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Investing in rural people

President's memorandum

Proposed additional loan to the Republic of Senegal for the Agricultural Value Chains Support Project (PAFA)

Note to Executive Board representatives

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For: Approval

Recommendation for approval

The Executive Board is requested to approve the recommendation for the proposed loan to the Republic of Senegal for the Agricultural Value Chains Support Project (PAFA) as contained in paragraph 20.

President's memorandum

Proposed additional loan to the Republic of Senegal for the Agricultural Value Chains Support Project (PAFA)

I. Context and justification

1. The development objective of the Agricultural Value Chains Support Project (PAFA) is to improve sustainably the incomes and livelihood systems of smallholders in the Senegal groundnut basin through their assimilation into profitable and diversified value chains. PAFA was approved by the Executive Board in September 2008 (EB 2008/94/R.13/Rev.1) for a six-year duration and became effective on 2 February 2010. Initial completion and closing dates are 31 March and 30 September 2016, respectively. The project covers parts of the regions of Kaolack, Diourbel, Fatick and Kaffrine.

2. The total cost of PAFA was estimated at US$36.61 million. The project is cofinanced by an IFAD loan of SDR 9.1 million, a grant of SDR 0.17, a Global Environment Facility (GEF) grant of US$5.0 million, an OPEC Fund for International Development loan equivalent to US$9.1 million, a contribution from the borrower of US$5.75 million, and a contribution from beneficiaries of US$1.68 million.

II. Status of project implementation

3. PAFA has been rated as "highly satisfactory" by successive supervision missions and the midterm review mission that took place in August to October 2014. After four years of implementation, PAFA has reached 25,400 households directly, representing 181 per cent of the targeted 14,000 households. The 2013-2014 portfolio review rated the fiduciary management of PAFA as "satisfactory" and determined that the project was compliant with legal covenants and that the submission of audit reports was timely and satisfactory to IFAD.

4. PAFA has achieved substantial results in terms of increased yields, food security, income generation and job creation. Production and productivity along the targeted value chains (millet/sorghum, cowpeas, sesame, maize, village poultry and hibiscus) have more than doubled. The average hungry period for households supported by the project has declined from six months to one month. The quantity of surplus millet marketed has grown from effectively nil at project start to 1-1.5 tonnes per household. The per-hectare gross margin of each targeted crop has increased by at least 390 per cent and up to 1,875 per cent. With this strong performance embedded in formal value chains using negotiated prices, smallholders now have increased income and capacity to self-finance.

5. It is highly likely that the achieved results will be sustainable, and PAFA is on track regarding its exit strategy. Sustainability is supported by the competencies acquired through the course of the project by smallholders, their farmers' organizations (FOs) and market operators. These competencies include: (i) producers saving to purchase inputs; (ii) clear and functional partnering arrangements with established institutions; (iii) effective contract farming arrangements among smallholders, FOs and market operators for the production and sales of commodities; (iv) graduation of 120 FOs from PAFA's declining input subsidy programme to self-financing for inputs; and (v) FOs taking responsibility for hiring and paying village-level technicians for assistance.

6. One of the main factors for success of the project is the contractual arrangement between FOs and market operators, which ensures a guaranteed market for the sale of smallholder producers' production at negotiated remunerative prices. Many market operators are local small and medium-sized enterprises/agricultural processors (SMEs) established in the regions of Kaolack, Diourbel, Fatick, Kaffrine, Thies and Dakar. These SMEs continue to face a number of constraints, including: (i) insufficient organization; (ii) old and weak equipment; (iii) weak technical and managerial capacity; (iv) lack of standardized packaging; and (v) poor product branding and marketing.

7. In spite of tangible progress in formalizing and commercializing PAFA's value chains, SME processing remains a serious bottleneck in the project's achievement of its potential. All value chain actors participating in the five value chain forums agree that processing capacity must be expanded to provide a proper market for smallholder production and thus to support income growth for all parties. The low capacity of SME processors is exacerbated by their limited access to appropriate finance as existing commercial financing requires tangible collateral, has rigid repayment schedules inappropriate to the seasonality of agricultural businesses and charges interest rates that are difficult for the SMEs to sustain.

8. PAFA is becoming a victim of its own success as smallholders continually augment their production and productivity while SMEs' processing capacity fails to keep pace, despite project activities to support the processing segment of the value chains. For the SMEs to increase their capacity to buy smallholder production, constraints to their operations must be tackled.

9. Additional financing to PAFA will support the project in addressing constraints faced by the SME processors, in particular: (i) technical and managerial capacity; (ii) enhancing value addition and output quality; and (iii) promoting the consumption and retailing of smallholders' crops through specialized local produce restaurants and other channels. The funding will also support processors' cooperatives, FOs and public institutions in continuing to improve the delivery of services to their members and constituents.

III. Project costs and financing

10. The additional financing amounts to SDR 650,000 (approximately US$900,000), in the form of a loan on highly concessional terms.

11. Distribution of costs by expenditure category is shown in the table below.

Table
PAFA additional funding by expenditure category
(United States dollars)

Category	*New IFAD loan amount*	*Percentage*
Equipment and vehicles	440 000	48.9
Technical assistance, studies and training	160 000	17.8
Service provider contracts	300 000	33.3
Total	**900 000**	**100**

IV. Financial management, procurement and governance

12. Country context and risk rating. The financial management arrangements for the proposed additional financing will be aligned with those of the ongoing PAFA, which have been found fully adequate by supervision missions and audits. The financial management risk of PAFA, assessed in accordance with IFAD guidelines, is deemed low.

13. Financial management. Responsibility for financial management of the additional funding will rest with the ministry in charge of finance. A full set of accounts will be

maintained in line with IFAD’s requirements and internationally recognized accounting standards. The interim financial reports and annual project financial statements prepared by the programme coordination unit for PAFA will include the additional funding, identified separately. Financial management arrangements are detailed in a financial procedures manual, which will be updated to integrate the additional funding, with the revised version submitted to IFAD for approval.

14. Accounts. The additional funding will be transferred by IFAD to a designated account managed by the ministry in charge of finance at a bank in Dakar that is acceptable to IFAD and in accordance with IFAD’s disbursement procedures. Funds will be transferred to PAFA’s operational account in Kaolack for project implementation.

15. External audit arrangements. The project will be audited annually by independent auditors acceptable to IFAD under terms of reference approved by IFAD and in line with the IFAD Guidelines on Project Audits. An audited, consolidated financial statement for the entire project, together with the required management letter, will be submitted to IFAD within six months of the end of each fiscal year.

V. Proposed amendments to the financing agreement

16. Once approved by the Executive Board, the financing agreement will be amended to take into account the additional IFAD financing. No new expenditure category will be created. This financing completes the financing plan initially approved with the project design and will not involve changes to the project description, project area or target group. The Government will cover tax related to the expenditure envisaged with the additional funding, in the form of exemption and/or cash, as required.

VI. Legal instruments and authority

17. An amendment to the current financing agreement between the Republic of Senegal and IFAD will constitute the legal instrument for extending the proposed additional financing to the borrower/recipient.

18. The Republic of Senegal is empowered under its laws to receive financing from IFAD.

19. I am satisfied that the proposed IFAD additional financing will comply with the agreement establishing IFAD and with the policies and criteria for IFAD financing.

VII. Recommendation

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

> RESOLVED: that IFAD shall provide a loan on highly concessional terms to the Republic of Senegal in an amount equivalent to six hundred and fifty thousand special drawing rights (SDR 650,000) (approximately US$900,000), and upon such terms and conditions as shall be substantially in accordance with the terms and conditions presented herein.

Kanayo F. Nwanze
President