This section looks at the history of IFAD operations and lessons learned from project experience. It also begins to outline some of the strategic considerations and priority areas for future operations.

**Regional Portfolio**

**Overview.** IFAD expanded its portfolio in the early and mid-1990s to include CEN borrowers. As of mid-2001, the Fund had supported 17 investment projects in the region: nine of which are currently under implementation; five that have been approved but are not yet effective; and three projects that have been closed. An overview of this portfolio is given in Table 7; summary details of all approved projects are given in Appendix II.

In considering the development of this portfolio, it is useful to identify two generations of project interventions. Until about 1996, most first-generation loans were actually World Bank-initiated, with IFAD joining as a cofinancier. The only exceptions to this are the first two investment projects in Albania (approved in 1993 and 1994), which were IFAD-initiated; and the first project in Georgia, which was World Bank-initiated but approved in 1997. Although the World Bank did not directly finance the two loans to Albania, it did cooperate closely with IFAD in the definition of areas of operational responsibility and a country strategy.

As a cofinancier of these early investments, a prime responsibility of IFAD was to

<table>
<thead>
<tr>
<th>Country</th>
<th>Total Projects</th>
<th>Project Type by Order of Executive Board Approval</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Ongoing</td>
<td>Closed</td>
</tr>
<tr>
<td>Georgia</td>
<td>2</td>
<td>Agriculture (2001).</td>
</tr>
<tr>
<td>Romania</td>
<td>1</td>
<td>Credit (1999).</td>
</tr>
<tr>
<td>The Former Yugoslav Republic of Macedonia</td>
<td>2</td>
<td>Credit (1997), Credit (2000).</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>14</strong></td>
<td>Credit 6; Agriculture 5; Irrigation 3; Other 3.</td>
</tr>
</tbody>
</table>

Notes: Ongoing includes approved projects not yet effective; project type defined by the Project and Portfolio Management System (PPMS) classification.

ensure that the overall design and implementation arrangements of each project adequately addressed the needs and concerns of the rural poor. A good example of this approach is the first investment loan to Armenia, where the World Bank financed the rehabilitation of primary and secondary irrigation canals and pumping stations, while IFAD worked with local communities to manage tertiary distribution networks.

As it gained experience in the CEN region, IFAD began to initiate projects on its own that now focus at least as much on the process of development as on actual physical output. These second-generation projects have mostly adopted a specific and long-term focus on institutional development. The three most recent mountain area development programmes in Albania, Azerbaijan and Georgia, for example, all include mechanisms to foster cross-sector representation and help coordinate regional, national and international development policies. IFAD’s approach to credit projects in the region has also clearly evolved. Specifically, whereas most first-generation projects either distributed credit through government channels or an individual bank nominated for this purpose, the emphasis now is to promote competition among private banks for the development of more sustainable financial services.

**Project financing.** As summarized in Table 8, total IFAD lending to the region amounts to USD 177.6 million thus far, and the total value of all projects including, cofinancing, and government and beneficiary contributions, is USD 379.5 million. In other words, for every dollar that IFAD has invested in the region, it has mobilized an additional USD 1.14 in total project financing. The average value of the 17 IFAD loans to the CEN region is USD 10.5 million, with individual investments ranging from USD 6.6 million to 16.5 million. Total project costs, including cofinancing, range from USD 9.2 million to 57.2 million.

In terms of project spending per capita, these data show that IFAD has invested USD 3.33 for every individual in the CEN region and USD 7.65 for every rural inhabitant. In terms of the rural poor, this works out to a total per capita investment of USD 14.48 (based

<table>
<thead>
<tr>
<th>Country</th>
<th>Approved Financing (USD '000)</th>
<th>IFAD Financing Per Capita (USD)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>IFAD</td>
<td>Total</td>
</tr>
<tr>
<td>Albania</td>
<td>34 290</td>
<td>52 109</td>
</tr>
<tr>
<td>Armenia</td>
<td>36 474</td>
<td>92 703</td>
</tr>
<tr>
<td>Azerbaijan</td>
<td>18 300</td>
<td>38 814</td>
</tr>
<tr>
<td>Bosnia and Herzegovina</td>
<td>33 330</td>
<td>78 122</td>
</tr>
<tr>
<td>Georgia</td>
<td>14 570</td>
<td>36 331</td>
</tr>
<tr>
<td>Republic of Moldova</td>
<td>8 000</td>
<td>19 510</td>
</tr>
<tr>
<td>Romania</td>
<td>16 464</td>
<td>34 110</td>
</tr>
<tr>
<td>The Former Yugoslav Republic</td>
<td>16 192</td>
<td>27 767</td>
</tr>
<tr>
<td>Republic of Macedonia</td>
<td></td>
<td>379 466</td>
</tr>
</tbody>
</table>

**Source:** PPMS (30 June 2001).
on USD 4.30 per day poverty line), or just USD 1.61 per person per year in the nine years since the first loan to the region was approved. Although individual projects can still have a direct and significant impact on specific groups of project beneficiaries, these calculations suggest that IFAD projects alone are unlikely to have a major impact on the overall incidence of rural poverty. Rather, as a relatively small financing institution, IFAD’s comparative advantage in the region rests with its ability to identify new approaches and demonstrate areas of success for broader application.

### Table 9: Project Cofinancing in the CEN Region

<table>
<thead>
<tr>
<th>Projects Supported</th>
<th>Total Contribution (USD ‘000)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Albania</td>
<td>5 211</td>
</tr>
<tr>
<td>Armenia</td>
<td>5 554</td>
</tr>
<tr>
<td>Azerbaijan</td>
<td>5 000</td>
</tr>
<tr>
<td>Bosnia and Herzegovina</td>
<td>234</td>
</tr>
<tr>
<td>Georgia</td>
<td>763</td>
</tr>
<tr>
<td>Republic of Moldova</td>
<td>1 000</td>
</tr>
<tr>
<td>Romania</td>
<td>800</td>
</tr>
<tr>
<td>The Former Yugoslav Republic of Macedonia</td>
<td>800</td>
</tr>
</tbody>
</table>

#### Multilateral Donors

- European Union: 5 211
- Islamic Development Bank: 5 554
- OPEC Fund: 5 000
- UNDP: 234
- World Bank/International Development Association (IDA): 93 724
- Total: 109 723

#### Bilateral Donors

- Germany: 4 680
- Netherlands: 896
- Netherlands Development Organisation (SNV): 763
- Saudi Fund for Development (SFD): 1 000
- Swedish International Development Cooperation Agency (SIDA): 800
- United States Agency for International Development (USAID): 10 000
- Total: 18 139

#### Domestic Financiers

- Project beneficiaries: 22 344
- Government (national): 27 633
- Local financial institutions: 10 893
- Local NGOs: 612
- Local private-sector: 1 100
- Other domestic sources: 1 049
- Total: 63 631

#### To Be Determined

- 10 353

Table 9 shows that IFAD has successfully initiated collaborative relations with a wide range of project financiers. In most cases, the data indicate that multilateral and bilateral agencies have preferred to focus their support on one or two countries, and there is now a good opportunity to cement these relations and introduce a more programmatic approach for funding new project investments. It is important to note that – in addition to project beneficiaries and borrowing governments – local financial institutions, non-governmental organizations (NGOs) and other private-sector sources have made substantial contributions to project costs in most countries, thereby increasing local ownership and prospects of long-term sustainability.

**Strategic Lessons**

Compared with other regions where IFAD operates, there are only a few investment projects in the CEN region from which to draw substantive lessons. The first loan to the region was approved only in 1993, and most projects are still ongoing. As shown in Table 7, only three projects in the CEN region have been closed and this includes a short-term emergency rehabilitation project in Bosnia and Herzegovina. Nevertheless, most other donors are also new to the region, and IFAD has established itself as a successful leader in the field of rural poverty alleviation and agricultural development. Despite these limitations, it is useful to review IFAD’s experience in the region so far as a step towards developing a more effective lending programme.

**Institution-building.** Most IFAD projects in the region have focused, either directly or indirectly, on institutional development. Of the 17 investment loans supported to date, six projects have been for the development of rural financial services, five for agriculture development and three for irrigation. Of the agriculture projects, three loans (to Albania, Azerbaijan and Georgia) include support for the establishment of mountain area development agencies. Likewise, an important focus of all three irrigation projects, and irrigation components of other projects, has been to build local management capacity through support for beneficiary-led water users’ association (WUAs). IFAD has also provided support to local and national governments in managing the process of agricultural privatization and land registration (in Azerbaijan and Georgia).

As discussed, the institutional vacuum caused by the collapse of central planning and state socialism contributes substantially to rural poverty in the CEN region. Successful projects, therefore, need to be based on a long-term strategy for building and strengthening new institutions, and also designed in a sufficiently flexible way to cope with current weaknesses. Most projects in the region have been slow to start up (because of the weak institutional base) but have made good overall progress in institutional development and capacity-building. Progress has been especially good for projects with direct supervision and/or persistent follow-up by IFAD country portfolio managers (CPMs). Experience, therefore, demonstrates the need for flexibility, technical support and intensive management support in project design and implementation. Projects in transition countries are also increasingly being prepared from a long-term perspective using a programmatic approach to help create the conditions needed for sustainable development.
IFAD’s experience also shows that special attention must be given to legal provisions. In Armenia, for example, a main focus of IFAD operations is to support the establishment of WUAs, but local laws do not yet allow the registration of non-profit organizations, thereby preventing each association from opening a bank account in its own name. In Georgia and Azerbaijan, IFAD’s approach to this type of problem has been to work with national and local governments to develop temporary legal arrangements for both land registration and the establishment of savings and credit associations. Based on lessons learned in implementing the new regulations, IFAD then engaged in dialogue with government to identify the best policies and procedures to be included in formal legislation. Again, these experiences all point to the need for intensive CPM and/or consultant follow-up to support implementation of project activities.

Mountain area development. Because of the severity of rural poverty in upland and mountain areas, many IFAD projects in the CEN region focus specifically on these locations. In addition to the credit projects in Romania and The Former Yugoslav Republic of Macedonia, past and ongoing projects in Albania, Armenia and Bosnia and Herzegovina have all targeted mountain area communities. Recently, the first jointly formulated IFAD project to cover two countries was approved for the mountain areas of Azerbaijan and Georgia.

While the emphasis on mountain areas can be justified by the high incidence of poverty in these locations, project experience shows that significant difficulties can be encountered in promoting sustainable market-led development in mountain areas, because of their isolation, poorly developed infrastructure and narrow agricultural resource bases. Therefore, instead of defining mountain areas by altitude alone, IFAD has found that a more systemic approach, based on how mountain communities interact with other parts of the national economy, is critical for success. This lesson became particularly evident during implementation of the Southern and Eastern Regions Rural Rehabilitation Project in The Former Yugoslav Republic of Macedonia, which first restricted the use of credit funds to specific disadvantaged mountain areas. Because of the narrow physical and human resource base in these areas, there was little demand for credit and disbursement rates were slow until a decision was made to expand the project area.1 Similarly, more than a year and a half into implementation of the Apuseni Development Project in Romania, disbursement of credit funds is very slow, partly because of the focus on specific disadvantaged mountain areas.2

For future mountain area projects to succeed, therefore, the unique challenge of working in these locations must be explicitly recognized as a design consideration. On this basis, IFAD is increasingly adopting a long-term programmatic approach to mountain area development. In Albania, it will support the establishment of a mountain area development agency to serve as the institutional means of approaching development on the basis of the distinct social and economic structures and systems of mountain areas. Similarly, the new Rural Development Programme for the Mountainous and Highland Areas, covering both Azerbaijan and Georgia, has adopted a long-term focus on shared development goals and seeks to promote international dialogue and new project approaches based on lessons
learned. This new approach to mountain area development is an ambitious undertaking for IFAD, and represents a clear effort to build on the lessons from past experience by moving away from the spot application of area-based subsector projects.

**Rural financial services.** Another important area of IFAD operations in the CEN region has been to support the development of rural financial services. As shown in Table 7, roughly one third of all IFAD projects in the region focus primarily on rural credit. Nearly all other projects have also included a credit component, including all three investments in Albania, the two most recent projects in Armenia and the new joint project for Azerbaijan and Georgia. Pilot credit schemes have also been included in the two projects in Bosnia and Herzegovina relating to farm reconstruction, and the most recent project in that country includes funds for both microfinance and long-term capital investment. These projects give IFAD considerable experience with rural credit in the region and provide a sound basis for policy dialogue on financial services that support the rural poor.

As with other focal areas, IFAD’s approach to rural credit in CEN countries has evolved over time, based on lessons learned. Its early approaches mainly emphasized rapid credit distribution, which was believed to be what newly privatized farmers needed most. In practice, however, the lack of sufficiently developed legal and regulatory frameworks made it difficult to target specific groups of beneficiaries and also to ensure adequate repayment. In Georgia, for example, credit unions, established under a temporary regulation, also served as the focal point for other government services and so lacked a clear identity and an adequate emphasis on financial discipline. In Bosnia and Herzegovina, it was decided that elected officials would choose the beneficiaries of livestock loans, and a single bank was selected to manage the credit component. Especially in the post-war environment, these arrangements caused credit to be seen mainly as a handout rather than something that had to be repaid. In Albania, IFAD partially compensated for the lack of a sufficiently developed regulatory framework by working through village credit funds as a simple way to ensure repayment through joint liability.

Taken together, these experiences pointed to the need for a long-term institutional focus and a clear separation from government as a service provider. Towards this end, second-generation credit projects in the Republic of Moldova, Romania and The Former Yugoslav Republic of Macedonia have been designed to support a central fund against which participating banks can borrow at discounted rates for lending to eligible beneficiaries. This approach not only aims to provide smallholder farmers and other entrepreneurs access to investment finance and working capital, but also allows participating financial institutions to acquire the agricultural lending experience needed for long-term growth and development. It also provides a clear way of shifting the credit risk over to private banks through variable interest rates. On the other hand, this approach demands relatively sophisticated management capacity and it is not yet certain that financial incentives alone are sufficient to attract new banks to develop specific services that target the beneficiary groups of primary importance to IFAD. Therefore, future credit projects may need to consider additional mechanisms that help direct credit funds for
strategic purposes, including development of market-driven input supply networks, long-term capital investment, trader credit and support for other non-farm rural services.

Another important lesson from IFAD’s credit projects in the CEN region is that considerable attention is still needed to develop the capacity for appraisal of individual loan applications. As discussed in Chapter II, bank officials in the region have almost no experience in the financial evaluation of small-scale investment loans, which is a serious constraint both to the uptake of credit and its effective use by project beneficiaries. Under the Farm Privatization Project in Azerbaijan, for example, unwieldy application, appraisal and disbursement procedures for small working-capital loans led to high transaction costs and deterred the uptake of credit by farmers. In other cases, insufficient attention was given to the overall viability of the proposed investment; and in The Former Yugoslav Republic of Macedonia some farmers are now finding it difficult to repay their livestock loans because of poor cash flow. Clearly, a balance needs to be struck between requirements for complex business plans and an adequate assessment of the overall viability of each proposed investment.

Market linkages. The main focus on market development in CEN countries has been to support the formation of producer groups, village-level dairy processing and provisions for trader credit through financial services projects. Although these initiatives are all important steps in the right direction, considerably more effort as well as an explicit recognition of the unique challenge of promoting market-led agricultural growth are needed to facilitate the transition from subsistence agriculture to market-based production. Especially in mountain areas, the development of sustainable and remunerative market outlets for smallholder produce has proven extremely difficult due to the physical isolation of these areas, their limited resource base and the high costs of transportation.

In this respect, experience from the CEN region shows that long-term success requires much more than improved on-farm productivity and that the ability of farmers to have access to and compete in output markets must also be considered in project strategies. Although the focus of early IFAD projects on productivity made good sense in the immediate post-transition period, the challenge now is to consolidate these efforts through the development of new market linkages for farm produce. Especially as CEN countries seek to develop economic ties with western Europe and other industrialized country markets, attention must be paid to product mix, quality and presentation to ensure better targeting of farmer products.

At a minimum, this requires that future projects account for market opportunities and constraints. In Bosnia and Herzegovina, for example, initial livestock restocking efforts sought to reach the maximum number of households by providing a one-cow ‘subsistence’ package. Although post-war conditions may have necessitated this approach, it quickly proved to be unsustainable since farmers could not produce a marketable surplus of milk and were thus unable to repay their livestock loans. Similar problems have been encountered in many other countries of the region in that the vacuum caused by the collapse of the former state marketing system provides little incentive for farmers to produce beyond the requirements of household subsistence.
Support for small and medium-scale rural enterprises that add value to local produce offers excellent potential for the development of rural market linkages. In Albania, the IFAD-supported Mountain Area Finance Fund (MAFF) has recently expanded its operations from very small loans distributed to farmers through village credit funds to larger-scale credit (USD 5,000-20,000) for rural small and medium-scale enterprises (SMEs). In Kukes, the capital of a remote northern district, MAFF provided a two-month loan to a local raki distiller giving the woman owner working capital to buy plums and grapes from nearby farmers. As she explained, “We used to get working capital from the National Commercial Bank, but this has stopped operating in rural areas. Without MAFF, there was no way we were going to buy the materials we need to continue production. Now we offer a guaranteed price, and farm produce is coming in from Kukes and neighbouring districts.” A similar loan was made in the village of Fush Arrez, allowing a small-scale butchery to buy pigs for fattening and feed from local farmers.

Box 2: Small and Medium-Scale Enterprises and Rural Markets in Albania

Longer-term steps that minimize the risk of market-based production and support private-sector growth are also important. Specifically, it is clear that more explicit recognition is now needed of the opportunities for private traders and other commercial investors to become involved in IFAD project strategies. Experience shows, for example, that support for small and medium-scale enterprises (SMEs) can be an effective way of developing new market outlets for smallholder produce (see Box 2). Although relatively advanced owners of rural SMEs are not normally the primary target group of IFAD operations, the private sector clearly has an important role to play in developing the input supply and output markets needed for long-term growth and poverty reduction. For its programmes to be sustainable over the long term, therefore, IFAD will need to focus more on developing new, mutually beneficial relations between private traders and small-scale producers.

Group formation. Working through beneficiary groups has been one of the main ways to channel project services in the CEN region. Using participatory methods, this approach has helped ensure that IFAD projects directly address the needs of local communities and has also been a key strategy for local institution-building. Especially with regard to market development, producer associations can play an extremely important role by strengthening farmers’ bargaining power, helping to spread the cost of major investments and lowering transaction costs for private traders. Although IFAD’s experience with producer groups in the region has generally been positive, several lessons stand out with significant implications for project design and implementation.

First, rural people and local and national leaders in the CEN region tend to be cautious and sometimes even sceptical about the potential benefits of group formation. As discussed in Chapter II, there is a general mistrust of new forms of collective action, including producers’ associations and cooperatives. Although this approach could help address many of the constraints rural producers face, few cooperatives and other marketing groups exist in a pure form as their development has been difficult to separate from the historical, political and social legacy of communism.

Against this background, IFAD’s experience shows that groups formed with the clear
objective of managing a common resource are often the most successful. As noted earlier, credit unions in Georgia served multiple purposes, thereby undermining their role as a focal point for well-disciplined rural financial services. By comparison, where credit associations have been formed specifically for the purpose of group lending, as in Albania and Armenia, this approach helped build cohesiveness through improved access to much-needed financial services. Similarly, WUAs in Albania, Armenia, Azerbaijan and Georgia formed with a clear mandate to plan the rehabilitation of shared canals, manage irrigation schedules and collect user fees for ongoing maintenance have also been generally successful.

Borrower priorities. While specific priorities may vary quite substantially, most borrower governments have expressed a strong preference for programmes with a clear financial return. Consequently, IFAD has tended to focus on the development of rural financial services and project approaches that shift credit liability away from governments to participating financial institutions and beneficiaries. Similarly, many borrower governments have been reluctant to use IFAD loan money for capacity-building and farmer training since the returns from these investments are less tangible and more difficult to quantify. Because these services are often important for targeting the poorest social groups and for supporting long-term growth (including European Union integration), it has sometimes been necessary for IFAD to mobilize grant cofinancing for agricultural training and extension components. This has especially been the case for intermediate-term borrowers where the higher cost of finance provides an additional incentive to focus on programmes with a clear financial return.

Within these limitations, IFAD’s experience shows that there is good potential for meaningful dialogue with borrower governments on rural development strategy. As many CEN countries are relatively small, IFAD has been able to develop close relations with the new governments at some of the highest levels of national decision-making. Through open discussion on rural development policies, it has succeeded in fostering local ownership and consensus on strategies for rural poverty alleviation. Especially when targeting marginalized areas not covered by other donors (such as the mountain areas of Albania), IFAD has been able to have a more significant voice in helping to plan national development policy than would likely have been possible by cofinancing large-scale multisector development programmes.

Other cross-cutting lessons. Several other lessons with important implications for regional strategy and individual project loans stand out from IFAD’s experience in the CEN region. Briefly, these may be summarized as follows:

- Given their limited resource base and small size of farm holdings, the rural poor often have to generate a considerable share of their income through off-farm activities.
- Once farmers have met their basic subsistence requirements, they are unlikely to invest in further on-farm improvements until they are assured of secure and remunerative market outlets.
- Because the skills needed to support rural development and commercialization in agriculture are very different from those needed in the former command system,
adequate attention must be given to human resource development at the institutional level.

- Local institutions promoting the establishment of credit associations, WUAs and other beneficiary groups need to be able to provide adequate training and implementation support.

- Lack of adequate extension and animal health services can seriously undermine the capacity of project beneficiaries to absorb new technologies, including those relating to improved livestock breeds, improved seeds and other specialized inputs.

- Many farmers still use traditional methods and have only a limited understanding of which crop and livestock products and cropping patterns offer the greatest potential for growth and profit in the new market economy.

- In view of the rapidly evolving social, political and economic situation in transition economies, programme design should not be overly specific at the outset.

- Poorly developed infrastructure unsuited to the needs of today’s more dispersed populations (including roads, schools, health centres, electrical power and telecommunications) is often a major constraint to growth in the remote areas where IFAD operates.
IFAD EXPERIENCE IN THE REGION

Endnotes

1 IFAD, 1996; UNOPS, 1999a.
2 UNOPS, 1999b.
3 IFAD, 2000e.
5 IFAD, 1999d.
6 IFAD 2000c; UNOPS, 1999a.
7 IFAD, 2000b.
8 Milns, 1999.
9 IFAD, 2000e.
10 IFAD, 2000a, 2000c, 2000d.
11 IFAD, 1999d, 2000a, 2000e.
This final chapter builds on the preceding analysis and outlines a medium-term strategy for IFAD operations in the CEN region. This strategy is guided by the need both to maximize impact for specific targeted beneficiaries and to contribute to the Millennium Development Goals (MDGs).

**Strategic Framework for IFAD**

**Main objectives.** IFAD’s overall strategic objective in the CEN region is to support the transition process with sustainable agricultural programmes that contribute to rural poverty reduction. Progress in this regard can be measured at the macro level by agricultural growth rates, trends in household expenditure, reduced income inequality and other indicators of rural living standards and human development. Within this context, however, it is important to recognize that IFAD investments alone are unlikely to have a major impact on overall sector performance and incidence of rural poverty. As noted in Chapter IV, total IFAD lending to the region to date averages slightly less than USD 14.5 per rural person living below the poverty line. At this level of investment, IFAD’s strategy depends on building effective partnerships with others to achieve meaningful growth in agriculture and other sectors that support the rural economy.

As a member of the international development community, IFAD is also guided by the need to contribute to the MDGs, which set targets for reductions in poverty, improvements in health and education, and protection of the environment (see Box 3). These goals are a formidable challenge to IFAD and the international development community, especially in the CEN region where the incidence of poverty has increased sharply since the start of the transition, with a corresponding deterioration in health status, education and gender equality.

As a small and specialized financing institution, IFAD needs to address the MDGs by concentrating its resources on a few areas of strategic importance. Although IFAD investments alone are unlikely to have a major effect in terms of halving the total number of rural poor in CEN countries, individual projects can still be of significant benefit and demonstrate replicable approaches for wider application. IFAD’s main contribution to the MDGs, therefore, will stem from its ability to devise and test innovative approaches for rural poverty reduction and to promote dialogue at the national, regional and international levels on effective development strategies.

IFAD projects in the region can also make a significant contribution to gender equality and natural resource management, even though they may not directly address the specific criteria set out in the MDGs (elimination of gender disparity in primary and
secondary education, and development of national strategies for sustainable resource management). IFAD recognizes that gender equality and improved environmental conditions are essential for a sustainable reduction in rural poverty and will continue to work to improve these areas through policy dialogue and the projects it supports.

**Operational approach.** To achieve these broad development objectives, IFAD will focus on a few areas in each country where it has a distinct comparative advantage, and where it can leverage its resources for maximum impact and demonstrate replicable project strategies for broader application. In this respect, success will be measured more by the impact of specific projects on targeted beneficiaries than by macroeconomic change and an overall reduction in the number of rural poor. At this level, the impact of IFAD projects can be measured by changes in on-farm productivity and cropping patterns, by the volumes of produce sold for cash, and by growth in the non-farm rural economy (including agricultural services and commodity trade relevant to the rural poor). Success can also be measured by the uptake of project strategies by governments and other donors, thus enhancing impact and allowing for wider coverage.

In implementing this strategy, IFAD will continue to use a variety of instruments. These will include traditional project loans, technical assistance grants for agricultural
and economic research, IFAD/NGO Extended Cooperation Programme (ECP) grants to foster new partnerships and the growth of civil society, and Special Operation Facility grants to speed implementation and improve impact. IFAD’s technical assistance programme, for example, is not a stand-alone instrument. Rather, it mirrors the Fund’s broad development strategies and has been designed to support the regional lending programme by promoting relevant research and knowledge transfer. IFAD’s experience in CEN countries also demonstrates the need for flexibility and technical and management support in project design and implementation. This often requires intensive CPM and/or consultant follow-up, which implies that special attention must be paid to technical assistance requirements at the project design stage.

Future programme activities will also seek to build on past successes and continue to target neglected areas where IFAD can ensure maximum visibility and establish a platform for dialogue with borrower governments, other donors and civil society on topics of critical importance to the rural poor. This is especially true with respect to mountain areas, which are often neglected by other donors even though some of the poorest and most vulnerable people in the region are found in these locations. IFAD has also gained considerable experience with the development of rural financial services and is helping to pioneer new institutional approaches that ensure improved access of the rural poor to the working capital and investment resources they need for increased productivity and market participation. Likewise, the Fund has successfully worked with WUAs and other beneficiary groups formed with the clear objective of improving local access to development resources.

Although the specific focus of IFAD operations will vary from country to country, each programme will seek to address the underlying causes of poverty for the poorest and most vulnerable rural groups in the region. In the case of mountain communities, for example, project experience shows that this demands recognition of the unique challenge of working in these areas and special consideration of the opportunities and constraints for interaction with other parts of the national economy. The physical isolation of these areas in particular is likely to require close cooperation with governments and other donors to develop the physical and social infrastructure needed to support economic participation at the regional, national and international levels. IFAD operations must also be guided by recognition that many of the rural poor in CEN countries do not depend on agriculture for their main source of livelihood. Support for agricultural services, agro-processing and other areas of the non-farm rural economy, therefore, will be critical for a sustainable reduction in the incidence of rural poverty. Finally, with regard to the unique role played by women in rural households, and in an environment where male migration for work is an important household coping mechanism, IFAD operations must also seek to ensure that women have access to the proposed investments and are adequately represented in all relevant rural associations and institutions.

**Opportunities for IFAD Investment**

In terms of specific areas for project intervention, the preceding analysis shows that a focus on long-term institutional development and support for new market linkages
offer some of the best opportunities to leverage IFAD resources for maximum impact. Again, project strategies will vary from country to country, but these two areas are of almost universal importance throughout the CEN region since inadequate institutional support and poor market access both define and limit the opportunities to move out of poverty for the vast majority of rural people. Other strategic areas for IFAD intervention may include support for improved on-farm productivity, development of the non-farm rural economy and creation of sustainable natural-resource management systems. The Fund will address these areas in part through the development of rural financial services that channel resources directly to activities that benefit the rural poor and support other new areas of relevant trade and investment.

**Institutional development.** While the specific priorities to be pursued depend on individual country circumstances, a fundamental element of IFAD’s strategy throughout the CEN region will be to strengthen the institutional capacity of government departments, private financial institutions and civil society to address the needs of the rural poor. Within this context, IFAD will place considerable emphasis on helping beneficiary groups create their own local institutions (including WUAs, savings and credit associations and marketing associations) to address local needs and help harness essential development resources. This focus requires a long-term commitment and programmatic approach to the region, both to give existing institutions a sharper pro-poor focus and for building new institutions when needed.

In the planning of future project loans, the wide-ranging constraints posed by non-existent and poorly functioning institution, viewed from another perspective, offer opportunities in that development policies and institutional arrangements are still not fixed. The new openness and fluidity in social and political affairs gives IFAD an opportunity to influence the policies and operations of government institutions, particularly at the local level. An important part of IFAD’s strategy, therefore, is to build awareness at the national and international levels of the importance of agriculture for economic growth and poverty alleviation. Depending on country circumstances, this is likely to involve working in close cooperation with ministries of agriculture to strengthen their capacities to lobby other branches of government and the donor community on behalf of the rural poor for enabling legal reform and additional development resources.

Institution-building is also about developing the skills and sensitivities needed to support pro-poor development strategies and participatory processes. Future projects, therefore, will continue to work with relevant government ministries, extension departments, financial institutions and community leaders to build an understanding of the constraints and opportunities for market-led agricultural growth and necessary entrepreneurial skills. As the transition experience makes abundantly clear, legal reform is only the starting point of institutional development. Considerable work is now needed to build essential services and capacities that support the region’s new farmers and provide opportunities to participate in the cash economy.

**Market linkages.** Within the broad framework of institutional development, the principal emphasis of future IFAD loans will be to foster new market linkages needed to support
the transition process and help rural people use agriculture for more than mere subsistence. This will include support for private extension networks, rural financial services, input supply arrangements, contract farming, and producers’ associations that improve the bargaining power of isolated smallholder farmers and other rural producers. In many other parts of the world, IFAD projects have also sought to address the challenge of market development through support for market information systems. Although this approach could help farmers to some extent in the CEN region in deciding on the best crops to grow, the unusual challenge of transition, including the redistribution of land in small parcels and complete lack of a tradition in crop marketing, demonstrates that much more is required to build new market outlets and competitive mechanisms.

Specifically, as the CEN portfolio matures, it has become increasingly evident that a more explicit recognition is needed of the opportunities for private traders and other commercial investors to become involved in IFAD project strategies. The private sector clearly has an important role to play in developing the markets needed for poverty reduction, but it is unlikely to work with the rural poor unless this represents a secure investment. In this respect, IFAD’s strategy will be to serve as a catalyst for change by helping to create the linkages and financial services needed to foster the development of new relationships between the private sector and small-scale producers. IFAD can also help to put in place appropriate institutional arrangements that facilitate the establishment of more efficient, transparent and well-regulated crop and livestock markets. Technical and financial assistance to establish a system of tradable warehouse receipts, for example, is one possible measure that could help isolated mountain farmers in particular to secure more favourable prices for the crops they produce and to branch into new activities.

Partnership-building is also a key element of the IFAD strategy for market development. This is particularly important in isolated mountain areas where the resources available to IFAD simply do not allow for investments in major infrastructure (such as rural roads, telecommunications, schools and health centres), which is needed to support long-term economic growth and market participation. IFAD projects do, however, provide a platform to identify the specific needs of targeted communities and to demonstrate replicable approaches. Especially by targeting neglected areas, IFAD has been able to increase its visibility and ensure a role in helping to coordinate development policy in partnership with governments, other donors and civil society.

On-farm productivity. As a precondition for economic growth and market participation, IFAD will also continue to support selected investments in improved on-farm productivity. Although many farmers have already met their basic subsistence needs, access to improved seeds, veterinary services and extension advice are still needed to support woman-headed households and other new farmers. As discussed, the transition experience clearly shows that new supply channels are needed to ensure that farmers have access to the seasonal inputs and other institutional services they require. Apart from contract farming and producers’ associations, investments to help develop private ploughing and hay-baling services, for example, can also contribute to the improved efficiency of smallholder agriculture and create jobs for rural workers. In addition, the
development of small-scale, community-managed irrigation systems is another area where IFAD has enjoyed particular success and can contribute to increasing productivity of food crops for home consumption and of new commodities for cash sale.

IFAD recognizes, however, that investments designed to promote increased productivity are unlikely to succeed over the long run unless they are market-oriented. As discussed, limited market access is often an even greater constraint for the majority of poor farmers who have often met their basic subsistence requirements but now have little incentive to produce a surplus for cash sale. Future investment projects will not overlook the importance of improved productivity as a necessary condition for growth, but this focus will also be balanced by a clear recognition that productivity gains are far from sufficient to ensure sustainable poverty reduction in transition economies.

**Non-farm rural economy.** IFAD investments will focus not only on primary agriculture production but also on other areas of the rural economy. This emphasis is justified by the large number of rural people who depend on activities other than farming for their main source of livelihood. Indeed, support for small and medium-scale agro-processors, agricultural service providers and other types of rural businesses offer some of the best opportunities to stimulate growth and build the new markets needed for poverty reduction. IFAD will target these enterprises through provisions for appropriate financial services and technical assistance to develop business plans and identify new market opportunities. Partnerships with local and international NGOs capable of providing these services will also be an important practical element of this strategy.

**Natural resource management.** Protecting the region’s fragile natural resource base is another important cross-cutting theme that future IFAD projects will need to address. As discussed, the general neglect and lack of respect for the environment during the era of central planning have led to severe pollution of agricultural land. The uncontrolled exploitation of forests for fuelwood and communal land for grazing, together with the lack of land preservation measures, has led to significant soil erosion and degradation, posing a serious threat to crop and livestock productivity. Future projects, therefore, will work to create the incentives that communities need to protect their local environment and undertake remedial action to arrest further water and land contamination and soil erosion. Again, these investments will be market-driven and focus on the financial benefit for local communities deriving from improved natural resource management.

**Rural financial services.** To support its programmes in each of the above areas, IFAD will continue to give high priority to the development of rural financial services as a fundamental precondition for sustainable economic growth. This emphasis is also an important part of IFAD’s strategy for institution-building. Future projects, therefore, will work with private banks and other service providers to develop seasonal credit and long-term investment facilities and to build necessary support for enabling legal reforms. As discussed in Chapter IV, IFAD has considerable experience with different approaches to rural credit and will continue to use various mechanisms that target specific beneficiary groups. Depending on country circumstances, these may include village credit associations that are aimed at new rural producers and help ensure repayment
through joint liability, or other more formal arrangements that target larger-scale SMEs and support new market linkages and growth in relevant areas of the non-farm rural economy. Within this context, the Fund will emphasize new channels of credit distribution that target not only individual family farmers but also commodity traders, agricultural service providers, agro-processors and other rural entrepreneurs.

**Non-Lending Activities**

In addition to IFAD’s lending programme, future interventions will also focus on partnership-building, policy dialogue and knowledge management as mutually reinforcing elements of IFAD’s subregional strategy. To reach its overall objective of a sustainable reduction in rural poverty, IFAD must focus on selected areas to achieve maximum impact. This in turn depends on successful knowledge management of proven strategies, dialogue with borrower governments and other stakeholders on policy reform, and partnership-building to allow wider coverage than IFAD could achieve on its own. These areas correspond with IFAD’s corporate Plan of Action.

**Partnership-building.** The development of new partnerships with other donors, international NGOs and local civil society is another key element of IFAD’s strategy. This focus is especially relevant in planning project strategies for CEN countries since most borrower governments, and especially those borrowing on intermediate terms, have expressed a strong preference for programmes with a clear financial return and a guaranteed cash flow to repay loan proceeds. This position has sometimes made it difficult to use loan money to finance institutional capacity-building and farmer training. IFAD must therefore continue to look for ways to mobilize grant cofinancing to cover essential investments in these areas.

To address this need, IFAD’s approach to partnership-building will be to share lessons from its experience and stimulate dialogue on development strategies and practical operations that promote economic integration and address the underlying causes of rural poverty.

As described in Chapter IV, IFAD has so far enjoyed considerable success in forging new partnerships with bilateral and regional donors in CEN countries. A major challenge, therefore, is to cement these relations and introduce a more programmatic approach. Thus far, most partnerships have focused on traditional cofinancing of individual projects, and IFAD now needs to explore new avenues of cooperation that build on the long-term priorities and strategic interests of each donor. In The Former Yugoslav Republic of Macedonia, for example, SIDA (Sweden) has recently agreed to provide cofinancing for administrative and technical costs of the new agricultural credit discount fund; and in Albania, a similar long-term relationship is beginning to develop with the Department for International Development (DFID) (United Kingdom). Both bilateral agencies have only recently begun to support activities in the agriculture sector in the Balkans; and the ongoing discussion of country strategies with these and other donors is helping to leverage IFAD’s position with respect to specific development priorities and also to ensure complementarity with other development activities. IFAD will also seek to develop and strengthen its relations with multilateral donors in the region including the Council of Europe Development Bank, the European Union and the World Bank.
IFAD will also continue to support a wide variety of ECP grants to enhance project impact in strategic areas and build partnerships with civil society. To the extent possible, these initiatives will continue to be cofinanced by participating NGOs and other donors, and by project beneficiaries themselves to ensure local ownership and long-term sustainability. In Armenia, for example, IFAD is supporting local NGOs on a matching-grant basis to develop civic-action groups that further economic development in the poor mountain areas covered by ongoing projects. In Azerbaijan and Georgia, grant financing is being used to help establish a mountain area network that will allow NGOs to draw on the combined strength, experience and resources of both countries in order to address policy, technical, social and institutional constraints. This approach to partnership-building contributes to the overall sustainability of IFAD’s investments and provides an opportunity to leverage additional resources for the cofinancing of future projects.

**Policy dialogue.** IFAD’s strategy for policy dialogue in the CEN region will be to lead by example through the projects it supports. On this basis, future operations will work to build consensus on policy issues by sharing lessons learned through partnerships with local and international stakeholders. IFAD is already helping to influence mountain area development policy in several countries, and has made good progress with respect to dialogue on the legal arrangements for land privatization and institutional approaches to the development of rural financial services.

Indeed, recent experience shows that there are especially good opportunities in the CEN region for meaningful dialogue with borrower governments and other donors on rural development strategies. As noted, the small size of most CEN countries that IFAD covers has allowed the Fund to develop close relations with the new governments at some of the highest levels of national decision-making. Especially when it has targeted marginalized areas not covered by other donors, IFAD has been able to establish its own unique identity and thereby exert influence on national and regional development policies.

IFAD will also pursue dialogue with other donors to draw attention to the importance of rural development, identify possible synergies and agree on areas of operational responsibility. This is especially relevant in the CEN region since most other donor programmes have so far focused on enterprise restructuring, industrial development, democratization and urban services. Far less attention has been given to agriculture and, even then, most attention has been focused on high-potential farm areas without specific regard to the poorest and most vulnerable groups. By focusing specifically on these groups and on the underlying causes of their poverty, IFAD is well positioned to demonstrate successful approaches and build a platform for dialogue on strategies that truly make transition work for everyone including the rural poor.

**Knowledge management.** The main objective of IFAD’s strategy for knowledge management in CEN countries is to document proven strategies that can be adapted for wider application and to identify key lessons from ongoing projects and new approaches that help maximize impact. In addition to detailed project completion reports, midterm evaluations and other normal reporting channels, a key element of IFAD’s strategy for improved knowledge management is to develop impact-oriented monitoring
and evaluation systems for the projects it funds. In Armenia, for example, IFAD has carried out detailed baseline and repeater surveys to assess the impact of its support for credit, irrigation and seed production. This information helped guide the preparation of a third project for Armenia and is also serving as a basis for ongoing dialogue with the Government and other donors on effective intervention strategies. Similarly, in Azerbaijan and Georgia, a new joint programme for mountain and highland areas will introduce a dynamic and participatory planning process and beneficiary-led impact monitoring to ensure that programme activities are responsive to beneficiary needs and alert to problems in implementation performance. Finally, in an effort to move beyond appraisal estimates and enhance its profile with respect to the global dialogue on the MDGs, IFAD will also increasingly focus on monitoring the number of beneficiaries actually served by each project and the quality of impact on rural poverty.

At the national level, country strategic opportunities papers (COSOPs) will continue to be one of the most important instruments of knowledge management. In addition to a focused analysis of the rural poverty situation in each country and lessons learned from previous operations, these papers will be the main vehicles for identifying strategic opportunities for maximizing the impact of IFAD’s resources. On the basis of the analysis presented in this subregional strategic opportunities paper, it will be especially important for future COSOPs to address the following issues: (i) the current status of and barriers to increased private-sector interaction with small-scale farmers; (ii) the strategic role for credit in helping to build stable and remunerative market linkages; and (iii) priority areas for technical assistance to farmers, private-sector stakeholders, government departments and other project partners.

Technical assistance grants are another important element of the strategy for improved knowledge management. Although this subregional assessment does much to synthesize IFAD’s experience in the region and to identify strategic opportunities, further research is still needed to help refine the strategy and identify the best areas for project intervention. Specifically, this assessment shows that limited access to market outlets for smallholder produce is one of the main constraints to growth and an important factor underlying the high levels of rural poverty. Indeed, many farmers continue to produce along similar lines as before and have only a limited understanding of which crop and livestock products and cropping patterns offer the greatest potential for growth and profit in the new market economy. On this basis, IFAD could make an important contribution to the regional knowledge base by implementing a special technical assistance study of market linkages, competitiveness and farm profitability to identify specific intervention strategies.

IFAD can also play an important role by helping to channel existing knowledge to the benefit of ongoing and future projects. As discussed, the limited capacity of bank officials to evaluate small-scale investment loans has been an important constraint to the development of effective rural financial services. In this respect, there is a good opportunity for IFAD to use technical assistance resources to review past experience with the appraisal of loan applications and to develop a tool kit to introduce bank officials and
other service providers to improved procedures. Financial institutions in other parts of the world have all had to address the challenge of striking a balance between detailed financial analysis of agricultural loans and the need for simple effective procedures. IFAD is well positioned to help share this knowledge and adapt proven technologies to suit the new institutions in CEN countries.

**Concluding Remarks**

This subregional poverty assessment and strategic opportunities paper sets out to provide an improved understanding of the nature and extent of rural poverty in the CEN region and to identify the basic elements of a medium-term strategy for IFAD operations in these transition countries. Although many other countries where the Fund operates are also in the process of moving from some form of central planning to market-based production, transition in CEN countries has been marked by an especially dramatic increase in rural poverty, the almost total loss of former guaranteed markets and the difficult adjustment from large-scale mechanized production to small-scale family farms. These unusual characteristics present an unparalleled challenge to IFAD, which can only be addressed through a long-term focus on institution-building and support for new market linkages that benefit primary producers and stimulate growth in the non-farm rural economy.

To help IFAD devise effective project lending and other intervention strategies, this paper has sought to provide an improved understanding of the unique set of circumstances that shape both the nature of poverty and the opportunities to move out of poverty for people in the CEN region. As such, the subregional analysis is expected to serve as a reference point to help guide future operations and policy dialogue for effective poverty reduction. Ultimate success, however, depends on the actual projects that IFAD supports and implementation of other non-lending activities. Only through careful selection and coordination of these interventions can IFAD truly provide the support that farmers and other rural residents need to move away from agriculture as a means of coping with poverty to market-based production as a route out of poverty.
Endnote

1 IFAD, 2000f.