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IFAD AND PERFORMANCE-BASED LENDING



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IFAD AND PERFORMANCE-BASED LENDING

I. INTRODUCTION

1. In view of the scarcity of resources compared with the needs of development and poverty reduction, there is concern to maximize the effectiveness of official development assistance. This note explains how IFAD integrates performance criteria when making decisions about resource allocation.
2. Effectiveness is measured in terms of impact in relation to objectives. IFAD was created with the goals of increasing agricultural production, reducing poverty and improving the nutritional status of the rural poor. Efficiency in terms of the cost of programme delivery is a continuing priority.
3. IFAD in principle is called upon to assist all its developing Member States. At the same time, to make the most effective use of its resources, the Fund allocates them through criteria relating to needs in terms of the extent and depth of rural poverty and the opportunity for achieving impact. This process rests on three pillars:
 - (a) IFAD's basic documents, which stipulate country priorities, based on need in terms of rural poverty reduction (see section II);
 - (b) the 1994 and 1999 regional lending shares agreed by IFAD's governing bodies (see section III); and
 - (c) decisions on country project lending within the agreed regional shares..
4. The decisions in (c) are made in response to performance, in terms of opportunities for efficient investments, the existence of an environment that allows resources to be effectively used for poverty reduction, the government's willingness to develop a pro-poor institutional environment with IFAD assistance and, finally, past country portfolio performance (see section IV).
5. The Fund is translating agreed regional lending shares into country allocations on the basis of past and expected performance with respect to impact – the convergence of need, enabling conditions and opportunities for cost-effective investment programmes.

II. COUNTRY PRIORITIES IN IFAD'S LENDING POLICIES AND CRITERIA

A. The Policy Framework

6. IFAD's basic documents, the Agreement Establishing the International Fund for Agricultural Development (articles 2 and 7) and the Lending Policies and Criteria (see sections III and IV) specify the Fund's policy for allocating loan resources.
7. The Fund is mandated to lend only to its "developing Member States". It is expected to give priority in its lending programme to the "poorest developing countries", "countries characterized by low food security and severe poverty in rural areas", "food-priority countries", the "poorest food-deficit countries", "low-income countries", "countries that face a serious aggregate food shortage or have large segments of population that consume food in quantities considered well below the established minimum standards" and "the poorest countries whose food problems require priority attention". Criteria are recommended in the Lending Policies and Criteria to determine priority status. These are:



- low per capita income;
 - projected cereal deficits;
 - the degree of protein-calorie malnutrition;
 - insufficient average increase in food production;
 - the potential for rapid, efficient, equitable and sustainable increases in food production, including availability of underutilized resources; and
 - balance-of-payment constraints.
8. The Executive Board must take into account debt sustainability and debt-servicing capacity.
9. The majority of IFAD loans are to be provided on highly concessional terms to countries with a 1992 per capita GNP below USD 805 or with “IDA-only” eligibility. The proportion was set at 67% of the amount lent annually.

B. Implementation of Lending Priorities

10. Using common definitions for poor countries, Table 1 shows how IFAD is complying with the criteria set out above, including priority to low-income food-deficit countries (LIFDCs) and its lending on highly concessional terms. The lower total lending levels for least-developed countries (LDCs) and highly indebted poor countries (HIPCs) eligible for debt intervention (DI) reflect the smaller number of countries concerned, below-average loan sizes in relation to absorptive capacity, and constraints on country programme development resulting from conflicts and arrears. IFAD’s priority attention to poor countries is reflected in the large number of projects devoted to them.

Table 1. Lending by Country Group

Country Group	Number of Countries	Total Lending 1995- 2001 (SDR million)	% of Total IFAD Lending	Average Loan Size (SDR million)	Number of Projects
LIFDCs	82	1 589.66	77	10.13	157
LDCs	48	727.00	35	9.32	78
Highly concessional	75	1 530.21	74	10.07	152
HIPC DI eligible	42	836.06	41	9.09	92
Total IFAD	118	2 057.81	100	10.04	205

Notes: Amounts in SDR million net of cancellations. Average loan refers to average IFAD lending per project. Loan 422-Kenya included (not part of lending programme because financed from prior loans).

III. ESTABLISHING REGIONAL LENDING SHARES: COUNTRY-BASED NEEDS ASSESSMENTS

A. The 1994 and 1999 Decisions on Regional Lending Shares

11. The Consultation for the Fourth Replenishment (1994-1995) established an ad hoc committee to establish a framework for planning future resource allocations in an equitable and transparent manner that took into account the criteria in articles 2 and 7 of the Agreement Establishing IFAD and in section III of the Lending Policies and Criteria. The committee sought to integrate the Special Programme for Sub-Saharan African Countries into the Regular Programme, reinforce the emphasis on Africa and include new Member States in IFAD’s lending programme.

12. The 1994 methodology used an “objective allocation” framework based on an index derived from about 20 indicators as an indicator of country need. The poverty indicators were:



- the Food Security Index (FSI), related to food production and consumption, and reflecting growth and variability);
- the Integrated Poverty Index (IPI), comprising the number of poor people, income distribution and the rate of growth of per capita GNP; and
- the Basic Needs Index (BNI), comprising an education index and a health index.

13. The size of the agricultural population was added to the criteria to reflect the importance of the sector and the need to support its development. This set of indexes is particularly relevant to the Millennium Development Goals.

14. The methodology was country-based. Results were aggregated into regional lending shares, to be administered by the Fund's regional divisions. The 1994 regional distribution is presented in Table 2.

15. Between 1994 and 1999, IFAD's membership increased by 13 countries, mainly in its administrative Near East and North Africa (NENA) region. This called for an update of the 1994 allocations by the ad hoc committee on regional allocations, created in 1999 in the context of negotiations for the Fifth Replenishment. Table 2 shows the 1999 update of regional lending shares.

Table 2. The 1994 and 1999 Allocations

	1994 Allocations (%) Document GC 18/L.11, Table 5	Revised 1999 Allocations
PA and PF (Africa I and II)	37.2	36.77
PI (Asia and the Pacific)	31.4	31.01
PL (Latin America and the Caribbean)	17.9	17.03
PN (Near East and North Africa)	13.5	15.19
Total	100.0	100.00

16. In formulating these regional shares, it was clear to Member States that the Fund must be flexible in determining and adjusting country allocations to reflect changing realities on the ground. The Fund would continue to request annual Executive Board approval of regional allocations, to be administered on a rolling three-year-average basis.

B. Implementing Agreed Regional Lending Shares

17. The regional structure of IFAD's lending since the 1994 decisions is illustrated in Table 3. Regional lending shares are complied with on a three-year rolling average basis. The 1997 shortfall in lending to Africa is being recovered over time, but the region's share of lending has exceeded the normal allocation since 1999, allowing gradual recovery.

Table 3. Regional Lending Shares – Actual¹

IFAD Lending by Year (SDR million, net of cancellations)								
	1995	1996	1997	1998	1999	2000	2001	Total
PA	48.05	46.90	13.45	58.45	62.55	62.55	58.15	350.10
PF	34.75	55.01	25.30	47.40	82.35	56.65	79.10	380.56
PI	79.15	70.70	128.75	77.45	76.30	98.05	83.95	614.35
PL	48.95	51.70	61.45	53.00	55.35	48.40	53.80	372.65
PN	48.70	40.80	59.30	63.40	39.50	46.60	41.85	340.15
Total	259.60	265.11	288.25	299.70	316.05	312.25	316.85	2 057.81
Annual Regional Shares								
	1995	1996	1997	1998	1999	2000	2001	Total
PA	18.51	17.69	4.67	19.50	19.79	20.03	18.35	17.01
PF	13.39	20.75	8.78	15.82	26.06	18.14	24.96	18.49
PI	30.49	26.67	44.67	25.84	24.14	31.40	26.50	29.85
PL	18.86	19.50	21.32	17.68	17.51	15.50	16.98	18.11
PN	18.76	15.39	20.57	21.15	12.50	14.92	13.21	16.53
Total	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00
Three-Year Rolling Average Share								
	1995	1996	1997	1998	1999	2000	2001	<i>1999 norm</i>
PA			13.62	13.95	14.65	19.78	19.39	18.38
PF			14.30	15.11	16.88	20.00	23.05	18.39
PI			33.94	32.39	31.55	27.13	27.35	31.01
PL			19.89	19.50	18.84	16.90	16.66	17.03
PN			18.24	19.04	18.07	16.19	13.54	15.19
Total			100.00	100.00	100.00	100.00	100.00	100.00

IV. TRANSLATING THE REGIONAL LENDING SHARES INTO COUNTRY LENDING

A. Background Considerations

18. In view of the statements in the Lending Policies and Criteria that “the Fund will not seek to develop a pattern of country allocations”, it was agreed that reaching decisions about loans and their size would require a step-by-step approach. This would consist of the following levels:

- (a) developing country eligibility in principle by membership in IFAD;
- (b) regional allocations that limit the amounts of loans available to a region or a country;
- (c) strategy regarding countries of concentration, including targeting beneficiaries; and
- (d) conditions affecting the decisions to make a loan and its size, with particular emphasis on performance.²

¹ All figures relate to the period from 1995 (the year of approval of the regional lending shares) to 2001; eligibility for lending terms and conditions is the current eligibility, irrespective of past status.

² Report of the chairperson of the Ad Hoc Committee on Regional Lending Shares.

**Box 1: Mauritania**

1. In order to ensure that the Fund's limited resources are used to make a maximum positive impact on the livelihood of the rural poor, IFAD has developed a number of instruments to assess the institutional capacity and policy environment for developing sustainable poverty-reduction programmes. The country strategic opportunities paper (COSOP) has been developed as the main modality to examine the opportunities and capacities in each country where IFAD operates to support effective and sustainable poverty programmes. This box explores the way the COSOP has provided a framework for resource allocation decisions in the case of Mauritania.
2. In Mauritania, IFAD projects in the late 1980s and early 1990s were plagued by a number of difficulties and their implementation was problematic with poor disbursement rates and unsatisfactory impact. Recognizing these issues, the Fund did not finance any new projects in Mauritania between 1994 and 2000 although ongoing projects continued.
3. As a first step towards addressing these issues and relaunching an effective programme in the country, in 1996 IFAD undertook a country portfolio evaluation (CPE). The CPE made an in-depth analysis of the causes of rural poverty in Mauritania and further, it carried out a full assessment of ongoing IFAD projects. In the light of this assessment, the CPE made important recommendations on measures to improve project implementation as well as focus future operations in the poorest and most vulnerable rural areas in Mauritania. The CPE recommendations provided the basis for a constructive dialogue with the Government of Mauritania, which has since taken strong measures to address some of the management and implementation problems of the Fund-supported projects.
4. Building on the CPE, IFAD developed a COSOP for Mauritania which was approved in May 2000. The COSOP underlined the importance in Mauritania of empowering the rural poor, especially the most vulnerable groups such as the *Adwaba* communities, strengthening grass-roots organizations, developing effective mechanisms for resource transfers to the rural population and improving land tenure for the poor and their access to markets and financial services. The period of the preparation of the COSOP coincided with the final stages of the development of the country's PRSP. IFAD sought to make an input to the PRSP and both the PRSP and the COSOP give priority to the poorest rural areas of Mauritania, where the population has long suffered from exclusion and marginalization.
5. In the framework of the strategic priorities of the COSOP, the first operation to be developed was the Poverty-Reduction Project in Aftout-South and Karakoro (PASK), approved in 2001. The main target group of the PASK was *adwaba* settlers consisting of other groups suffering from exclusion. It sought to promote their empowerment as well as giving them access to financial services, more supportive local institutions and more diversified income-generating opportunities. The PASK served as a major instrument for the implementation of Mauritania's PRSP. It provided an opportunity for the Government of Mauritania to utilize the proceeds of the debt relief it received from the enhanced HIPC-DI to cofinance the project, providing about USD 8 million, or some 35% of the total investment cost of the project.
6. The decision by IFAD to relaunch funding in the country through the PASK was thus made in the framework of a careful analysis during the previous four years of the underlying causes of rural poverty and the opportunities to address them, undertaken in full consultation with the Government. Moreover, it was also placed firmly in the context of the wider policy development carried out by donors under the PRSP in the country. Although it is too early to assess its implementation, the PASK is based on the active participation of the intended beneficiaries, the full support of the Government and in the light of an in-depth assessment of the institutional and administrative capacities of the country.
7. A second operation that is being prepared under the strategic perspectives of the COSOP is the second phase of the Maghama flood recession improvement project. This intervention will target another area with a very high level of poverty. The Government has now accepted to fully devolve the resolution of land tenure issues to the local populations and their organizations. This will allow the second phase to build on the achievements of the first, in a more supportive policy environment, to achieve a stronger impact on the production, incomes and well-being of the rural poor in the project area. This experience also illustrates the value of undertaking a policy dialogue in the context of Fund-supported projects to promote policy development favourable to the needs and priorities of the poor.
8. The experience of Mauritania shows how a dialogue based on a careful review of the underlying causes of poverty and management and policy issues, can help strengthen the implementation and impact of poverty projects, even in difficult conditions. Building on this analysis and the improvements in implementation brought about by the earlier dialogue, the COSOP, undertaken in a participative way in partnership with the Government and other stakeholders, focused priority on the poorest groups and helped promote pro-poor changes in policies and institutions that create the potential for stronger project performance and impact on poverty. Through this dialogue and with commitment of the authorities, Mauritania has given growing attention to rural poverty issues. It is perhaps the first country in which a Fund-supported rural poverty-reduction project has been consciously formulated as a key implementing instrument for the PRSP for rural areas. Moreover IFAD was able to mobilize substantial cofinancing not only from the OPEC Fund but also from the Government of Mauritania, thus significantly enhancing the allocation of resources for the rural poor.



B. Criteria for Allocating Regional Shares into Country Lending

19. In order to translate the 1999 regional lending shares into country lending, the regional divisions first identify the circumstances that limit effective lending, such as arrears or civil strife. Against this background, the resources available to the region are allocated through the COSOP process (see Box 1 for the example of Mauritania) on the basis of needs-based and performance-related criteria. The criteria applied are the following:

(a) Responding to country needs

- (i) Breadth of poverty, as measured by poverty in the agricultural and rural population. There is no strict proportionality between IFAD lending and the regional rural population, but countries with the highest number of rural poor tend to receive the largest amount of lending.
- (ii) Depth of rural poverty, as measured by the United Nations Development Programme Human Development Index (HDI). Smaller countries such as Bhutan, Nepal and Mongolia are allocated greater shares mainly because of their very low HDI.
- (iii) Per capita GDP. This criterion is principally articulated through the lower priority given to middle-income countries, except when there is a strong commitment to rural poverty reduction consistent with IFAD's, or when there is an opportunity to develop a national strategy based on "lead experience". Some middle-income countries, such as Brazil and Mexico, have a significant incidence of rural poverty; IFAD targets its lending operations towards the rural poor in such countries.
- (iv) The size of indigenous populations. This is related to the depth and extent of poverty, complemented by the conditions faced by the indigenous rural population. It is particularly relevant to Andean and Central American countries.
- (v) Natural disasters that have a serious impact on poverty and food security among rural populations. The effect of hurricane Mitch in Honduras and El Salvador was an example.
- (vi) Assessment of countries' absorptive capacity.

(b) Portfolio performance (see Box 2 for the experience in Nigeria)

- (i) A coherent national rural poverty-reduction strategy. This must include provisions to address gender issues affecting poor women and their dependants.
- (ii) Economic and sectoral policies. These must guarantee fair market transactions.
- (iii) Transparency and efficiency in public resource allocation and use. This must include external assistance channelled through the public sector. Appropriate levels of national public resources must be allocated in support of the national rural poverty-reduction programme.
- (iv) There must be accountability and efficiency in public institutions and administration.



- (v) Civil-society institutions must be encouraged and there must be recognition of their role in the development process. A favourable legal and regulatory framework must be in place.
 - (vi) Mechanisms involving significant participation by all groups of the poor in local processes of development planning, public resource allocation and public services. These must include women and minorities.
 - (vii) Respect for traditional mechanisms through which the poor maintain access to and manage natural resources at the community level.
 - (viii) Efforts by governments to strengthen governance, if necessary with IFAD support.
 - (ix) With respect to project portfolio performance:
 - (a) national ownership, particularly share of domestic contribution to project financing and willingness to promote cofinancing with other donors;
 - (b) disbursement rates and disbursement lag;
 - (c) implementation performance, as reflected in average project rating for ongoing projects;
 - (d) average period from project approval to effectiveness; and
 - (e) number of extensions per project.
- (c) **Limiting circumstances**
- (i) Chronic arrears problems, total days of project suspensions and numbers of suspensions. For about ten years it has not been possible to consider pipeline development in a significant number of countries.
 - (ii) Situations of political instability, civil strife and poor internal security. IFAD strives where possible to make a contribution to the resumption of development and peacebuilding in post-conflict situations.
 - (iii) Poor administration, unsupportive policy and weak commitment to the rural poor.

V. CONCLUSIONS

20. IFAD is implementing the country lending priorities established under the Agreement Establishing IFAD and the Lending Policies and Criteria and with the three-year rolling-programme framework of regional lending shares established by the ad hoc committees of 1994 and 1999. In translating the regional lending shares into country programmes, the Fund is applying needs - and opportunity - related criteria through COSOPs to ensure the effectiveness of its lending programme.

21. The *Strategic Framework for IFAD 2002-2006* contributes to IFAD's effectiveness by renewing and clarifying the Fund's objective: enabling the rural poor to overcome their poverty, by strengthening the capacity of the rural poor and their organizations, improving their equitable access to productive natural resources and technology and increasing their access to financial services and markets. The enabling environment and opportunities for IFAD-supported activities are analysed against these strategic objectives. IFAD's mission and its local-level entry point for interventions determine the needs-based and performance-related decision-making criteria.



22. Allocating resources to country programmes is not an automatic process. It is the result of a decision-making procedure, supported by COSOPs. COSOPs define needs and opportunities; further programme design and implementation are built on them.

23. Other international financial institutions (IFIs) have introduced performance-based lending systems. Their criteria for performance relate mainly to their impact objectives and preconditions, including sound macroeconomic management, structural policies, policies for social inclusion, public-sector management and institutions. This has not prevented them from operating in poorly performing countries, post-conflict countries and other unfavourable environments. In such circumstances they adopt approaches that are less flexible and more project- than programme-oriented. IFAD's concerns relate more to the microeconomic level, local governance and empowerment and participation of the poor, especially poor rural women, which requires specific performance criteria. Thus the performance-based systems of other IFIs are not simply transposable to IFAD. As statistical information on strategic framework objectives becomes available, it will be integrated into the performance criteria in order to strengthen further, and make more systematic, IFAD's approach to resource allocation at the country level.

Box 2: Nigeria

Nigeria is the largest country in Africa in terms of population, a country with high levels of rural poverty. It is obviously a country where poverty-reduction needs are great. Yet during the 1980s and most of the 1990s, when the country was ruled by autocratic military regimes, it would have been hard to argue that macro-level economic and governance performance qualified the country for substantial development aid. Most donors simply pulled out. IFAD-supported projects are designed on the basis of local institutional capacity and opportunities for the rural poor to enhance their productivity and output. Their implementation and impact depends on the micro-level environment. In fact, the performance of IFAD projects in Nigeria proved to be quite good.

The Cassava Multiplication Project (1987-97) achieved notable success. It made improved cassava varieties available to farmers, thus significantly contributing to much higher production – this during a period when demand for cassava products was strong as the result of a ban on rice imports and falling urban incomes, which led to substitution of higher-priced food staples by cassava. The Sokoto and Katsina State Agricultural and Community Development projects (1993/94-2001) successfully pioneered participatory approaches to community development and reaching women. The Artisanal Fisheries Development Project (1994-97) introduced improved fish-smoking devices that have been widely adopted in southern Nigeria, reducing post-harvest losses and improving income generation.

In 1998, when the country returned to civilian rule, IFAD in view of its extensive experience and track record in Nigeria, was in a good position to launch relatively rapidly a new programme in response to the more favourable overall conditions created by the new Government. Project completion reports summarizing findings on the two Katsina and Sokoto projects were followed by a participatory process to develop a new COSOP, which the Board reviewed in April 2001. The document concluded that IFAD should concentrate on community development, rural decentralization, natural resource management and smallholder development. The primary focus of IFAD is on building social capital and establishing processes that strengthen pro-poor institutions and financing mechanisms geared towards participatory governance, which is a precondition to accountability. Since then, two new projects have been approved and two are under design.

Nigeria is an example illustrating the importance of the micro environment for IFAD-type rural poverty programmes. Some of those who advocate performance-based criteria concentrate on macro-level performance and criteria. These are certainly important, but for IFAD-type projects, the environment at the micro-level and local institutional capacity is as, if not more, important. Moreover, successful participatory rural poverty programmes can contribute to strengthening capacity and governance at the local level and enhancing the voice of poor groups in community-level decision-making. Such poverty programmes at the local level can provide building blocks for improving governance more widely. Had IFAD relied primarily on macro-level performance criteria, it would probably have led to the suspension of its Nigeria projects. This would have disrupted the interventions described above, which proved successful and have allowed a rapid development of a project pipeline after the return to civilian rule.