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IFAD
Investing in rural people

President's report

Proposed loan to the Republic of Azerbaijan for the Livestock Productivity and Marketing Improvement Programme

Note to Executive Board representatives

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For: **Approval**

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Appendices

Abbreviations and acronyms

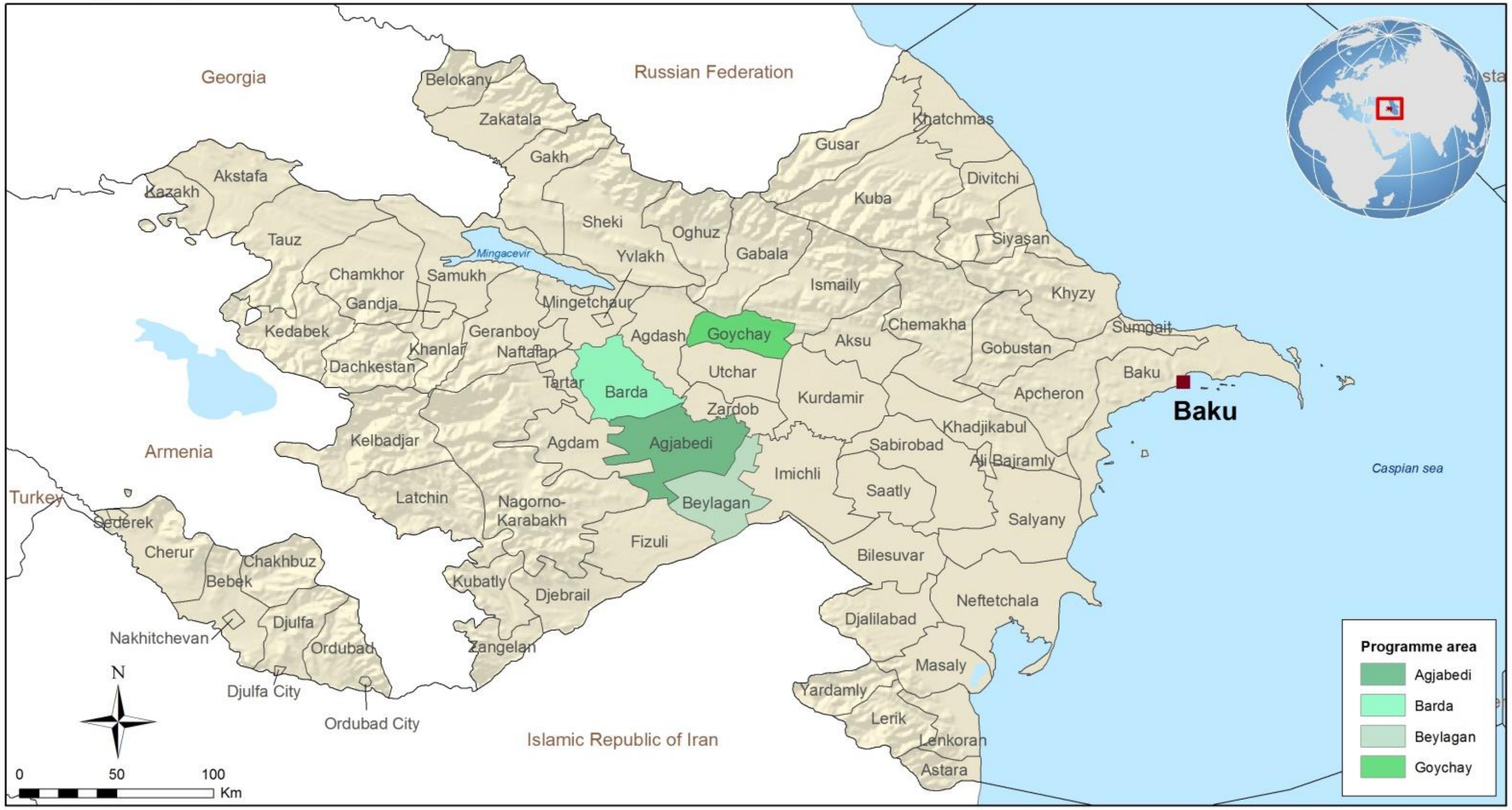
CIG	common interest group
LPMIP	Livestock Productivity and Marketing Improvement Programme
M&E	monitoring and evaluation
MoA	Ministry of Agriculture
MSMP	multistakeholder marketing platform
PBAS	performance-based allocation system
PMU	programme management unit
PRST	programme regional support team
RIMS	Results and Impact Management System
RWG	*rayon*-level working groups

Map of the programme area

The Republic of Azerbaijan

Livestock Productivity and Marketing Improvement Programme

Project design



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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 | 12-05-2015

Republic of Azerbaijan

Livestock Productivity and Marketing Improvement Programme

Financing summary

Initiating institution:	IFAD
Borrower:	Republic of Azerbaijan
Executing agency:	Ministry of Agriculture
Total programme cost:	US$32.5 million
Amount of IFAD loan:	US$10 million
Terms of IFAD loan:	Ordinary: Maturity period of 18 years, including a grace period of 3 years, with an interest rate per annum equal to 100 per cent of the IFAD reference interest rate
Financing gap:	US$16.2 million.
Contribution of borrower:	US$4.7 million (US$2.2 million in phase 1 and US$2.5 million in phase 2)
Contribution of beneficiaries:	US$1.6 million (US$1.1 million in phase 1 and US$0.5 million in phase 2)
Appraising institution:	IFAD
Cooperating institution:	Directly supervised by IFAD

Recommendation for approval

The Executive Board is invited to approve the recommendation for the proposed loan to the Republic of Azerbaijan for the Livestock Productivity and Marketing Improvement Programme, as contained in paragraph 60.

Proposed loan to the Republic of Azerbaijan for the Livestock Productivity and Marketing Improvement Programme

I. Strategic context and rationale

A. Country and rural development and poverty context

1. **Socio-economic background**. Azerbaijan is an upper-middle-income country located in the southern Caucasus, with a population of approximately 9.5 million. The country covers about 87,000 km^2, with 47 per cent of the people living in rural municipalities. About 46 per cent of the population is employed, with 39 per cent working in agriculture and agroprocessing. Azerbaijan's GDP was US$37.8 billion in 2016 (World Bank report) and the per capita gross national income was estimated at US$4,760 in 2016.[1] Domestic growth, averaging 14.4 per cent per year from 2000 to 2009, combined with Government of Azerbaijan poverty alleviation programmes, led to sharp decreases in national poverty levels to about 5.6 per cent by 2013. However, GDP growth reached only -3 per cent in 2016, owing to falling oil prices. Statistics show significant disparities exist between rural and urban areas and across regions and social groups, with the depth of poverty greater in rural areas.

2. The oil and gas sectors that have been fuelling economic growth employ only a tiny fraction of the population. Agriculture generates two fifths of rural household income, but has low levels of productivity and accounts for only 6 per cent of GDP (2016), which highlights the relative poverty within the sector. An estimated 850,000 rural smallholder households produce more than 90 per cent of agricultural output. Most farmers now have fragmented landholdings (1-3 hectares [ha]) and from 3 to 10 head of livestock, and are constrained in achieving production economies of scale, accessing support services and marketing their limited output.

3. Agriculture. Rangeland, arable land and pasture comprise about 4.77 million ha and formerly were predominantly fertile, with a reasonable productive potential, particularly in the lowlands. Although the agroclimatic conditions suit a variety of crops, the cropping pattern countrywide is dominated by wheat, barley and forage for animals. More than three quarters of the cropped area was developed for irrigation prior to the 1990s; however, a substantial proportion of the irrigation and drainage systems fell into disrepair after independence, greatly reducing smallholder production.

4. Changes in climate and their impact on Azerbaijan agricultural systems and the rural economy are evident and confirmed by recent studies. Increased temperatures (+2.40 degrees Celsius by 2050), changes in rainfall (-20 per cent by 2050) and rain intensity, together with the shift from a planned to a market

[1] World Bank, *World Development Indicators* (Washington, DC, 2016).

economy, are magnifying existing challenges to the agriculture sector and farmers' management practices.

5. Traditionally, rural households depend on livestock for food, cash and as a stock of wealth. This makes livestock an important element in farming systems, particularly for the large number of small, privately-owned mixed farms. An estimated 2.5 million cattle and 8 million sheep and goats are managed, and poultry is an important cash earner for women and the general household.

B. Rationale and alignment with government priorities

6. To sustain growth, Azerbaijan's acknowledged main challenge and priority is to diversify its economy, introduce market-based policies and strengthen public services, with the overall goal of reducing economic dependence on the oil sector. The Government is in the process of implementing significant reforms in agriculture and rural development that present opportunities for IFAD to engage in a new generation of projects.

7. The Azerbaijan livestock production system currently generates only half of what it could produce. Small-scale livestock farmers are having difficulty feeding their livestock because of reduced fodder production and availability of grazing. This leads to suboptimally fed animals, which are more prone to disease and produce far below their potential, especially in terms of milk yield and calving rate. To offset low animal productivity, farmers have resorted to keeping more underfed animals. This is creating an unsustainable economic and environmental situation in the livestock sector.

8. Azerbaijan is currently importing a significant amount of meat and dairy products, even though livestock numbers have increased since the breakup of the Soviet bloc. Local production is failing to satisfy increasing demand for meat and dairy products, especially that of urban consumers for higher-quality products. The Government wants to encourage new initiatives to upgrade and demonstrate improved technical productivity, leading to increased smallholder incomes in the traditional livestock sector.

9. The sector has a high economic and job creation multiplier effect, because most rural families are involved in livestock production and marketing. The cross-gender nature of these activities provides income opportunities for women and youth. There is strong market demand for quality livestock products that could be produced by traditional livestock herders/farmers using improved management practices. The programme will address these challenges by assisting farmers in introducing better livestock management and commercial practices. This will help farmers produce and market more and better-quality products and take advantage of the evident import substitution opportunities, which will absorb increased production and reward improved quality. Support for the programme will offer major opportunities for increasing rural incomes for IFAD's target group. At the same time, mainstreaming climate resilience interventions in programme investments and stakeholder capacity development will reduce smallholder farmers' vulnerability to climate shocks.

II. Programme description

A. Programme area and target group

10. The Livestock Productivity and Marketing Improvement Programme (LPMIP) is designed to support the IFAD target group of poor farmers in Agjabedi, Barda, Beylagan and Goychay *rayons* (districts), where 22 per cent of Azerbaijan's poor live. The total rural population of the identified target districts is estimated at 335,546 individuals in 79,198 households. Livestock is the main cash earner for these farmers, while backyard vegetable plots provide family nutrition and, occasionally, marketable products.

11. The programme will target about 20,500 smallholder livestock-producing households in about 140 rural settlements. Within the LPMIP *rayons*, the programme will initially emphasize areas assessed by the land capability assessment as having degraded soils. The LPMIP primary target group will be smallholder livestock farmers for whom livestock is a source of income, food security and a social security safety net. Within this group, the programme will target poor smallholder farmers, the poorest woman-headed households and youth.

12. Poultry value chain activities will target 1,800 of the poorest households headed by women for transfer of assets in the form of 1,200 poultry packages and 600 start-up packages for alfalfa forage production. Women will work in groups to facilitate training and to provide mutual support.

13. The programme will encourage participation by commercially oriented smallholder farmers in group activities. There will be a strong focus on rural women – a priority for IFAD support, owing to their critical role in livestock production – and on their social and economic responsibilities and their vulnerable position in society. The programme will also work with about 70 small-scale milk and dairy traders and processors and livestock traders, who are actors in the market linkages of the primary target group.

14. Youth in rural areas are involved in agriculture and livestock, given that their families are engaged in these activities and off-farm employment opportunities are restricted. In addition to the young livestock farmers that are invited into village livestock common interest group (CIG) activities, the programme plans to engage with young women and men graduates of the Ganja Agricultural University by building their capacities and interest in making a career in or starting a livestock business.

B. Programme development objective

15. The overall programme goal is to contribute to reducing rural poverty (increased incomes and reduced vulnerability of poor rural households) by supporting the Government’s economic diversification programme.

16. The development objective is to increase smallholder farmers’ incomes from improved livestock production and marketing activities in the programme *rayons*, together with strengthened resilience to climate shocks.

17. The programme uses a market-led, demand-driven, private-sector development strategy engaging the value chains linking smallholder livestock farmers and local-level marketing groups with larger meat and milk market chains serving urban consumers. This should lead to higher farm incomes for livestock farmers and reduced rural poverty. The programme aligns with other government programmes to improve food security and reduce rural poverty.

18. Given the high vulnerability to climate change, LPMIP will mainstream a climate-smart approach throughout its activities. Climate resilience will be increased by rehabilitation and limited upgrading of existing irrigation and drainage systems and pasture – linked to improved management of pasture, fodder and livestock to improve productivity and flexibility.

C. Components/outcomes

19. LPMIP activities will be organized in two mutually supportive components to develop solutions that will help upgrade the whole livestock value chain from production to processing and marketing. Programme activities will be coordinated under the programme management component.

Component 1. Market-led sustainable livestock production

20. **Outcome 1. Livestock productivity improvements sustainably increased with climate resilience**. Two outputs will increase livestock production and improve productivity.

21. **Output 1.1. Livestock productivity improvements implemented**. This group of activities will develop the "soft" capacity of farmer groups to contribute to preparation of community-level village development and climate vulnerability plans to guide and prioritize investments in pastures and public infrastructure (irrigation, drainage and soil rehabilitation) so as to improve farmer access to livestock feed. In one *rayon*, possibly Agjabedi, a pilot activity will be undertaken to demonstrate that development of a *rayon*-level land management plan can guide targeting and design of village-level natural resource management and productive investment activities.

22. **Output 1.2. Climate-resilient productive infrastructure used**. To support the improvements in livestock production, the programme will fund community investments in advanced irrigation, drainage and land rehabilitation (with some upgrading in identified critical parts) for forage production and pasture rehabilitation, natural seed banks and adoption of climate-resilient practices and technologies.

23. To complement the investments, programme funds will be used to support demonstration, early adoption and innovative activities such as improved in-field water management, improved animal housing, upgraded stock water supplies and improved fodder conservation techniques. Funding will be provided for pilot demonstrations of establishing pastures on the small areas of suitable common grazing land remaining in some villages. Households can also improve additional alfalfa, silage or feed-storage areas, buying simple feed processing gear or installing equipment – using matching grants – to improve milk hygiene and quality.

24. After initial, smaller matching-grant-supported activities, the programme will support some individual farmers and CIGs in developing investment and business proposals for loans from the commercial banking sector.

25. The poorest woman-headed households will have access to start-up packages for poultry and for alfalfa forage production to provide an initial boost towards sustainable poultry or livestock production.

Component 2. Increased return from livestock products

26. **Outcome 2. Smallholder livestock producers receive higher product prices and returns from Azeri markets and consumers**. Two outputs will support value chain development and facilitate market linkages.

27. **Output 2.1. Improved livestock market-chain processes functioning**. In addition to local and *rayon*-level traders, small-scale processors and *rayon* market participants, individual farmers and farmers' groups (that have graduated from production-oriented capacity-building activities or are deemed market-ready) will be offered the opportunity to develop their capacity in market-chain-related product quality improvement, business and financial planning and management. To help farmer and value chain stakeholders develop a shared understanding of market needs, and to ensure that planned investments to improve product quality and/or market access are appropriate, multistakeholder marketing platforms (MSMPs) will be brokered by service providers for the main value chains. These will be formed in each *rayon* to address constraints in local market chains. A priority MSMP activity will be to link smallholder producers to existing large-scale production and processing facilities in or near the programme *rayons* to provide assured higher price outlets for aggregated higher-quality milk, meat and poultry.

28. **Output 2.2. Investments made in livestock market-chain improvement**. Aggregation, processing and marketing opportunities identified by MSMPs will be developed through market stakeholders' own resources, supplemented by programme grants for developing business plans and/or building the capacity of the MSMPS to assess and develop proposals. The matching grants will fund demonstration innovations or early adoption of small initiatives to improve raw product quality, facilitate aggregation and delivery to markets or processors, upgrade small-scale processing activities and other incremental improvements in market chains.

Component 3. Programme management

29. In addition to programme coordination, implementation management and monitoring and evaluation (M&E), this component will include activities to facilitate increased access to financial services and policy dialogue.

III. Programme implementation

A. Approach

30. The programme will be implemented over eight fiscal years – 2018-2025 – and is part of a phased, programmatic approach over two performance-based allocation system (PBAS) cycles. The programme will build on ongoing IFAD-supported country operations, with some refinements in coordination and management mechanisms and the use of service providers to enable effective delivery of agribusiness elements. The refinements include: (i) integration of agribusiness competence into IFAD's programme management unit (PMU) through a field-based programme regional support team (PRST) based in the programme area; (ii) incorporation of contract management procedures in the PRST; (iii) provision for collaboration with various financial institutions and operators in the dairy and red meat industries and with NGOs; and (iv) use of private service providers and implementation partners for field-level activities.

B. Organizational framework

31. Institutional responsibility for management and implementation of LPMIP at the central level will rest with the State Service for Management of Agricultural Project and Credits under the Ministry of Agriculture (MoA), which is currently responsible for all major agriculture- and livestock sector development projects. As with past IFAD-financed projects, a programme steering committee will provide strategic and policy advice and guidance and will be appointed by decree of the Minister for Agriculture. At the working level, more focused *rayon*-level working groups (RWGs) will be established to link programme activities with the *rayon* executive committees and to approve grant proposals.

32. Coordination, monitoring and oversight will be the responsibility of a smaller PMU under the authority of the MoA. The PMU will handle all financial and administrative matters such as M&E, disbursement, procurement, accounts, audits, etc. Currently, the PMU is responsible for implementing the IFAD-funded Integrated Rural Development Project.

33. The PRST will be established and located in Agjabedi to facilitate implementation of programme activities at the *rayon* level through a continuous process of technical backstopping, implementation support and progress reporting. It will be resourced with a team leader, a community infrastructure engineer, and specialists in M&E, community development, gender and rural finance. One *rayon* coordinator will be recruited in each of the other three targeted *rayons* to coordinate and monitor programme activities and supervise service contracts.

C. Planning, monitoring and evaluation, and learning and knowledge management

34. The annual workplan and budget will guide programme implementation and provide a set of benchmarks against which programme performance can be measured each year. The PMU will consolidate the programme's quantitative financial and physical output data in the management information system.

35. The LPMIP will have a comprehensive M&E system to generate all information needed for managing programme activities. An M&E specialist will be part of the PRST to manage M&E activities at the regional level. Three *rayon* coordinators will be based at the *rayon* level to strengthen M&E capacity for village-level demand-driven activities. The Results and Impact Management System (RIMS) will be fully incorporated in the programme M&E system.

36. Continuous learning and knowledge management will be fully integrated into the LPMIP and mainstreamed in implementation at all levels. Knowledge products on programme information, experiences and results will be compiled and disseminated on an ongoing basis. Learning notes will be developed at the village/*rayon* level documenting innovative models, best practices and lessons learned. Knowledge management activities will also provide the detailed information needed for the policy dialogue process – to promote a more supportive policy framework for livestock development.

D. Financial management, procurement and governance

37. **Risk assessment and financial management arrangements**. The inherent risk is assessed as high. As a result, the programme will largely follow the same stand-alone financial management arrangements already established under the ongoing IFAD project, reducing the risk to medium. In this regard, the PMU will: (i) appoint a qualified finance manager and a programme accountant; (ii) record all programme transactions in a customized accounting software in accordance with the cash-basis accounting of the International Public Sector Accounting Standards; and (iii) prepare periodic financial reports in formats agreed with IFAD. In addition, the PMU will maintain a designated account in United States dollars for the IFAD loan and an operating account in Azerbaijani *manats* in a commercial bank to receive financing from the designated account, as well as a separate counterpart account for the Government's contribution. IFAD financing will be disbursed against duly certified withdrawal applications in accordance with IFAD disbursement procedures, to be specified further in the programme implementation manual. Moreover, the programme's consolidated financial statements will be audited annually by an independent audit firm, in accordance with Internal Standards on Auditing and the IFAD Guidelines on Project Audits. The audit report, together with the management letter, will be submitted to IFAD within six months of the end of the fiscal year.

38. **Procurement**. IFAD procurement guidelines will be followed for all types of procurement to be funded from IFAD loan proceeds. For procurement of goods, works and services to be financed with government contributions, the laws of the Republic of Azerbaijan on public procurement provisions will apply.

39. **Governance and financial management risks**. The inherent risk is rated as high, although notable improvements have been made in the country's public financial management systems, as documented in the Public Expenditure and Financial Accountability report published in December 2014 (World Bank). LPMIP has been designed with measures to enhance governance: involvement of farmers and private-sector stakeholders in the selection of investments; review of grant applications; and decentralized RWGs to oversee programme activities. IFAD's policy on preventing fraud and corruption in its activities and operations will be applied to all programme activities.

E. Supervision

40. IFAD can make a constructive contribution to the programme's success by providing close, timely technical supervision for the implementing agencies at critical times during the programme implementation period. The IFAD team, supported by subject matter specialists in partnership with the Government, will participate in annual supervision missions to supervise and provide implementation support to the programme. As part of these missions, a financial management specialist will follow up on identified risks and support mitigation actions.

41. Supervision missions will take into account the risks identified during programme design. RWGs will also have an important supervisory role. IFAD will take a systematic approach to providing missions with the required technical expertise to address emerging issues and will hold periodic implementation review workshops starting from programme year 2.

IV. Programme costs, financing and benefits

A. Programme costs

42. The total estimated cost of the programme over eight years is US$32.52 million, including: (i) market-led sustainable livestock production (80 per cent of costs); (ii) increased return from livestock products (12 per cent); and (iii) programme management (8 per cent).

Table 1
Programme costs by component and financier
(Thousands of United States dollars)

	IFAD loan	*Financing gap 1*	*Financing gap 2*	*Borrower phase 1*	*Borrower phase 2*	*Beneficiaries phase 1*	*Beneficiaries phase 2*	*Total*
Component	*Amount*	*Amount*	*Amount*	*Amount*	*Amount*	*Amount*	*Amount*	*Amount*
1. Market-led sustainable livestock production	8 118	1 664	11 141	1 906	2 249	684	225	25 987
2. Increased return from livestock products	841	393	1 440	248	260	452	268	3 903
3 Programme management	1 041	21	1 503	64	-	-	-	2 630
Total	**10 000**	**2 079**	**14 084**	**2 219**	**2 509**	**1 136**	**493**	**32 520**

B. Programme financing

43. The programme cost of US$32.5 million is expected to be mobilized from two IFAD loans, government budget allocations, beneficiary contributions, participating banks and further cofinancing or IFAD financing. The first IFAD loan of US$10.0 million will be allocated to phase 1 of LPMIP, absorbing the entire 2016-2018 PBAS allocation over the first four years. The financing gap of US$16.2 million may be sourced by subsequent PBAS cycles (under financing terms to be determined and subject to internal procedures and subsequent Executive Board approval) or by cofinancing identified during implementation. As such, it is expected that total external financing for the two phases, including IFAD, will be US$26.2 million, representing 81 per cent of total costs. The Government will fund the balance of US$4.7 million (US$2.2 million in phase 1 and US$2.5 million in phase 2), representing 14 per cent of total costs; and beneficiaries US$1.6 million (US$1.1 million in phase 1 and US$0.5 million in phase 2), representing 5 per cent of total costs.

Table 2
Programme costs by expenditure category and financier
(Thousands of United States dollars)

Expenditure category	*IFAD loan*		*Financing gap 1*		*Financing gap 2*		*Beneficiaries phase 1*		*Beneficiaries phase 2*		*Borrower/ counterpart phase 1*		*Borrower/ counterpart phase 2*		*Total*
	Amount	*%*	*Amount*	*%*	*Amount*	*%*	*Amount*	*%*	*Amount*	*%*	*Amount*	*%*	*Amount*	*%*	*Amount*
1. Works	1 060	10.5	798	13.1	6 298	62.1	-	-	-	-	407	4.0	1 574	15.5	10 136
2. Equipment and materials	1 945	82.0	-	-	-	-	-	-	-	-	426	18	-	-	2 371
3. Vehicles	125	68	-	-	-	-	-	-	-	-	59	32	-	-	184
4. Grants	4 500	36.9	157	1.3	3 726	30.7	1 128	9.2	485	4.0	1 272	10.4	935	7.7	12 203
5. Training	431	29.5	314	21.5	643	44	7	0.5	8	0.6	55	3.8	-	-	1 461
6. Workshops	88	41.9	35	16.9	86	41.1	-	-	-	-	-	-	-	-	210
7. Consultancies, local	824	24.3	723	21.4	1 839	54.3	-	-	-	-	-	-	-	-	3 384
8. Consultancies, international	284	57.6	52	10.6	156	31.8	-	-	-	-	-	-	-	-	493
9. Salaries and allowances	568	36.6	-	-	984	63.4	-	-	-	-			-	-	1 552
10. Operating costs	174	33.2	-	-	351	66.8	-	-	-	-			-	-	526
Total	**10 000**	**30.7**	**2 079**	**6.4**	**14 084**	**43.3**	**1 136**	**3.5**	**493**	**1.5**	**2 219**	**6.8**	**2 509**	**7.7**	**32 520**

C. Summary benefit and economic analysis

44. Programme implementation will lead directly to increased income for farmers and rural entrepreneurs. Benefits will accrue from: (i) increased fodder and forage yields and livestock productivity due to improved land capability, application of improved inputs and enhanced husbandry; (ii) an increased proportion of marketed farm produce; (iii) reduced losses during production, processing and transportation of produce through innovative technology; (iv) improved quality of products, which attracts higher prices, as a result of the demand by processors for more reliable inputs/outputs; and (v) better-quality food products for consumers. Longer-term benefits will derive from the planned knowledge management of lessons learned.

45. Overall programme analysis yielded an economic internal rate of return of 17.8 per cent, with a net present value of US$13.8 million. Switching values shows that the economic viability is robust to adverse changes in programme costs, and the programme remains viable with increases in capital and recurrent costs or delay of benefits.

D. Sustainability

46. Sustainability is central to LPMIP and will be achieved in multiple ways:

(a) Environmentally – by improved climate resilience in production through improved land capability, application of improved inputs and enhanced animal husbandry;

(b) Market and commercial sustainability – through targeting of value chains with comparative advantage and credible market opportunities, with immediate opportunities to increase income and the profits necessary to attract further investments;

(c) Institutionally – through the use of existing and emerging service providers operating at the local level to deliver programme services and investments to strengthen their capacity;

(d) Economically – through selective use of limited partial matching grants intended to trigger "first mover" investments and innovations in value chains, closely linked to partnerships with mainstream banks and non-bank financial institutions to create access to mainstream financing; and

(e) Technically – through investment in landscape restoration where needed around supported infrastructure and irrigation schemes.

E. Risk identification and mitigation

47. Programme activities will focus on two livestock value chains to avoid programme complexity, as lessons from other projects highlight the risks of trying to implement overly complex projects. The programme will use the existing PMU with an established track record in implementing IFAD projects.

48. Other risks associated with programme activities are the following:

(a) National institutions and implementing partners generally lack capacity for social mobilization and cohesive marketing approaches. To mitigate this risk, the programme will: take into account the necessity of instituting adequate structures; and support development of the needed capacities (of enabling institutions, service delivery organizations and producer organizations), relevant covenants and approaches at early stages of implementation.

(b) Government policies continue to promote the concept of grain self-sufficiency at the expense of sustainable forage production to support increased meat and milk production. The programme will demonstrate that the production of higher-quality milk and meat can profitably replace more expensive imports.

(c) Given the history and heritage, post-Soviet era farmers are not accustomed to forming groups around a commercial or profitable interest or to manage and exploit common pastures and reclaimed waste land. Very little effort has been made to improve their knowledge, skills and practices to become commercial livestock farmers. The programme will build on existing informal groups (e.g. "solidarity groups"), which will be the entry point towards more focused community organizations and approaches such as training and learning experiences (innovation platforms, farmer field schools). Matching grants will also be used as an incentive to engage farmers.

V. Corporate considerations

A. Compliance with IFAD policies

49. LPMIP has been designed to be implemented in a manner consistent with IFAD standards, policies and strategies on targeting and gender, matching grants, financial management, procurement, private-sector involvement, the environment and climate change.

50. The programme will enhance social cohesion by strengthening value chains and forming CIGs that reflect IFAD targeting and gender policies. Programme activities will stress the need for further financial inclusion and intensified financial education to improve rural people’s savings and borrowing opportunities. A focused programme of community infrastructure, start-up and matching grants, which target planned programme beneficiaries, should assist these groups in developing their creditworthiness and assets, and facilitate access to the commercial lending sector. The grants will be tailored to the needs of smallholder farmers and market-chain small and microenterprises.

51. The environmental and social aspects of the proposed programme were found to comply with IFAD’s safeguard policies. The programme is classified in category "B" according to IFAD’s Administrative Procedures for Environmental Assessment.

B. Alignment and harmonization

52. The programme strategy and activities are designed to link with and complement other government-funded livestock and food security programmes. Significant opportunities exist for IFAD to work with MoA in sectoral policy dialogue and institutional capacity-building. The programme is particularly designed to address the gaps identified in other donor programmes supporting the agriculture sector,

with a view to creating synergies (i.e. the European Bank for Reconstruction and Development [EBRD], European Union, Food and Agriculture Organization of the United Nations, German Agency for International Cooperation, Swiss Agency for Development and Cooperation, United Nations Development Programme, United States Agency for International Development and the World Bank).

53. In particular, the programme will complement a new World Bank project that also provides support to the livestock sector, focusing on animal health and veterinary services. To capitalize on the recently signed memorandum of understanding between IFAD and EBRD, the programme will closely coordinate with EBRD's agribusiness-supported activities with the private sector. In particular, it will tap the service providers that have benefited from and been certified by the EBRD programme.

C. Innovations and scaling up

54. The programme will support demonstration, early adoption and innovative activities such as improved in-field water management, improved animal housing, upgraded stock water supplies and improved fodder conservation techniques. The LPMIP grant scheme will fund innovative activities, subject to implementation by the participating household of the demonstration being prepared to allow publication of detailed cost and benefit information. Publicity for the innovation will use display boards and/or extension leaflets, linked to field visits by interested farmers.

55. Innovations and best practices at the village level will be documented for the purposes of replication and scaling up. Farmers implementing innovations and best practices will serve as mentors to other farmers to accelerate scaling up and replication of the innovations.

D. Policy engagement

56. To address policy issues that may reduce the benefits of programme activities, structured interaction with market-chain stakeholders will ensure that stakeholders are aware of government strategies and policies relating to livestock, pasture management and livestock value chains, and can provide feedback regarding their concerns and priority issues to be addressed. Annual review and planning processes for village development plans, village-level CIGs and the MSMPs will provide the starting points for policy dialogue. These will be consolidated through knowledge management activities, including annual experience-sharing forums. Studies may be commissioned to quantify costs and benefits of current or suggested policies. The PMU/PRST will lead policy consultations involving smallholder farmers, market stakeholders and the Government.

VI. Legal instruments and authority

57. A programme financing agreement between the Republic of Azerbaijan and IFAD will constitute the legal instrument for extending the proposed financing to the borrower. A copy of the negotiated financing agreement is attached as appendix I.

58. The Republic of Azerbaijan is empowered under its laws to receive financing from IFAD.

59. I am satisfied that the proposed financing will comply with the Agreement Establishing IFAD and the Policies and Criteria for IFAD Financing.

VII. Recommendation

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

> RESOLVED: that the Fund shall provide a loan on ordinary terms to the Republic of Azerbaijan in an amount equivalent to ten million United States dollars (US$10,000,000), and upon such terms and conditions as shall be substantially in accordance with the terms and conditions presented herein.

Gilbert F. Houngbo
President

Negotiated financing agreement

Livestock Productivity and Marketing Improvement Programme

(Negotiations concluded on 6 December 2017)

Loan Number: ______________

Programme Title: Livestock Productivity and Marketing Improvement Programme ("LPMIP" or "the Programme")

The Republic of Azerbaijan (the "Borrower")

and

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

(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 Programme Description and Implementation Arrangements (Schedule 1) and the Allocation Table (Schedule 2).

2. The Fund's General Conditions for Agricultural Development Financing dated 29 April 2009, amended as of April 2014, and as may be amended hereafter 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 to the Borrower (the "Financing"), which the Borrower shall use to implement the Programme in accordance with the terms and conditions of this Agreement.

Section B

1. The amount of the Loan is ten million United States dollars (USD 10 000 000).

2. The Loan shall be subject to interest on the principal amount outstanding at a rate equal to the IFAD Reference Interest Rate, payable semiannually in the Loan Service Payment Currency, and shall have a maturity period of eighteen (18) years, including a grace period of three (3) years starting from the date that the Fund has determined that all General Conditions precedent to withdrawal have been fulfilled in accordance with Section 4.02(b).

3. The Loan Service Payment Currency shall be the USD.

4. The first day of the applicable Fiscal Year shall be 1 January.

5. Payments of principal and interest shall be payable on each 15 May and 15 November.

6. There shall be a Designated Account maintained in a commercial bank denominated in USD. There shall also be an Programme account in Azerbaijani Manat (AZN) to receive financing from the Designated Account in a commercial bank. In addition, there will be a separate counterpart account for the Borrower's contribution.

7. The Borrower shall provide counterpart financing for the Programme in cash and exemption from taxes in the amount not less than two million and two hundred thousand United States dollars (USD 2.2 million) for the first phase of the programme.

Section C

1. The Lead Programme Agency shall be the State Service for Management of Agricultural Project and Credits under the Ministry of Agriculture (MoA).

2. The following are designated as additional Programme Parties: the Ministry of Ecology and Natural Resources, the Ministry of Economy, the Ministry of Finance, the Central Bank, the State Committee on Women, Child and Family Issues, Amelioration and Irrigation Open Joint Stock Company and participating Rayons.

3. The Programme Completion Date shall be the eighth anniversary of the date of entry into force of this Agreement (first phase of the programme is 3 years and the second phase is 5 years).

Section D

The Loan will be administered and the Programme supervised by the Fund.

Section E

1. The following is designated as an additional ground for suspension of this Agreement:

(a) Key Project staff shall have been transferred, suspended, or terminated without the Fund's prior no-objection.

(b) Any institutional changes have been made by the Borrower to the Programme Steering Committee and/or the Programme Management Unit without the prior consent of the Fund, and the Fund has determined that such changes are likely to have a material adverse effect on the Programme; and

(c) The Programme Implementation Manual, or any provision thereof, has been abrogated, waived, suspended, or amended without the prior consent of the Fund and the Fund has determined that this is likely to have a material adverse effect on the Programme.

2. The following are designated as additional general conditions precedent to withdrawal:

(a) the Programme Director, Finance Manager, and Procurement Specialist shall have been duly authorised to function;

(b) The Programme Implementation Manual including the Financial Management Procedures has been approved by IFAD and a Financial and Accounting System is functional.

3. This Agreement is subject to approval by the Borrower.

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

For the Borrower:

Minister for Finance
of the Republic of Azerbaijan
Ministry of Finance
Samad Vurgun St. 135
AZ 1022 Baku, Azerbaijan

For the Fund:

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

This Agreement, dated _________, has been prepared in the English language in two (2) original copies, one (1) for the Fund and one (1) for the Borrower.

THE REPUBLIC OF AZERBAIJAN

____
Authorized Representative
Name and title

INTERNATIONAL FUND FOR
AGRICULTURAL DEVELOPMENT

____
Gilbert Houngbo
President

Schedule 1

Programme Description and Implementation Arrangements

I. Programme Description

1. *Target Population.* The Programme will target about 20,500 smallholder livestock rearing households, among them the poorest women-headed households and youth. The Programme will also work with small-scale women and men milk and dairy traders and processors, and livestock traders who are actors in the market linkages for the target group.

2. *Programme Area.* The Programme shall work in Agjabedi, Barda, Beylagan and Goychay rayons. Based on performance other districts (Rayons) can be included.

3. *Goal and Objective.* The overall Programme goal is to reduce rural poverty (increased incomes and reduced vulnerability of poor rural households) by supporting the Government's economic diversification programme. The Programme development objective is to increase smallholder farmers' income from improved livestock production and marketing activities in Programme rayons with strengthened resilience to climate shocks.

4. *Components and Outcomes.* Programme activities shall be organised in two mutually supportive components aimed at developing solutions that will help upgrade the milk and meat value chains and selected investments in poultry. Given the high vulnerability to climate change, LPMIP will mainstream a climate smart approach throughout its activities. Programme activities will be coordinated under the Programme Management component.

4.1 Component 1: **Market-led sustainable livestock production**

Outcome 1: *Livestock productivity improvements sustainably increased with climate resilience*

The Programme will develop the 'soft' capacity of farmer groups to contribute to the preparation of community level village development and climate vulnerability plans to guide and prioritise investments in pastures and public infrastructure to improve farmer access to feed for livestock. In one rayon, possibly Beylagan, a pilot activity will be undertaken to show how development of a rayon level land management plan can guide targeting and design of village level natural resource management and productive investment activities.

The Programme will fund community investments in advanced irrigation, drainage and land rehabilitation for forage production and pasture rehabilitation, natural seed banks and adoption of climate resilient practices and technologies.

The poorest women-headed households will have access to poultry start-up packages and start up packages for alfalfa forage production to provide an initial boost towards sustainable poultry or livestock production.

To complement the investments, Programme funds will be used to support demonstration, early adoption and innovation activities such as improved in-field water management, improved animal housing and improved fodder conservation techniques.

Other matching grant activities could include upgrading animal housing, improving stock watering facilities, improving alfalfa hay, silage or feed storage areas, buying simple feed processing activities or installing equipment to improve milk hygiene and quality. The programme would further support developing investment and business proposals to facilitate borrowing from the commercial sector.

4.2 Component 2: **Increased return from livestock products**

Outcome 2: *Smallholder livestock producers receive higher product prices and returns from Azeri markets and consumers*

In addition to local- and rayon-level traders, small scale processors and rayon market participants, individual and groups of farmers who have graduated from production oriented capacity building activities or are deemed market-ready will be offered the opportunity to develop their capacity in market chain related product quality improvement, business and financial planning and management. To assist, farmer and value chain stakeholders develop a shared understanding of market needs and that planned investments to improve product quality and or market access are appropriate, multi-stakeholder marketing platforms (MSMP) to be brokered by service providers, for the main value chains (milk, meat and poultry) will be formed in each rayon to address constraints in the local market chains. A priority MSMP activity will be to link smallholder producers with existing large-scale production and processing facilities.

Aggregation, processing and marketing opportunities identified by MSMPs will be developed through market stakeholders' own resources supplemented with programme grants for developing business plans and/or developing the capacity of the MSMP to assess and develop the proposals. The matching grants will fund demonstration innovation or early adoption of small initiatives to improve raw product quality, facilitate aggregation and delivery to markets or processors, upgrade small scale processing activities, and other incremental improvements in the market chains including providing support to MSMP members to link to existing rural finance facilities.

4.3 Component 3: **Programme Management**. In addition to the Programme coordination, implementation management and monitoring and evaluation (M&E) activities, this component will include activities to facilitate increased access to financial services and for Policy Dialogue.

II. Implementation Arrangements

5. *Lead Programme Agency*. Overall institutional responsibility for the effective management and implementation of the Programme at the central level shall rest with the State Service for Management of Agricultural Project and Credits under the MoA.

6. *Programme coordination.* A Programme Steering Committee (PSC) shall be appointed by a decree of the Minister of Agriculture, composed of representatives from MoA, the Lead Programme Agency, the Ministry of Finance, the Central Bank, State Committee on Women, Child and Family Issues, the Ministry of Economy, Ministry of Ecology and Natural Resources, and the Programme Director. The PSC will carry out annual Programme reviews, approve the Annual Workplan and Budget (AWPB), offer strategic and policy advice and resolution and coordinate with parallel or complementary initiatives to enhance rural development in the programme area. The PSC will meet at least once a year and on an ad-hoc basis as necessary.

7. At rayon level, rayon working groups (RWG) will be established based on Local Agricultural Departments offices comprising: the Head of Rayon Agricultural Departments; a representative from the livestock industry; a farmers' representative and the Programme Director (or his designated representative) with the rayon coordinator as the secretary. This group will supervise the village selection process, approve all grants, address coordination and resource issues within that rayon, and champion knowledge sharing.

8. At local level the Programme will closely work with the municipality and village executive committees (ExCom) to ensure that village development plans (and action plans) and commodity business plans are developed and implemented in a participatory

and complementary manner between the Programme components and align with other initiatives from government and donors. At village level, a Community Programme Committee is the key implementation and coordination group.

9. *Programme Management Unit*. Programme coordination, supervision and monitoring will be undertaken by a small Programme Management Unit (PMU) located within the Lead Programme Agency in Baku. The PMU will be resourced from the existing IPMU (Programme Director, Financial Manager, Procurement Officer, M&E Officer, an accountant, Community Development Specialist, Administrative Manager/Coordinator with International Organisations, Office Manager). Additional staff members shall be recruited on competitive basis as needed. The appointment and removal of these key staff members shall be subject to the non-objection of the Fund.

10. A Programme Regional Support Team (PRST) will be established and located in Beylagan rayon to facilitate the implementation of Programme activities in four targeted rayons through a continuous process of technical backstopping, implementation support and progress reporting. It will also support the active engagement of the communities in Programme implementation through participatory planning and monitoring. The PRST will be resourced with a team leader, M&E/ Contracts Management specialist, Community Development and Gender specialist, Community Infrastructure Engineer and Rural Finance specialist. A Rayon Coordinator, one in each of the targeted rayons, will be recruited to coordinate and monitor programme activities, and supervise service contracts. All staff will be selected on a competitive basis and retained on performance based contracts.

11. The AWPB will guide Programme implementation and provide a set of benchmarks against which Programme performance can be measured each implementation year. The PRST will prepare draft rayon AWPBs for each Programme Year in line with IFAD requirements, with inputs from service providers and agencies. These will be consolidated by the PMU. The first AWPB will be presented during the start-up workshop and sent to the Fund for non-objection. The following 12-month AWPBs will be submitted to the PMU for review and approval, and to the Fund for non-objection no later than sixty days before the beginning of the relevant Programme Year. The PMU will consolidate the Programme's quantitative financial and physical output data in the Management Information System.

12. *Programme Implementation Manual.* The PMU shall prepare a draft Programme Implementation Manual (PIM) and shall forward it to the Fund for its non-objection. If the Fund does not comment on the draft PIM within thirty (30) days after receipt, it shall be deemed to have no objection. The Lead Programme Agency shall adopt the PIM substantially in the form approved by the Fund. The PIM, or any provision thereof, may not be waived, suspended, terminated, amended or modified without the prior agreement of the Fund.

13. Within 180 days of entry into force, the Programme will have a comprehensive M&E system to generate all information needed for managing the Programme activities. All M&E staff at PMU and PRST shall be in place and, working with Rayon Coordinators, will ensure systematic measurement of performance indicators and provide continuous data on implementation progress at rayon levels. The system will include process and activity output and outcome indicators that will allow for disaggregation of data by different needed levels. The Results and Impact Management System (RIMS) will be fully incorporated in the Programme M&E system. Continuous learning and knowledge management (KM) will fully be integrated into the Programme and mainstreamed into implementation across all levels.

14. No later than 90 days after the start of the Programme the PMU will manage a comprehensive baseline survey which will be updated on annual basis to track the different Programme indicators over time, including for the Mid-Term Review. During the Programme's final year, a completion survey will be conducted. Results will be compared against the baseline to assess Programme impact.

Schedule 2

Allocation Table

1. *Allocation of Loan Proceeds.* (a) The Table below sets forth the Categories of Eligible Expenditures to be financed by the Loan and the allocation of the amounts of the Loan to each Category. All amounts are 100% net of taxes, Government contribution and beneficiary contribution:

Category	Loan Amount Allocated (expressed in USD)
I. Works	950 000
II. Equipment and Material (including vehicles)	1 860 000
III. Consultancies	1 470 000
IV. Grants and subsidies	4 050 000
V. Operating Cost	670 000
Unallocated (10%)	1 000 000
Total	10 000 000

(b) The terms used in the Table above are defined as follows*:*

Category III "Consultancies means Eligible Expenditures related to training, workshops as well as local and international consultancies as defined in the AWPB.

Category V "Operating Cost" includes Eligible Expenditures related to Salaries and Allowances.

2. *Start-up Costs*. Withdrawals in respect of expenditures for start-up costs incurred before the satisfaction of the general conditions precedent to withdrawal shall not exceed an aggregate amount of two hundred thousand USD (USD 200 000).
(To be delivered to Executive Board representatives.)

Logical framework

AZERBAIJAN LIVESTOCK PRODUCTIVITY and MARKETING IMPROVEMENT PROGRAMME LOG FRAME

Results	Indicators				Means of verification			Assumptions (A) Risks (R)
Hierarchy	**Name**	**Baseline**	**Mid Term**	**End target**	**Source**	**Frequency**	**Responsibility**	
Outreach	HHs receiving project services	0	10,000	20,500	▪ Baseline, completion, ▪ M&E system	Y1, Y3, Y8	**PCU**	
	Individuals receiving project services (men/women)	0	11,000	22,900	▪ Baseline, completion, ▪ M&E system	Y1, Y3, Y8	**PCU**	
	Individuals receiving project services (men)	0	10,000	20,500	▪ Baseline, completion, ▪ M&E system	Y1, Y3, Y8	**PCU**	
	Individuals receiving project services (women)	0	1,000	2,400	▪ Baseline, completion, ▪ M&E system	Y1, Y3, Y8	**PCU**	
	Individuals receiving project services (youths)	0	1,000	3,000	▪ Baseline, completion, ▪ M&E system	Y1, Y3, Y8	**PCU**	
Goal: Reduced rural poverty (increased incomes and reduced vulnerability of poor rural households) by supporting the government's economic diversification programme	▪ Reduced vulnerability[2] of 20,500 poor participating households (20% of households report improvement in assets ownership index		10,000	20,500	▪ Baseline, completion survey	▪ Y1, Y3, Y8	▪ PCU	▪ Stable macroeconomic atmosphere (A) ▪ Non-oil sector maintains priority (A) ▪ Inflation remains at an average of 5% per annum (A) ▪ GoA rural development economic diversification policies disadvantage small farmers (R)
Programme Development Objective: Increased smallholder farmers' income from improved livestock production and marketing activities in programme rayons with strengthened resilience to climate shocks	▪ At least 75% of the 20,500 targeted households increased net farm income (RIDE)	0	20%	75%	▪ Baseline & completion survey	▪ Y1, Y3, Y8	▪ PCU	▪ Conducive government policies (A) ▪ Programme outcomes stimulate economic growth (A) ▪ Reduced imported livestock, meat and dairy products have to meet same quality standards as locally produced product (A) ▪ GoA encourages imported livestock products to restrict retail meat and dairy product prices (R)
	▪ At least 5,000 households increased their climate resilience (RIDE)	0	1,000	5,000		▪ Y1, Y3, Y8	▪ PCU	

[2] Measures for vulnerability will be assessed during inputs of the social and targeting consultant during late March 2015. The measure that can be readily assessed in Azerbaijan could include: food security (decreased child malnutrition); improvement in HH assets; resilience and adaptive capacity increased; women's empowerment increased, reduced proportion of income from remittances, cash and near cash savings reserves.

Results	Indicators				Means of verification			Assumptions (A) Risks (R)
Hierarchy	**Name**	**Baseline**	**Mid Term**	**End target**	**Source**	**Frequency**	**Responsibility**	
Outcome 1: Forage production and livestock productivity sustainably increased with climate resilience	▪ Improved productive infrastructure over 5,900 ha (RIDE 1.1.2)	0	2000	5,900	▪ Baseline, completion, Progress reports	▪ Y1, Y3, Y8	▪ PCU	▪ MoA can develop effective partnerships with private sector (A) ▪ Government support planting of forage crops (A) ▪ Government subsidizing and supporting planting of other crops (R) ▪ Livestock epidemic disease (R) ▪ Lack of private veterinary service (R) ▪ Government supports public veterinary services (A) ▪ Climate change is in line with current predictions
	▪ Livestock production (beef, milk, sheep meat poultry) increased by 30% by rayon	0	10%	30%		▪ Y1, Y3, Y8	▪ PCU	
	▪ Government led policy review workshops takes place to address key livestock productivity constraints modalities. (RIDE 1)	0	2	4		▪ Y1, Y3, Y8	▪ PCU	
Outputs 1: **1.1** Livestock productivity improvements implemented	▪ Number of people trained in livestock production practices and technologies.	0	10,000	20,500	▪ Baseline, completion, Progress reports	▪ yearly	▪ PCU	
1.2 Climate resilient productive infrastructure used	▪ **Value of small grants used to develop business plans for MSMPs**	**0**	**USD 1.17 million**	**USD 2.47 million**				
	▪ Number of Ha brought under good agriculture practice.	0	2,000	5,900				
Outcome 2: Smallholder livestock producers receive higher product prices and returns from Azeri markets and consumers	▪ 80% of targeted producers benefit from improved markets access ((RIDE 2.1.6).	0	20%	80%	▪ Baseline, completion, Progress reports	▪ Yearly	▪ PCU	▪ LPMIP MoA can develop effective partnerships with private sector (A) ▪ Willingness of smallholder farmers to engage in livestock value chain development (A) ▪ Municipal policies support central markets at rayon level (R) ▪ Reduced market chain costs/increased selling prices are captured by farmers (R)
2.1 Functional improved value chain livestock market	• **Number of MSMPs have their capacity built in quality production, business planning and management.**	**0**	**28**	**56**	▪ Baseline, completion, Progress reports	▪ Yearly	▪ PCU	
	• No. of supply contract farming arrangements in place between producer groups and large processors.	0	10	**20**				
2.2 Channelled investments in improved livestock market	• **Value of matching grants for demonstrations and early initiatives.**		**USD 4.27 million**	**USD 7.45 million**				