

Republic of Azerbaijan

North-East Development Project Project Performance Assessment

Executive Summary

1. With a population of 9.1 million, Azerbaijan is located on the shores of the Caspian Sea in the eastern part of the South Caucasus region. The country gained independence in 1991 following the collapse of the Soviet Union. Prior to independence, its economy was based mainly on agriculture and agroprocessing. Post-independence turmoil led to increased poverty during the 1990s but, thanks to large off-shore investments in the oil sector since 1995 and growing world oil prices, Azerbaijan experienced a growth of oil revenue in the 2000s and, since then, average GDP growth has exceeded 20 per cent per year.
2. To date, the Fund has approved five lending projects/programmes in Azerbaijan, corresponding to total IFAD loans of US\$67.5 million and project costs of US\$192.3 million. The North-East Development Project (NDP), the third project in the cohort, was implemented during the period 2006-2011. The expected total cost of the project was US\$25 million, including an IFAD loan of US\$12.56 million. At completion, the actual total cost amounted to US\$40 million, with the Government covering the additional costs.
3. The project was designed and implemented in a transitional context. The transition from a farming system based on large-scale collective farms to one based on small, private farms with owners from varied occupational backgrounds but few with farm management experience was a challenging scenario, further compounded by very run-down irrigation systems, weak extension services, poor agricultural management and low productivity. Given this testing implementation environment, NDP's successful introduction of participatory irrigation management on 31,000 ha of irrigated land, to the benefit of some 15,000 households, was an impressive achievement.
4. **Project performance.** Adopting a participatory irrigation management approach, NDP successfully established water user associations (WUAs) and rehabilitated some 31,000 ha of farmland, largely in line with the 32,000 ha estimated at appraisal. Significantly increased water supplies and improved water-use efficiency provided a sound basis for introducing higher-value crops, increasing crop yields and expanding livestock activities. WUAs made an encouraging start to managing the rehabilitated irrigation systems and distributing water to irrigators in an equitable manner. Thanks to improved extension services and water supplies there have been encouraging increases in crop, forage and livestock productivity, with yield increases of 30 per cent for crops and 60 per cent for orchard fruits.
5. Leveraging the increased supply of irrigation water, NDP's modest investments in agricultural extension services, cattle genetic improvement and bee-keeping led to significant production benefits for small farmers and showed strong potential for meeting the need to improve the food security and income of small farmers, who constitute the majority of Azerbaijan's rural population.
6. NDP set up a credit line, which was managed through participating financial institutions, including three commercial banks and one microfinance institution (MFI). The aim was to provide sustainable gender-sensitive financial services to smallholder farmers and other microentrepreneurs, including individuals and groups. Credit uptake took off rapidly: the banks provided 139 medium-sized individual loans, with an average loan size of US\$30,000; the MFI provided 42

individual loans, with an average loan size of US\$9,100. These credit services resulted in increased investments in small-scale livestock, fruit and crops, and repayment rates were close to 100 per cent.

7. Results of marketing and small and medium-sized enterprise (SME) activities are disappointing, and there is little evidence of improved marketing, storage or processing facilities on the ground. Most produce is still sold individually through village trade, local markets or traders; marketing through organized producer or cooperative groups is negligible, just 6 per cent in the case of crops and 1 per cent for livestock. Apart from disappointing performance under the marketing and SME component, most project objectives were achieved.
8. **Sustainability.** WUAs are not yet fully established or financially secure. They currently manage to cover their operating costs but carry no reserves and do not have the resources to undertake major repairs to earth-moving equipment or replace it, or to undertake an increasing maintenance load. Unless water charges are increased, the rehabilitated structures are likely to deteriorate again and the efficiency of water delivery to decline. In such a scenario WUA members will see little value-added in continuing their membership, thereby jeopardising WUA survival.
9. The benefits generated from farm activities, including crops, orchards, livestock and bee-keeping, are expected to be sustained and expand as farmers become convinced by increased crop and livestock yields. However the sustainability of agricultural and livestock technical services in the project areas is uncertain as there is no service provider in place to continue services after project closure.
10. The success of participating banks indicates sustainability of established credit and other financial services to rural clients. However their continued eligibility to use the IFAD revolving fund will need to be resolved, especially if the lending volume to rural clients is to be maintained.
11. **Innovation and scaling up.** NDP was not significantly innovative inasmuch as it mainly adapted approaches that were already tested. However, delivering participatory irrigation management and rural financial services through partnerships with the private sector, NGOs and commercial banks on a significant scale in the Azerbaijan's context are innovative features that were subsequently scaled up in following projects.
12. **Gender equality and women's empowerment.** Although gender equality was already embedded in Azeri society, IFAD's insistence on mainstreaming women's equality in project activities has contributed to strengthening their position in the agrarian society. During implementation, women participated as WUA members and are employed in management teams and as members of elected boards. Some 15 per cent of beneficiary households were female-headed, and women participated actively in farm demonstrations and training in agricultural and food processing technologies. Women represented 30 per cent of the beneficiaries of technology transfer through field demonstrations and 40 per cent of recipients of micro credit through group lending.

Main recommendations

13. **Enhance sustainability to ensure upcoming benefits.** To improve the sustainability of WUAs supported by NDP, better operational coordination between State Amelioration and Irrigation Committee (SAIC) and IFAD projects would be mutually beneficial and may help resolve the long-outstanding issue concerning SAIC's stance on transferring management responsibilities to WUAs. In the case of projects such as NDP that are predominantly involved in irrigation reconstruction and will ultimately fall under SAIC management, there would be advantage to place an irrigation implementation team under SAIC management, as in the case of World Bank projects. To resolve key sustainability issues and mitigate risks that

could jeopardise the project's economic viability, IFAD and the Government should consider an exit strategy, such as a modest post-project investment with mainly technical and management assistance.

14. **Increase investment in marketing and processing.** Lessons learned from NDP also highlight the need for marketing and processing services in integrated irrigation projects because improved irrigation could lead to a large increase in farm production in project areas. However, as many farm products are of basic quality and homogenous, they compete on the same local market channels. The marketing of agricultural products should be significantly enhanced in future irrigation projects and new marketing channels explored.
15. The most outstanding challenge is to develop capable and influential producer organizations for marketing, storage, packaging, branding and product positioning, which are closely linked with private-sector investment. This complex issue calls for the involvement of commercially-oriented specialists with relevant marketing experience in design and execution, possibly backed up by tax and subsidized investment incentives to pump-prime commercial investment in the subsector.
16. **Increase investment in agriculture and livestock.** The proportion of investment in agricultural crop and livestock productivity in integrated irrigation projects should be emphasized to reflect the importance of such activities to IFAD target groups. Without sufficient economic benefits for small farmers, investment in irrigation would not be sufficiently justified. There are a few key areas where IFAD interventions could update services to improve agricultural and livestock productivity, such as: adaptive agricultural research, sustainable extension services, and bee-keeping and orchard development.