

**PROJECT INFORMATION DOCUMENT (PID)
CONCEPT STAGE**

Report No.: AB1794

Project Name	Agricultural Competitiveness and Sustainable Rural Development
Region	LATIN AMERICA AND CARIBBEAN
Sector	Agricultural extension and research (50%); General agriculture, fishing and forestry sector (50%)
Project ID	P086626
Borrower(s)	GOVERNMENT OF ECUADOR
Implementing Agency	Ministry of Agriculture
Environment Category	<input type="checkbox"/> A <input checked="" type="checkbox"/> B <input type="checkbox"/> C <input type="checkbox"/> FI <input type="checkbox"/> TBD (to be determined)
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1. Key development issues and rationale for Bank involvement

Sector Background: Agriculture is just too important as an economic sector to be ignored not only because of its dominant role in rural areas but also because it has significant forward and backward linkages to the rest of the economy and is a major generator of export income. Agriculture contributes up to 10 percent of GDP, some 46 percent of all exports, and is the main employment sector. Aside from traditional export crops such as banana, coffee and cacao, the agriculture sector has successfully been expanding the production of non-traditional export crops such as flowers, broccoli, hearts of palm, pineapple, and passion fruit. *Increasing agricultural and rural productivity should be a key element in the development strategy of Ecuador.*

Productivity levels are low compared to other countries in Latin America, particularly in cereals, pulses, tubers, and other traditional staples. Ecuador's productivity in traditional export crops is also below that of most of its competitors. Various factors have historically contributed to this, including weak ancillary services, high protection, a very unequal land tenure system, weak organization of producers, and weak integration of value chains. Political and economic instability in the country have also contributed. Low productivity prevents Ecuador from taking full advantage of its rich and diversified natural resources endowment, reduces agricultural competitiveness, and is a major factor explaining the persistence of rural poverty, which in 2001 encompassed 62 percent of the rural population of the *Sierra* and 50 percent of that of the *Costa*.

Falling behind its neighbors in agricultural competitiveness¹. The figures below highlight the weak performance of the Ecuadorian agricultural sector compared to its neighbors, Colombia and Peru, in terms of its overall growth rate as well as on crop yields.

Agricultural and Non-Agricultural Growth Rates 1970-99

	Agricultural	Non - Agricultural
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¹ The figure is from the 2000 Ecuador agricultural census and FAO that were used in the "Flagship Report". The second figure is from the Andean Community Database as cited in the World Bank's Ecuador Rural Development Strategy (2005).

Ecuador	0.7	5.1
Colombia	1.9	4.3
Peru	2.1	2.2

Yields for major crops (ton/ha, 2003)

	Ecuador	Colombia	Peru
Maize (yellow)	2.32	3.61	3.92
Maize (white)	0.64	1.66	1.25
Rice	3.84	5.02	6.79
Bananas	26.69	33.32	n/a
Coffee	0.29	0.90	0.69
Potatoes	8.82	17.53	12.21
Tomatoes	14.66	26.04	29.10
Oranges	8.00	12.38	12.73

Ecuador faces new conditions for competitiveness due to dollarization and trade liberalization following free trade agreement (FTA) negotiations with the US and other trade partners. Although dollarization generates greater macroeconomic stability it also entails a loss of flexibility in the Government of Ecuador's ability to deal with external shocks, taking away the option of devaluation as an "easy" method to redress balance of payments disequilibria and increase competitiveness. The FTA being negotiated with the US may open new opportunities for non-traditional exports to the US market but is also likely to increase the flow of cheap US staples to Ecuador. Even in the absence of this agreement, an increased trade opening of Ecuador's agriculture seems an unavoidable reality which is bound to modify competitive conditions.

For a highly tradable sector like agriculture to successfully face the new situation, a big leap forward in the basic conditions of competitiveness is required. Critical in this aim is the improvement of ancillary services, in particular technology research and transfer, rural finance, sanitary and phytosanitary services (SPS), market information, and input supply. Other areas where improvements are needed include: land tenure security and an adequate functioning of land markets; strong economic coordination between producers, processors and exporters or wholesale buyers along the value chains; and an adequate organization of producers according to their lines of specialization. Since many of these services and systems are public goods by nature or require strong public-private cooperation, improving the institutional capacity of the public sector to develop the systems or provide the services is another requirement.

In a very dualistic agricultural economy such as Ecuador's, where small and semi-subsistence producers coexist with medium-size commercial farmers and large plantation-type farms, often in the same line of business, **there is a strong risk that the opportunities and threats implicit in the new conditions be very asymmetrically distributed.** Poorly endowed producers may have to share in the burden of the adjustment while being bypassed by the new opportunities. For the impact of the new conditions to be equitably distributed among rural sectors, special efforts are needed to ensure that the improvement of the above services and systems reach the lower echelons of the farming community.

The proposed project will support the Government of Ecuador (GOE) in increasing competitiveness in the agricultural sector to successfully and equitably face the new conditions. The possible areas of intervention, which are many, are examined in the Ecuador Rural Development Strategy

document prepared by the World Bank, and have been summarized above. The project, however, will be selective, due to scope limitations deriving from fiscal constraints, and to the need to keep operations simple in view of limited implementation capacity of the Ministry of Agriculture (MAG). The areas of interventions selected for the proposed project consist of (1) supporting small farmers to become more competitive and benefit from the new opportunities by diversifying and intensifying their production through the building of strategic alliances with processors, exporters or wholesale buyers, (2) improving governance and technology in selected value chains, and (3) enhancing some areas of MAG that are considered key for competitiveness. The selection of these areas reflects (a) GOE priorities for the project, (b) comparative advantages for Bank interventions under current circumstances in Ecuador, (c) poverty reduction concerns, and (d) recommendations made in the Ecuador Rural Development Strategy document of the Bank.

Rationale for Bank Involvement. Four main reasons justify Bank involvement in this project:

1. **Acquired advantages in the country.** The Bank has considerable knowledge of agriculture and rural development issues in Ecuador relevant to the proposed project's objectives. This experience has been acquired through projects like PROMSA, SICA, PRODEPINE and PROLOCAL, and through the preparation of a Poverty Assessment Document and a Rural Development Strategy. The Bank has also experience in working with MAG.
2. **Value added.** The Bank can bring value added in the form of international experience relevant to the proposed project, as acquired through its analytical activities and through projects related to institutional support, agricultural knowledge systems, and support to improve competitiveness of small farmers in various countries in the region (Bolivia, Brazil, Chile, Colombia, Mexico, Nicaragua and Argentina).
3. **Continuity.** The Bank's involvement can ensure continuity in the efforts to improve governance and technology in value chains, and provide support to small farmers to become competitive. Continuity in these efforts is particularly relevant in view of the general political instability of the country and the instability in the senior management of the agricultural public sector.
4. **GOE Request.** GOE has requested the Bank's support in this area.

Government Strategy. GOE has recently completed through an Inter-Institutional Commission under MAG's leadership the systematization of various initiatives conducted in recent years by key stakeholders to define development priorities and policies for the sector. This resulted in the adoption by executive order on May 18, 2006 of a long term policy strategy for the sector articulated in the document "Políticas de Estado para el Sector Agropecuario Ecuatoriano 2006-2016". The concept and specific proposals of the present project are strongly consistent with the adopted policy which includes the improvement of agricultural profitability and competitiveness among its key objectives. The proposed CADERS project is seen by GOE as an important instrument to operationalize and implement the state's agricultural policy.

Support to CAS Objectives. GOE's request for a project to support agricultural competitiveness is included in the CAS which cites improving agricultural productivity, providing financial services to the poor, and supporting agriculture research as key elements of the Bank's program in Ecuador. The proposed project is listed in the CAS program matrix for an estimated amount of US\$80 million. However, due to the limited fiscal space existing in the country, a much reduced scope is being considered for the proposed project that is likely to amount around US\$25 million (of which an estimated US\$20.0 million IBRD loan).

Lessons Learned from AAA and Previous Bank Projects. The project concept is fully in line with the 2005 Rural Development Strategy prepared by the Bank, which identified the need for public investment to increase small farm competitiveness, improve value chains, and enhance MAG in order to assist farmers to meet current challenges and benefit from new opportunities.

Lessons learned from similar Bank-financed projects in the region (including the PROMSA and SICA² projects in Ecuador) include:

1. Competitive funds are a useful mechanism to allocate resources for research, technology transfer, farm modernization and other investments, which have been successfully adopted in Ecuador.
2. There is need to articulate closely the processes of generation and transfer of agricultural technology.
3. The methods for technology generation and transfer should ensure that benefits reach a large number of producers. Also, to be effective, they should clearly respond to the technology needs of the value chains.
4. There is an important demand for information from individual farmers and value chains. Information systems should facilitate exchanges among rural actors conducive to collective action such as the signing of competitiveness agreements and other mutually beneficial arrangements within the chains.
5. The *Consejos de Cadena* are useful economic coordination mechanisms, whose operation should be widened and strengthened particularly at the regional level.
6. Due to the institutional instability of the country and fast staff turnover, it is important to ensure high technical capability and continuity of project teams. Autonomous PIUs, however, have shown to be little conducive to country ownership and sustainability.

Other Partner Activities. At present, there is one project operating within MAG that is funded by a multilateral agency, IDB: the *Proyecto de Regulación y Administración de Tierras* (PRAT). PRAT is a US\$15 million project to regularize land tenure in pilot municipalities that started in 2003. Other relevant projects with donor funding in the pipeline, include: (a) the IFAD-funded US\$15 million *Corredor Central* project, a rural development (RD) project approved by IFAD's Board but not yet operational that targets a strip of rural municipalities in the central part of the country, (b) a Government of Belgium-funded Euro 12 million RD project designed to operate in the northern and north-western part of the country; an IDB-supported US\$7.5 million project with SESA to enhance SPS services, currently under preparation and scheduled to go to IDB's Board for approval in October 2006; and another IDB-funded US\$7.5 million project to support small rural businesses, also going to its Board in October 2006.

The IDB project to support SESA is strongly complementary to the proposed CADERS project since good SPS services are an essential ingredient of agricultural competitiveness. It is fortunate that this project is under preparation because it will cover an important need that would otherwise be difficult to address with the limited resources available for the proposed operation. *Therefore, CADERS proposal will not include activities related to the provision of SPS services.*

The other three projects in MAG's pipeline have strong complementarities with the proposed CADERS in the area of support to small farmer competitiveness. Altogether, the three projects have some US\$14 million earmarked for this purpose. This is a small amount compared to needs, hence leaving plenty of space for including a component to support small farmer competitiveness under the proposed CADERS project (some US\$9-11 million). However, having four donor-supported projects operating simultaneously in the country with comparable target groups will pose challenges that will require a strong coordination among the involved agencies. In addition, the IDB project also overlaps with the present proposal in the area related to the support to value chains. MAG, MEF and the relevant

² The *Proyecto de Modernización de Servicios Agropecuarios* (PROMSA), completed in January 31, 2005, covered agricultural research, extension and sanitary aspects, the first two components financed by the World Bank and the latter by IDB. The *Servicio de Información del Censo Agropecuario* project (SICA), also completed in January 31, 2005, was instrumental in the development of agricultural information systems, the strengthening of chain organizations, and the examination of agricultural foreign trade issues.

donors are aware of the potential problems involved and of the need to ensure the articulation of the projects before they begin operating. The discussion of the best way to articulate these projects has already started and will continue during project preparation. MAG has written to the Ministry of Economy and Finance indicating its preference that IDB focus its assistance on supporting SESA. This is an issue where the team seeks guidance from the review meeting.

Evidence of Borrower's Interest. MAG has shown commitment to the improvement of agricultural competitiveness through its efforts in recent years to strengthen value chain organizations, agricultural information systems, research and technology transfer systems, and sanitary and phytosanitary systems, *inter alia*. PROMSA and SICA were instrumental to these activities. Notwithstanding these efforts, weaknesses in these areas are still large, and there is need to sustain the investment efforts and maintain the policy commitment. Also, as indicated before, GOE has adopted a long-term state policy and strategy for agriculture. Other Government efforts to improve competitiveness are the creation of the International Trade and Investment Council (COMEXI) and the Export Promotion Corporation (CORPEI). Finally, a PHRD grant was requested by GOE to prepare the project and is already in place.

2. Proposed Project Development Objective(s)

The proposed project will promote agricultural competitiveness through (i) helping small producers to form and operate productive alliances with processors, exporters and wholesale buyers, (ii) improving governance and technology development in selected value chains, and (iii) assisting MAG in carrying out institutional improvements in key areas related to competitiveness.

3. Preliminary Project Description

The total project cost is estimated at US\$25 million, of which a Specific Investment Loan (SIL) of US\$20 million is proposed.

Proposed Components

Component 1: Promotion of Production Alliances (US\$9 to 11 million)³

This component will assist small producers to set up or expand strategic production alliances with processors, exporters and wholesale buyers. It has two subcomponents:

- **Subcomponent 1.1: Organizational Support to Production Alliances.** This subcomponent will support the establishment of alliances between small producers and processors, exporters and wholesale buyers in selected geographic areas and/or lines of production. This includes project information dissemination, organization of producer groups, support to the formalization of the alliances, and technical assistance and training to prepare and implement alliance business plans to enhance competitiveness.

³ By **productive alliances** we refer in this document to agreements established between groups of producers and prospective buyers. The buyer could be a processor, an exporter, a supermarket or another type of wholesale buyer. The agreement would normally require producers to supply a certain amount of produce of established quality with certain regularity. It would normally also indicate a commitment from the buyer to buy that quantity at a certain price. The alliance may include other things such as the provision by the buyer of certain inputs, credit or technical assistance; a commitment from producers to use agreed sanitary practices in the production process or in the post-harvest; an agreement to share price risk between buyer and sellers in certain ways; an agreement to increase the amount produced/bought over time; etc.

- **Subcomponent 1.2: Funding of Alliance Business Plans.** This component will establish a financing mechanism to help implement the alliances' business plans. This will be done through a competitive fund. The fund will finance technical assistance, training, farm equipment, processing equipment, inputs, working capital, and other supporting investments required by small producers to participate in the alliances. The competitive selection process will consider *inter alia* the commitment of the partners downstream of the value chain to enter into the alliance, the profitability and sustainability of the activities proposed, the cost of the investments required, and the returns to labor generated. The alliances to be supported should help intensify and/or diversify production by small farmers. Financing from the fund will consist of matching grants, with producers co-financing the investments required by mobilizing other financial sources (credit, own resources, supporting funds from NGOs or other government programs, funding from the partner in the alliance, etc.).

Component 2: Strengthening Governance and Technology Development in Selected Value Chains⁴ (US\$5 to 7 million)

This component will enhance the competitiveness of selected value chains at national and/or regional level through improved governance as well as technological innovation. It will build on progress made by SICA and PROMSA.

Technical assistance will be provided by the project to value chains for (i) improving the functioning of consultative councils, preparing strategic plans, examining competitiveness issues within the chains, identifying technology and investment needs, representing the interests of the chains, implementing conflict resolution and price negotiations mechanisms, and others; (ii) supporting small producer associations to increase their active participation and strengthen their negotiating capacity within the chains; and (iii) designing and promoting mechanisms, such as *parafiscalidad*, to increase the financial sustainability of producer associations. Diagnostic and planning work will be carried out using participatory methods.

This component will also establish a matching grant fund to support innovations to address the strategic technological constraints of the selected value chains at regional and national levels. The mechanism will be flexible and will finance proposals which may combine applied research, technology dissemination, and farmer training. Priorities will be established according to guidelines to be defined during project preparation based on criteria reflecting aspects such as poverty reduction, competitive advantage, technological need, feasibility, potential impact, and market demand considerations.

Component 3: Institutional Strengthening of MAG (US\$2 to 3 million)

This component will provide support to the Ministry of Agriculture to widen and modernize its operations in key functions related to competitiveness. The areas selected for support are: (a) the formulation and monitoring of sectoral policies, including the negotiation of commercial agreements; (b) the provision of accurate and timely agricultural statistics (structural, continuous production data, producer prices, market information, and industry consumption of agricultural products), building on the work done by SICA; (c)

⁴ We refer to **value chains** in this document in the sense of *supply chains*, that is, coordinated systems of entities, activities, information and resources involved in moving a product or service from supplier to customer. The entities of a chain typically consist of primary producers, service providers, processors, distributors, and retail outlets. The policy in Ecuador, as in many other LAC countries, has been to assist food and agriculture-related producers to organize themselves in value chains coordination entities, usually called *Consejos de Cadenas*, according to their line of business. The SICA project was directly involved in providing assistance to these coordination entities. The value chain concept was described and popularized by Michael Porter in his book, Competitive Advantage: Creating and Sustaining Superior Performance, New York, NY, The Free Press, 1985.

the planning and monitoring of special programs and projects; and (d) the improvement of the legal and normative environment for agriculture competitiveness and trade development. The project will finance technical assistance, training, software, relevant equipment, study tours, surveys, and the like.

Component 4: Project Management (US\$1 to 2 million)

This component will support effective project management, monitoring and evaluation. It will finance the provision of technical assistance, goods, equipment and incremental operating costs to support the establishment and operation of a project coordination team within MAG, the setting up and operation of a management information system (MIS), and the implementation of M&E and learning arrangements. The component will also ensure that effective fiduciary arrangements are in place during implementation.

4. Safeguard policies that might apply

To be developed.

5. Tentative financing

Source:	(\$m.)
BORROWER	5
INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT	20
Total	25

6. Contact point

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