO-LENCA has not changed but has been expanded to integrate possible absorption of the GEF grant for Horizontes del Norte. This development objective is to improve the incomes, employment opportunities, food security and general living conditions of the poor rural population, focusing on social inclusion, gender and vulnerability to climate change, and with a view to reducing poverty and extreme poverty.
23. Project indicators have not changed, but some have been reduced to take into account the decreased resources now available. The impact indicators for the project are as follows:
  - (a) Approximately 11,000 (down from 13,500) families benefit directly from the project, while another 22,000 families benefit indirectly. In total, about 264,000 people (down from 360,000) will be direct and indirect beneficiaries.
  - (b) At least 75 per cent of direct beneficiary families increase their gross family incomes by at least 25 per cent.
  - (c) About 2,200 new jobs (on and off-farm) are created, of which at least 25 per cent are for youth and 25 per cent for women.
  - (d) 50 per cent of the target population that today suffers from food insecurity has sustainable access to safe and nutritious food.
  - (e) Child malnutrition decreases by 10 per cent (from 50 to 40 per cent) in the project area.
  - (f) At least 75 per cent of beneficiary rural families increase their physical assets by 20 per cent.

### C. Outcomes/components

24. The project components have not changed:

- (a) Component 1: Development and strengthening of rural organizations. The objective of this component is to develop and strengthen the organizations of the rural poor, enhancing the human capital of their members. Activities will include implementation of plans for organizational strengthening, to enhance the organizations' internal governance structures and administrative procedures; basic capacity building in sustainable production; and commercialization and access to rural financial services.
  - (b) Component 2: Productive and business development. The objective of this component is to strengthen and consolidate beneficiary organizations while transforming them into self-sustaining and competitive units that are able to respond to market requirements. The component also aims to produce tangible socio-economic and environmental benefits for the organizations and their communities, including by providing funds directly to the beneficiary organizations. The project will make both productive development plans and business plans available – these mechanisms have not been changed.
  - (c) Component 3: Improvement of rural infrastructure and management of natural resources. The main objective of this component is to offer poor rural families – especially beneficiaries of the development plans implemented under component 2 – better infrastructure to support production and access to markets. The component also seeks to improve natural resource management and adaptation to climate variability to ensure the sustainability of production and incomes and improve resilience in case of natural disasters.
  - (d) Component 4: Project management and coordination. This component includes all activities related to the coordination of project activities.
25. Activities associated with Horizontes del Norte have been integrated into component 2 and consist of developing 18 business plans for municipalities in the departments of Atlantis, Cortés and Santa Barbara: 16 business plans and 2 productive development plans.
26. At the end of this document a comparative logical framework illustrates the changes in objectives, activities, key performance indicators and means of verification of the revised design document.

## VII. Realigned project implementation

### A. Organizational framework

27. The description of project implementation activities has been updated to reflect recent changes at the Ministry of Agriculture and Livestock. These changes are mainly in response to changes that occurred in 2014 following the Government's decision to redefine its role in the execution of externally financed projects in the agriculture development sector.
28. Before 2014, the financing agreements of all IFAD projects in Honduras included provisions for supporting the administration of funds and the procurement of goods and services by UNDP, which supported IFAD-funded projects in activities related to financial management.
29. In March 2014, the Government of Honduras requested IFAD formally to amend all its financing agreements, replacing the services provided by UNDP Honduras with management by the newly created UAP in the Ministry of Agriculture and Livestock.
30. The request was the result of a sovereign decision taken by the Government after an analysis of the cost-effectiveness of internalizing the management of activities carried out by UNDP Honduras. The Government informed IFAD of its intention to create the UAP to cover the tasks previously handled by UNDP as a way of reducing costs and gaining efficiencies in the management of project activities, while strengthening institutional capacities at the government level.

31. The Ministry of Agriculture and Livestock's UAP is now the executing unit within the Government dealing with the implementation of PRO-LENCA and all other IFAD-funded projects. Its duties and functions are to:
- (a) Ensure that all financial management arrangements are in place and implemented for all projects under its execution;
  - (b) Coordinate the preparation of annual work plans and budgets and procurement plans with PMUs;
  - (c) Prepare project financial statements at the end of each fiscal year, with support from PMUs;
  - (d) Coordinate the necessary activities for the submission to IFAD of consolidated annual audit reports within six months of the end of the fiscal year;
  - (e) Plan, coordinate and monitor activities related to project procurement;
  - (f) Coordinate project implementation activities together with the PMU; and
  - (g) Coordinate the M&E and knowledge management of all projects executed in the Ministry of Agriculture and Livestock, together with PMUs and the Ministry's Project Planning, Evaluation and Management.
32. These changes to project management have already been included in the PRO-LENCA financing agreement.
33. The project will now have one central and two regional offices, rather than the one central and three regional offices originally planned. This decrease is a result of the reduction in available budget and subsequent cost-savings efforts.

## VIII. Realigned project costs and financing

34. The revised total project cost is now estimated at US\$27.8 million for a period of six years. The previous total cost was US\$34.1 million, meaning a reduction of about 18 per cent of the total cost. Considering the lag in project implementation, the Government of Honduras has already requested a two-year extension in the implementation period.
35. IFAD will finance 74 per cent of the total revised cost through existing loan 899-HN, for an amount of approximately US\$14.3 million, and a new loan financed with the residual resources coming from Horizontes del Norte, for an amount of approximately US\$6.2 million. The GEF grant previously associated with Horizonte del Norte will contribute an additional US\$3.0 million to the financing available for the revised PRO-LENCA – 11 per cent of the total cost. These investments aim to help fill the financial gap caused by the Government's restriction on contracting the planned funding by OFID, for an amount of US\$14.5 million.
36. The remaining cost will be covered by the Government, accounting for 4 per cent or US\$1.1 million in the form of tax exoneration (down from US\$1.3 million), and the beneficiaries, accounting for 12 per cent or US\$3.2 million in kind or as contributions to the financing of investment plans (down from US\$4.0 million). Tables 1 and 2 detail the new indicative project costs by category of expenditure and financier.
37. The IFAD loan from the cancellation of loan 839-HN represents new financing to the Government of Honduras for PRO-LENCA, and will bear different loan terms. Loan 839-HN (Horizontes del Norte) was approved at highly concessional terms, while the new loan for PRO-LENCA will bear blend terms. This change takes into account the country's graduation (2013) in its IFAD lending terms, in line with the World Bank.

Table 1  
**Indicative project costs by component and financier**  
 (Thousands of United States dollars)

	<i>IFAD loan 899-HN</i>		<i>IFAD new loan</i>		<i>GEF</i>		<i>Government of Honduras</i>		<i>Beneficiaries</i>		<i>Total</i>	
	<i>Amount</i>	<i>%</i>	<i>Amount</i>	<i>%</i>	<i>Amount</i>	<i>%</i>	<i>Amount</i>	<i>%</i>	<i>Amount</i>	<i>%</i>	<i>Amount</i>	<i>%</i>
1. Development and strengthening of rural organizations	3 010	73	-	-	734	18	356	9	-	-	4 100	15
2. Productive and business development	7 832	53	2 221	15	2 116	14	51	-	2 485	17	14 705	53
3. Improvement of rural infrastructure and management of natural resources	667	11	3 847	66	-	-	594	10	743	13	5 851	21
4. Project management and coordination	2 783	87	124	4	151	5	129	4	-	-	3 187	11
<b>Total project costs</b>	<b>14 293</b>	<b>51</b>	<b>6 192</b>	<b>22</b>	<b>3 000</b>	<b>11</b>	<b>1 130</b>	<b>4</b>	<b>3 228</b>	<b>12</b>	<b>27 843</b>	<b>100</b>

Table 2  
**Indicative project costs by category of expenditure and financier**  
 (Thousands of United States dollars)

	<i>IFAD loan 899-HN</i>		<i>IFAD new loan</i>		<i>GEF</i>		<i>Government of Honduras</i>		<i>Beneficiaries</i>		<i>Total</i>	
	<i>Amount</i>	<i>%</i>	<i>Amount</i>	<i>%</i>	<i>Amount</i>	<i>%</i>	<i>Amount</i>	<i>%</i>	<i>Amount</i>	<i>%</i>	<i>Amount</i>	<i>%</i>
1. Rural infrastructure (works)	-	-	3 847	74	-	-	577	11	743	14	5 167	19
2. Vehicles and equipment	835	76	-	-	92	8	172	16	-	-	1 099	4
3. Investments in business plans (grants)	3 745	62	824	14	-	-	-	-	1 520	25	6 089	22
4. Investments in productive development plans (grants)	3 234	63	1 397	27	-	-	-	-	515	10	5 147	18
5. Investments for climate change adaptation (grants)	-	-	-	-	1 902	81	-	-	450	19	2 352	8
6. Training, technical assistance and service contracts (including for climate change under GEF)	3 997	78	-	-	863	17	294	6	-	-	5 154	19
7. Salaries	1 895	94	124	6	-	-	-	-	-	-	2 019	7
8. Operating costs	586	72	-	-	144	18	87	11	-	-	817	3
<b>Total project costs</b>	<b>14 293</b>	<b>51</b>	<b>6 192</b>	<b>22</b>	<b>3 000</b>	<b>11</b>	<b>1 130</b>	<b>4</b>	<b>3 228</b>	<b>12</b>	<b>27 843</b>	<b>100</b>

## IX. Recommendation

38. I recommend that the Executive Board approve the proposed allocation of funds deriving from the cancellation of loan 839-HN (Horizontes del Norte) to the PRO-LENCA project, and the realignment scheme of PRO-LENCA in terms of the following resolutions:

RESOLVED: that the Fund shall approve the allocation of cancelled funds of loan 839-HN to PRO-LENCA. This financing will be provided in the form of a loan on blend terms for the amount of approximately SDR 4.51 million to the Republic of Honduras and upon such terms and conditions as shall be substantially in accordance with the terms and conditions presented herein;



RESOLVED: that the Fund shall approve the realigned design of PRO-LENCA and upon such terms and conditions as shall be substantially in accordance with the terms and conditions presented herein.

Kanayo F. Nwanze  
President