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MULTILATERAL INVESTMENT FUND

BRAZIL

**SUPPORT FOR PROMOTING PRIVATE INITIATIVES IN THE STATE
OF ALAGOAS**

(BR-M1059)

DONORS MEMORANDUM

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ABBREVIATIONS

| | |
|--------|---|
| AFAL | Agência de Fomento do Estado de Alagoas [State of Alagoas Development Agency] |
| ESR | Environmental and social review |
| IBGE | Instituto Brasileiro de Geografia e Estatística [Brazilian Geography and Statistics Institute] |
| IPEA | Instituto de Pesquisa Econômica e Aplicada [Economic and Applied Research Institute] |
| MSE | Micro and small enterprises |
| MSME | Micro, small, and medium-sized enterprises |
| PEU | Project executing unit |
| PNAD | Pesquisa Nacional por Amostra de Domicílios [National Household Survey] |
| SEPLAN | Secretaria de Estado do Planejamento e do Orçamento [Planning and Budget Secretariat], State of Alagoas |

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SUPPORT FOR PROMOTING PRIVATE INITIATIVES IN THE STATE OF ALAGOAS
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EXECUTIVE SUMMARY

| | | | | | | | |
|---|--|------------------------|-----------------------|--------------------|-----------------------|--------|----------------------|
| Beneficiary/ Executing agency: | Agência de Fomento do Estado de Alagoas (AFAL) [State of Alagoas Development Agency], Brazil | | | | | | |
| Beneficiaries: | 1,800 microentrepreneurs; 60 small and medium-sized enterprises. | | | | | | |
| Financing: | <table> <tr> <td>MIF (nonreimbursable):</td><td>US\$2,200,000 (40.7%)</td></tr> <tr> <td>Local counterpart:</td><td>US\$3,200,000 (59.3%)</td></tr> <tr> <td>Total:</td><td>US\$5,400,000 (100%)</td></tr> </table> | MIF (nonreimbursable): | US\$2,200,000 (40.7%) | Local counterpart: | US\$3,200,000 (59.3%) | Total: | US\$5,400,000 (100%) |
| MIF (nonreimbursable): | US\$2,200,000 (40.7%) | | | | | | |
| Local counterpart: | US\$3,200,000 (59.3%) | | | | | | |
| Total: | US\$5,400,000 (100%) | | | | | | |
| Objectives: | <p>The <i>general objective</i> of the project is to contribute to the economic development of Alagoas through the expansion, diversification, and modernization of micro, small, and medium-sized enterprises (MSMEs). The <i>purpose</i> is to consolidate an innovative model of a public-private development agency through pilot initiatives to promote economic inclusion and facilitate the competitive development of MSEs.</p> <p>The program will be divided into five components.</p> | | | | | | |
| Execution and disbursement period: | 48 months. | | | | | | |
| Special contractual clauses: | (i) Approval by the Bank of the project implementation plan and the annual work plan for year one; (ii) evidence that the Operating Regulations are in effect; and (iii) evidence that 5% of AFAL's capital is private and this is reflected in the composition of its board. | | | | | | |
| Environmental and social review: | The ESR Secretariat reviewed this operation on 28 March 2008 and its comments have been incorporated into paragraph 7.2. The operation was accorded a "C" classification. | | | | | | |
| Coordination with other donors: | None. | | | | | | |

I. BACKGROUND AND JUSTIFICATION

A. The state of Alagoas, social exclusion, and development potential

- 1.1 The state of Alagoas is located in Brazil's northeastern region. With an area of 27,818 km², it is the country's third smallest state. In 2006, its population was 3 million.¹ The profile of the state's productive system is marked by: (i) scant diversification;² (ii) little dynamism because the main economic sectors operate with low value added, low technological intensity and low productivity; (iii) heavy reliance on the public sector, which accounts for 27% of GDP and one third of all formal employment; (iv) regional concentration (two thirds of GDP is produced in the capital region); and (v) one half of the working population employed in the informal sector.³
- 1.2 In recent decades, Alagoas' social indicators for health, education, poverty, and inequality have been among the lowest in Brazil. In 2004, 60.3% of the population was living in poverty, while 44.4% was indigent—the highest rates in the country.⁴ In 2006, Alagoas had the second-worst poverty reduction rate in the entire northeast. Education indicators point to low human capital. In 2005, the illiteracy rate for people over the age of 15 continued to be the highest in Brazil (29.3%) and average schooling for adults over the age of 25 was 4.2 years—the lowest in the northeast.
- 1.3 In recent years, Alagoas (like the entire northeastern region) has benefited considerably from federal government transfer payments, particularly through social programs such as Bolsa Familia. It is estimated that such transfers account for one third of state GDP.⁵ For example, in 2006, Bolsa Familia and the program to eradicate child labor, targeted to the very poor, transferred R\$22 million/month, to the benefit of 350,000 families.
- 1.4 Despite the constant financial injections and increasing local demand, Alagoas has been experiencing the lowest GDP growth amongst northeastern states (1.8% in 2006) due in part to a combination of fragile institutions and weak entrepreneurship made up of a small modern sector and a large traditional one. The weakness of public institutions is evident in the administrative problems of municipal governments and insufficient technical skills to transform new opportunities into development. The Alagoan business sector, which has grown up around an economy highly concentrated in a single-crop (sugar cane), consists mainly of very

¹ PNAD/IBGE, 2006.

² Sugar and sugar-cane based alcohol contributes 84% of the gross value added of farm production and 85% of industrial processing.

³ IPEA, 2006.

⁴ Poverty line: per capita family income less than one-half the minimum wage or R\$190/month. Indigence line: per capita income below R\$125/month. IPEA, Radar Social, 2006.

⁵ The Federal Ministry of Social Welfare transferred R\$140 million/month in that year.

small, undercapitalized companies. Last, the knowledge institutions present in the state have extremely weak links to the region and to the productive sector.

- 1.5 This assessment is being used as the backdrop for an **Alagoan Strategic Vision** built on broad consultation, participation, and consensus guided by the Alagoas Planning and Budget Secretariat (SEPLAN). This strategic vision is based on three main objectives:
- a. Promoting economic inclusion. Two avenues have been proposed: (i) strengthening local productive capacity (low-income economy) by boosting demand of the poor through government transfer payments; and (ii) converting social safety nets into measures that strengthen the capabilities of the poor.
 - b. Promoting economic and regional integration. The size of the transfers and infrastructure programs envisaged would make it possible to create an economic foundation that integrates the different geographical regions of Alagoas for the first time in its history.
 - c. Integrating Alagoas into the global economy. In this picture of economic change, it is indispensable to develop a network of international political and economic relations.

B. Challenges and opportunities in Alagoan society

- 1.6 The main weakness, then, is the high level of poverty, sometimes extreme, which translates into low levels of social development and high levels of exclusion. This situation derives from lack of access by most of the population to economic opportunities and training, thus hindering participation by the low-income groups in economic development. This vicious circle is perpetuated by constraints on development potential such as:
- a. The difficulties encountered by micro and small enterprises (MSEs) in finding solutions, on their own, to the requirements for diversification, production modernization, and management.
 - b. The institutions (municipal governments, business associations, knowledge centers, etc.) that should support the local development process do not have the capacity, which means that development initiatives are inconsistent, disjointed, and, in particular, unable to expand on positive and inclusive productive experiences.⁶
 - c. The scant capacity to generate dynamic enterprises with high value added limits the potential for using existing natural and human resources.
- 1.7 Moreover, technical and institutional capacity limits the ability to tap the opportunities generate by government transfers, thus increasing the likelihood of

⁶ For example, although Alagoas has one of the most successful production cooperatives in Latin America—Pindorama—this experience has not been replicated or extended to other parts of the state.

creating economic dependence, production disincentives, and problems in sustaining the transfer .

- 1.8 Through the participative process of building the Alagoan Strategic Vision, however, a more dynamic atmosphere has been created, making it possible to envisage development opportunities that include:
- a. The existence of assets, particularly natural resources, which, as other northeastern states have shown, can offer a solid foundation for development, the main ones being coastal tourism judging from the numerous (albeit haphazard) business initiatives that exist, fruit farming irrigation (similar to Pernambuco), and fish farming in the San Francisco river delta.
 - b. Transfer of income which, as indicated, creates an environment not conducive to development although it can offer a development opportunity. Development can be brought about by increased consumption (in 2007 estimates were 6% for the country as a whole, but over 15% for Alagoas) if the low-income economy is strengthened⁷ (with an impact on the economic inclusion of marginal social groups), while also helping small enterprises to link up to networks and production chains.
 - c. The infrastructure programs under way in Alagoas under the Plano de Aceleração do Crescimento (PAC) [growth acceleration plan] such as the construction of an irrigation canal in the semiarid part of the state, macrodrainage in agricultural regions, modernization of highways and the port of Maceió, and revitalization of the lagoon complex and the San Francisco river delta.
- 1.9 One extremely important factor in the state's productive development is the start up of the Alagoas Development Agency (AFAL). The agency, which has now been formally created, is a technical and institutional instrument based on public-private cooperation, open to private capital, whose strategic function is to promote inclusive productive development. AFAL which is currently being structured, has the following two functions:
1. To promote local competitiveness. Through the use of different types of technical-cooperation programs, AFAL would promote: (i) the development of local productive arrangements—MSE clusters – with a regional approach that facilitates economic inclusion; (ii) the linking together of public, private, and knowledge institutions for productive development initiatives aimed at poverty reduction; and (iii) dissemination and incorporation of innovations in production.
 2. To promote access to credit. Proposing to act as a second-tier financial institution, AFAL will modernize the microcredit sector, spreading new

⁷ Cicero Péricles de Carvalho, *Economia Popular. Uma via de modernização para Alagoas*, EDUFAL, 2007.

methodologies and new products tailored to low-income groups and strengthening microfinance institutions.

- 1.10 Public resources equivalent to US\$5 million have now been budgeted for AFAL's capital, and its operation will be funded initially by the state and subsequently with revenue from its lending operations and fees for administering third-party funds⁸. AFAL will also manage the Alagoas anti-poverty fund financed with a percentage of exports, which could be used to finance technical assistance projects.

C. Rationale

- 1.11 To contribute to the economic development of Alagoas, the project will support **the development of an innovative development agency model based on demonstration pilot projects**. The pilot projects, which will directly benefit low-income groups, will use a private-sector model, and target diversification and modernization of the business fabric, and the integration of MSEs into the formal economy. AFAL is an innovative initiative in the Brazilian context owing to both its governance—a capital structure based on public and private partnerships—and its technical excellence in promoting production. AFAL will coordinate and strengthen market transparency and the supply of financial and nonfinancial services, with a view to making its initiatives sustainable.
- 1.12 AFAL and SEPLAN, to which it reports, view the MIF as an ideal partner, because it is a multilateral development agency with considerable experience in implementing and administering initiatives to promote small enterprises. The MIF model and operating principles are considered innovative and conducive to the sustainability of the initiatives, and can be adapted to the state's different development conditions and priorities. This project would support AFAL in its early stages, introducing and adapting methods for the design, execution, and monitoring of productive development operations, with a focus on promoting the productive and business sectors.
- 1.13 The project is a pilot experience which, if successful, would be considered by the development agencies of other Brazilian states. The process of adapting the technical assistance project monitoring and design tools and methodologies for private-sector empowerment could lead to a learning experience in which best practices are disseminated to other countries.

⁸ Some of AFAL's share capital is now held by the private sector and a public offering is being prepared to increase its capital and give formal recognition to private sector organizations such as business associations and chambers of commerce. Also, AFAL is negotiating with Banco Nacional de Desenvolvimento Econômico (BNDES) and Serviço Brasileiro de Apoio às Micro e Pequenas Empresas (SEBRAE) on a contribution of resources and on their being represented on AFAL's board of directors.

II. THE PROGRAM

A. Objectives

- 2.1 The *general objective* of the project is to contribute to the economic development of Alagoas through the expansion, diversification, and business modernization of MSMEs. The *purpose* is to consolidate an innovative model of a public-private development agency that promotes economic inclusion and facilitates the competitive development of MSEs, by means of pilot initiatives.

B. Project description

1. Component 1. Building technical capacity (MIF: US\$283,400; counterpart: US\$395,000)

- 2.2 The objective of this component is to consolidate AFAL as an institution of technical excellence and boost its capacity to interact with a network of public and private organizations, making it more efficient and effective in its actions to develop MSEs.
- 2.3 The project will provide technical assistance and training to: (i) establish internal working methodologies for AFAL with regard to product identification and supervision of activities; (ii) update AFAL's business plan and develop its strategic plan, facilitating careful control of the agency's sustainability, an important factor in maintaining Central Bank authorization to operate as a second-tier financial institution; (iii) train AFAL's technical experts in project analysis, selection, and management; (iv) support AFAL's development through peer tutoring and exchanges with similar institutions in Brazil and other countries; and (v) support the design and implementation of a marketing and communications plan.

2. Component 2. Support for innovation and sustainability in microfinance institutions (MIF: US\$29,200; counterpart: US\$626,800)

- 2.4 The objective of this component is to design and implement a strategy to promote the Alagoas microfinance market. To that end, it would help AFAL to develop technical assistance activities for microfinance to bolster the financing available for the sector.
- 2.5 To strengthen AFAL's capacity to provide technical assistance for microfinance institutions, support would be furnished for: (i) defining such a strategy for developing new microfinance products and deepening the sector, thus facilitating the entry of new agents; (ii) the design of innovative products and their dissemination to microfinance institutions; and (iii) three pilot technical assistance and training initiatives to implement the strategy. The latter initiatives would benefit microfinance institutions wishing to enter and expand the Alagoas market, or to diversify their product range, and would include such activities as dissemination of risk assessment methodologies, support for operating and risk control systems, implementation of accounting or financial systems, and procurement of information systems. These technical assistance activities will be

backed by AFAL staff, who will help train and prepare them to continue the activities after project completion.

3. Component 3. Building the local foundations for development (MIF: US\$204,400; counterpart: US\$362,600)

- 2.6 This component would support the process of building institutional and human capacity to create a favorable environment for developing and implementing pilot initiatives in each of the state's economic regions: the Atlantic coast, the San Francisco river area, the sertão (semiarid area), the Agreste, the Zona da Mata, and the metropolitan zone of Maceió. The project will finance training and technical assistance activities for:
- a. Institutional development of public and private local entities. The following is planned: (i) support for public and private entities engaged in regional economic development to augment their technical capacity to identify, design, manage, and monitor productive-development and economic-inclusion projects; and (ii) development in the municipalities and other public institutions of the capacity to interact with companies.
 - b. Development and dissemination of technical capacity to establish networks of companies. The project would build this capacity through practical and technical training and would therefore support: (i) training for specialized consultants and AFAL staff, with a view to forming and administering networks of companies; and (ii) twenty programs to generate business networks.
 - c. Development of technical capacity for social empowerment initiatives in civil society organizations (public, NGOs, and other institutions) in the different economic regions. Initiatives will be developed to assist the poorest social groups so they can join the formal economy by boosting self-confidence and facilitating employment. To that end, the project will support: (i) technical training for professionals from civil society organizations; and (ii) identification and implementation of a maximum of 10 pilot initiatives, with financing of up to 70% of cost, which may not exceed US\$20,000. Such initiatives would benefit communities living in extreme poverty and their purpose will be to facilitate their economic inclusion. They may include training in the technical and vocational areas, entrepreneurship, and self-confidence.

4. Component 4. Selection and implementation of pilot projects (MIF: US\$1,107,400; counterpart: US\$1,173,900)

- 2.7 The objective of this component is to support initiatives for local competitiveness intended to boost the competitive advantages of the six economic regions selected. It would involve the following activities: (i) development of guidelines for competitive fund invitations; (ii) workshops to publicize the competitions;

- (iii) project evaluation and selection; and (iv) project implementation and monitoring.
- 2.8 The entities promoting these initiatives may be networks of companies, private civil society organizations, or local public entities, in which case priority will be given to those having an operational partnership with a private organization. The pilot projects will be of four types: (i) strengthening of clusters of companies (local productive arrangements); (ii) vertical productive chains with anchor companies; (iii) local competitiveness projects; and (iv) particularly innovative initiatives. The first three kinds of projects should draw on the lessons learned in earlier projects and consider the action plans of MIF project clusters for productive integration and local competitiveness. The project must not cost more than US\$120,000, with the competitive fund defraying up to 80% of the cost. Recurrent costs (personnel, rental of premises, maintenance of equipment and infrastructure, public utilities, etc.) will not be eligible for financing.
- 2.9 In selecting the projects, priority will be given to those that: (i) are an initiative developed by a partnership of entities and/or enterprises; (ii) help to improve living conditions (poverty, income, or employment rates); and (iii) promote innovative productive activities or generate higher value added. All projects must comply with the environmental exclusion list.
- 2.10 For instance, to better position the project and to boost AFAL's capacity, an initial precursor project (Support for sheep and goat farming in the Alto Sertão region) was identified during the analysis. The project's estimated value is US\$120,000 and it will be carried out by COOFADEL, the most significant cooperative in this area. The Alto Sertão is a semi-arid area, with the state's lowest human development indicators, where family farms predominate (97% of all properties). Sheep and goat farming, apart from being a special tradition in the area, offers: (i) the most suitable activity for the semi-arid area; (ii) an opportunity to apply accessible technologies along the production chain; and (iii) an opportunity to improve management and processes, with an impact on value added. The precursor project would strengthen the sector's production chain; specifically, it would: (i) coordinate each specialized phase of the production chain: breeding-fattening-transport-slaughter-refrigeration-marketing; (ii) create a certified source of animal control (federal inspection stamp); and (iii) promote access to urban markets, through differentiated product strategies (special cuts and sausages). The project would benefit 500 producers, improving their productivity and raising their incomes by more than 60%.
- 2.11 The processes of project selection and project administration and monitoring will be performed by AFAL according to criteria and standards acceptable to the MIF. These are described more fully in the project Operating Regulations.

5. Component 5. Systemization of lessons learned and dissemination of the outcomes (MIF: US\$74,000; counterpart: US\$100,300)

- 2.12 The objective of this component is to illustrate the most efficient ways of promoting and supporting basic development and disseminating the experiences and outcomes.

The following activities are planned: (i) to develop and implement a project monitoring system (includes the establishment of the baseline); (ii) to document the lessons learned, particularly with regard to the establishment of AFAL itself and the development of tools and projects to promote economic inclusion; and (iii) to hold two events to disseminate the outcomes and the lessons learned.

III. COST AND FINANCING

- 3.1 The project will cost a total of US\$5,400,000, of which 40.7% (US\$2,200,000) will be provided by the MIF as nonreimbursable financing. The executing agency will finance the counterpart funding.

| Budget items | MIF | Counterpart | TOTAL | % |
|---|------------------|--------------------|------------------|-------------|
| C 1, Building technical capacity | 283,400 | 395,000 | 678,400 | 12.6% |
| C 2, Support for innovation and sustainability in microfinance institutions | 29,200 | 626,800 | 656,000 | 12.1% |
| C 3, Building the local development foundations | 204,400 | 362,600 | 567,000 | 10.5% |
| C 4, Pilot project selection and implementation | 1,107,400 | 1,173,900 | 2,281,300 | 42.2% |
| C 5, Monitoring and systemization of lessons learned | 74,000 | 100,300 | 174,300 | 3.2% |
| Executing unit | 277,200 | 501,600 | 778,800 | 14.4% |
| Annual evaluations | 50,000 | - | 50,000 | 0.9% |
| Annual financial audits | 68,000 | - | 68,000 | 1.3% |
| Contingencies | 95,400 | - | 135,200 | 2.5% |
| Impact evaluation account | 11,000 | - | 11,000 | 0.2% |
| TOTAL | 2,200,000 | 3,200,000 | 5,400,000 | 100% |

- 3.2 **Sustainability.** Project sustainability is based on two factors: (i) the government of Alagoas' commitment to develop and support AFAL and to ensure that funding will continue to come from the anti-poverty fund; (ii) the Central Bank of Brazil requirement that AFAL be operationally sustainable within its first three years, as a condition for recognition as a second-tier financial institution; (iii) at the local level, the sustainability of businesses and institutions that stand to benefit directly will be ensured by the project outcomes themselves, as higher economic returns and greater institutional efficiency are produced.

IV. EXECUTION MECHANISM

- 4.1 **Executing agency.** The executing agency will be the Alagoas Development Agency (AFAL), a joint public and private, closed corporation, established under Law No. 4688 of 16 June 2004, with the state of Alagoas holding a controlling interest. AFAL is a budgetary unit linked to the Planning, Management, and Financial Coordination Secretariat. As a financial institution, AFAL is subject to Central Bank supervision and inspection, and is required to follow National Monetary Council guidelines with respect to its composition and operations. AFAL

- will act as the financial agent for the socioeconomic programs and as manager of the funds provided by the state government.
- 4.2 **Organization for execution.** The executing unit, which will report to AFAL's manager, will have two project coordinators (one responsible for the initiatives to support the microfinance market and the other for technical assistance for company competitiveness and economic inclusion—the latter supported by a technical assistant), an accountant, and an assistant. An executive committee for subproject selection and evaluation will also be set up, with responsibility for pilot project evaluation and selection. The committee will have five members: the president of AFAL, a representative of the Federal University, a representative of the private sector, a MIF representative, and the project coordinator.
- 4.3 **Results-based disbursements.** Disbursements will be conditional on meeting targets to be determined together by the executing agency and the MIF. Attainment of the targets will not affect the project targets set out in the logical framework. Under the risk- and performance-based project management framework, 10% of the funding will be advanced, subject to the project conditions (see the executive summary). All subsequent disbursements will be made as requested by the executing agency, provided that it has met all targets. The amounts of successive disbursements will be determined on the basis of project spending requirements. Expenses incurred since the date the project eligibility date (17 March 2008) to a maximum of US\$50,000 will be recognized as local counterpart funding.
- 4.4 **Procurement.** The beneficiary will procure goods and services and consulting services for the project that have been approved in advance by the Bank, in accordance with the procurement plan. All procurement will be carried out according to the Bank's policies (documents GN-2349-7 and GN-2350-7) and the MIF guidelines, and reviewed ex ante.

V. MONITORING AND EVALUATION

- 5.1 **Project progress reports.** The executing agency will present the project progress reports to the Bank's Country Office in Brazil within 30 days after the end of each six-month calendar period. These reports must be in a format agreed on in advance with the MIF. The reports will describe the progress of the project, the extent to which the targets have been met, the outcomes and the extent to which they contributed to accomplishment of the project objectives, based on the logical framework and other operational planning tools. They must also describe any problems encountered during project execution and potential solutions. Within 90 days after the end of the project, the executing agency will present a final report to the MIF (final progress report) describing the outcomes, the sustainability plan, and the lessons learned.
- 5.2 **Financial monitoring.** The executing agency will set up and keep proper financial accounting, internal audit, and project filing systems, in accordance with the IDB/MIF accounting and audit rules and policies. The MIF will engage

independent auditors (firms or individual accountants) to perform annual audits of the financial statements. The cost of the audits will be defrayed out of the MIF contribution, according to Bank procedures.

- 5.3 **Evaluations.** Three annual evaluations and a final evaluation will be performed by independent consultants, selected and hired by the Bank. The financing will cover the cost of the evaluations. The first evaluation will take place 12 months after the first disbursement; the second 24 months into the project or when 50% of the financing has been disbursed, whichever comes first; and the third in month 36. The final evaluation will be performed when 95% of the funding has been disbursed. The first two evaluations will cover, amongst other elements: (i) the extent to which the outcomes and indicators in the logical framework have been attained, particularly those relating to the number of beneficiary enterprises and the development of promoter institutions; (ii) AFAL's efficiency; (iii) the selection system, based on the quality of projects selected; (iv) the extent to which groups in extreme poverty have access to the project; and (v) the effectiveness of the monitoring system. The third evaluation will consider: (i) AFAL's sustainability; (ii) the outcomes of the first subprojects; and (iii) the development of microfinance market innovations. The final evaluation will consider: (i) the number of families related to MSE project participants that have increased their incomes; and (ii) development of social capital in the target areas and evidence of public-private development promotion arrangements.

VI. PROGRAM BENEFITS AND RISKS

- 6.1 **Benefits.** The project will directly benefit 1,800 microentrepreneurs and 60 SMEs through the subproject to support local productive arrangements, value chains, and local competitiveness initiatives. Three microfinance institutions will also benefit directly and an indirect benefit will be the deepening and expansion of the market. The following will also benefit from the project: (i) communities where subproject activities have been carried out, particularly poorer communities; (ii) institutions in the different economic regions and the communities that have boosted their activities as a result of the project; and (iii) AFAL itself, which through the project will acquire knowledge and experience to support productive and social inclusion processes.
- 6.2 **Risks.** The main risks associated with this operation are: (i) difficulty of entrepreneurs and entities in cooperating under the project; (ii) the weakness of the executing agency (AFAL); and (iii) the limited technical capacity available in the state. To mitigate the first risk, specific activities involving linkage and training for entrepreneurs are planned and one specific activity is designed to build confidence and form networks of enterprises. To mitigate the second risk, the first component and part of the second will entail developing AFAL's capacity and organization and ensure there is private sector participation in its equity and representation on its board of directors. Lastly, the third risk will be mitigated by the component 3 activities for human resource training and technical assistance for the institutions

in the six economic regions, and AFAL's efforts to recruit human resources inside and outside the state.

VII. ENVIRONMENTAL AND SOCIAL CONSIDERATIONS

- 7.1 The present project will not entail negative social or environmental effects. In fact, given its focus on creating job opportunities for low-income communities, it is expected to have a positive social impact. The project has been accorded a classification of "C".
- 7.2 The subprojects will be aimed at social inclusion and the creation of sustainable employment, in order to improve the quality of life in the beneficiary communities. The program will not finance subprojects with negative social and/or environmental impacts, as defined in the MIF's exclusion list. To accomplish this aim, the MIF will participate directly in project selection.

BRAZIL
SUPPORT FOR PROMOTING PRIVATE INITIATIVES IN THE STATE OF ALAGOAS
(BR-M1059)
LOGICAL FRAMEWORK

| NARRATIVE SUMMARY | INDICATORS | MEANS OF VERIFICATION | ASSUMPTIONS |
|---|--|--|--|
| GOAL | | | |
| To contribute to the economic development of the state of Alagoas through the expansion, diversification, and modernization of MSMEs. | Three years after the end of the project: <ul style="list-style-type: none"> - 50% of beneficiary families increase their income by 20%. - 50% of beneficiary companies increase their sales by 35% and their profitability by 20%. - 50% of beneficiary companies belong to nontraditional sectors such as tourism, fish farming, and fruit farming. | <ul style="list-style-type: none"> - Statistics from the state of Alagoas - Surveys and ex post evaluation by the executing agency, in comparison with the baseline | <ul style="list-style-type: none"> - Macroeconomic and political conditions in the state of Alagoas and Brazil remain stable. - There are no natural disasters affecting the subproject areas. |
| PURPOSE | | | |
| To consolidate an innovative model of a public-private development agency which, through pilot projects, promotes economic inclusion and facilitates MSE competitive development. | By the end of the project: <ul style="list-style-type: none"> - AFAL is operating with at least 49% of its capital is privately financed. - 1800 microenterprises and 60 SEs¹ have benefited from technical assistance and access to financing. - 50% of the subprojects are sustainable - AFAL maintains promotional activities through the business promotion subprojects. - At least 50% of the subprojects help to create new jobs in the sectors assisted. | <ul style="list-style-type: none"> - Project progress reports - Final evaluation report - Official statistics - Semiannual project reports prepared by the PEU - Data on progress compared to the baseline compiled at the start of the project (project monitoring system) | <ul style="list-style-type: none"> - The subprojects are integrated into local, state, and regional economic development dynamics. - AFAL maintains its political independence. - AFAL attains the sustainability indicators necessary to operate as a development agency (Central Bank authorization). - AFAL is able to take public and private funds to develop its operations. |

¹ Small enterprises (promoters).

| NARRATIVE SUMMARY | INDICATORS | MEANS OF VERIFICATION | ASSUMPTIONS |
|--|---|---|--|
| COMPONENTS | | | |
| <p>Component 1 – Building technical capacity</p> <p>To consolidate AFAL as an institution of technical excellence and boost its capacity to interact with a network of public and private organizations making it more efficient in its development activities and more effective in offering services suited to MSMEs.</p> | <p>By month 12:²</p> <ul style="list-style-type: none"> - Personnel in AFAL's and project management areas are trained. - AFAL web site is readily accessible. <p>By month 15:</p> <ul style="list-style-type: none"> - 15% of AFAL's equity is privately sourced. <p>By month 24:</p> <ul style="list-style-type: none"> - A network of partner organizations offering services and financing in AFAL's five lines of action has been established, with at least 10 members. - A network of financial institutions seeking second-tier financing has been established, with at least four members. <p>By month 36:</p> <ul style="list-style-type: none"> - AFAL is financially sustainable thanks to the demand for financial resources from IFIs and the network of providers of nonfinancial services it has built up. | <ul style="list-style-type: none"> - Training plans - Project monitoring system - Project progress reports - Data on AFAL's web site - Interagency agreements - Capitalization of AFAL - Annual financial report - Midterm and final evaluation reports | <ul style="list-style-type: none"> - The technical personnel contracted has the capacity to implement the training and technical assistance received - AFAL's strategic plan and business plan present realistic indicators. - The private sector sees the benefits of capitalizing AFAL. |
| <p>Component 2 – Support for innovation and sustainability in microfinance institutions</p> <p>To design and implement a strategy to promote the Alagoas microfinance market.</p> | <p>By month 24:</p> <ul style="list-style-type: none"> - 3 microfinance institutions have received training in methodologies of evaluation, risk control, and financial management. <p>By the end of the project:</p> <ul style="list-style-type: none"> - 3 microfinance institutions have achieved the standards of excellence set by AFAL (arrears, innovation, and regional coverage) and at least 3 new institutions have entered the local market. - The microfinance institutions that received training increase their client coverage by an average of at least 20%. | <ul style="list-style-type: none"> - Outcome indicators of the 3 microfinance institutions - Project monitoring system - Project progress reports - Midterm and final evaluation reports | <ul style="list-style-type: none"> - The 3 microfinance institutions have implemented the standards of excellence set by AFAL. - Attractive local conditions exist to develop and expand microfinance services. |

² The months established in the logical framework are counted from the first disbursement of the MIF's contribution to the project.

| NARRATIVE SUMMARY | INDICATORS | MEANS OF VERIFICATION | ASSUMPTIONS |
|--|--|---|---|
| <p>Component 3 – Building the local foundations for development</p> <p>To support the process of building institutional and human capacity to create an environment conducive to development and execution of pilot initiatives in each of the state’s economic regions: the Atlantic coast, the San Francisco river area, the sertão (semiarid area), the Agreste, the Zona da Mata, and the metropolitan Maceió area.</p> | <p>By month 12:</p> <ul style="list-style-type: none"> - 15 public and private entities—potential subproject promoters—have been identified and evaluated (training requirements). <p>By month 24:</p> <ul style="list-style-type: none"> - 20 public and private entities have been trained in the areas identified to support the pilot initiatives. <p>By month 36:</p> <ul style="list-style-type: none"> - 20 public and private entities are linked to the subprojects. <p>By the end of the project:</p> <ul style="list-style-type: none"> - 20 public and private entities participate in pilot subprojects in 15 communities, benefiting at least 20 families per community (increase in employment and income). | <ul style="list-style-type: none"> - Agreements signed between public and private entities in excluded communities, and the subprojects - Data on the communities compared to the baseline - Project monitoring system - Project progress reports - Midterm and final evaluation reports | <ul style="list-style-type: none"> - Public and private entities in excluded communities see the benefit of becoming involved in the subprojects. - Excluded communities participate and are integrated into the project. |
| <p>Component 4 – Selection and implementation of pilot projects</p> <p>To support initiatives for local competitiveness to boost the competitive advantages of the six regions selected</p> | <p>By month 24:</p> <ul style="list-style-type: none"> - Between 5 and 8 subprojects start up and are in operation with the target beneficiaries: local productive arrangements, production chains, regions, and innovative initiatives. - Each region has at least one subproject started up and in operation. <p>By month 36:</p> <ul style="list-style-type: none"> - Between 10 and 15 subprojects are started up and in operation with the target beneficiaries: local productive arrangements, production chains, economic regions, and innovative initiatives. <p>By month 46:</p> <ul style="list-style-type: none"> - Between 16 and 22 subprojects are implemented and evaluated, with the final reports published on line. | <ul style="list-style-type: none"> - Contracts for executing the subprojects signed by the PEU - Project monitoring system - Project progress reports - Midterm and final evaluation reports | <ul style="list-style-type: none"> - The beneficiaries and participating institutions develop the pilot subprojects successfully. |

| NARRATIVE SUMMARY | INDICATORS | MEANS OF VERIFICATION | ASSUMPTIONS |
|---|--|--|--|
| <p>Component 5 – Monitoring and systemization of the lessons learned</p> <p>To illustrate the most effective ways of promoting and supporting basic development, disseminating the lessons learned and the project outcomes.</p> | <p>By month 12:</p> <ul style="list-style-type: none"> - Project monitoring system implemented on line. <p>By the end of the project:</p> <ul style="list-style-type: none"> - Case studies and lessons learned from the project disseminated to at least 20 institutions nationally, through publications, videotapes, events, etc. | <ul style="list-style-type: none"> - Project monitoring system and web page - Project progress reports - Midterm and final evaluation reports - Communications strategy documents and replicability plan | <ul style="list-style-type: none"> - The institutions involved continue to be interested in disseminating the outcomes and expanding the scope of the project. |
| ACTIVIDADES | | | |
| <p>1.1 Development of working methodologies</p> | <ul style="list-style-type: none"> • By month 6, methodologies have been established for project preparation, monitoring, and lessons learned by AFAL. • By month 24, the procedures and methodologies used have been evaluated. | <ul style="list-style-type: none"> - Document containing the methodologies for project preparation, monitoring, and lessons learned by AFAL | <ul style="list-style-type: none"> - The materials and training courses can be adjusted to the needs of the technical staff hired by AFAL under this component. |
| <p>1.2 Updating the business plan and development of AFAL's strategic plan</p> | <ul style="list-style-type: none"> • By month 6, an updated business plan is available. • By month 24, the strategic plan has been produced. | <ul style="list-style-type: none"> - AFAL's new business plan - AFAL's strategic plan | |
| <p>1.3 Training for AFAL's technical experts in project analysis, selection, and management</p> | <ul style="list-style-type: none"> • By month 4, AFAL's staff has been trained in administration, finance, and accounting. • By month 6, training has been provided in project analysis, selection, and management. • By month 12, training for AFAL's staff in administration, finance, and accounting has been updated. • By month 18, training in project analysis, selection, and management has been updated. | <ul style="list-style-type: none"> - Training plan in administration, finance, and accounting - Training plan in project analysis, selection, and management - List of persons trained | |

| NARRATIVE SUMMARY | INDICATORS | MEANS OF VERIFICATION | ASSUMPTIONS |
|--|---|---|--|
| 1.4 Exchange of experience and knowledge and mentoring | <ul style="list-style-type: none"> • By the end of the project, visits have been made to at least 2 national and 3 international development agencies, and 3 practical experiences have been carried out. • By the end of the project, 10 exchanges of AFAL staff have taken place with other regional and international development agencies. • By the end of the project, 6 missions involving management staff from other national and international development agencies have visited Alagoas. | <ul style="list-style-type: none"> - Monitoring reports by the missions | |
| 1.5 Design of AFAL's marketing plan and communications and promotion strategy | <ul style="list-style-type: none"> • By month 14, the marketing plan and the communications strategy, and the web site with databases on state and federal financing and subsidies available have been implemented. • By month 24, AFAL is being promoted in the state of Alagoas. | <ul style="list-style-type: none"> - The marketing plan and communications strategy developed | |
| 2.1 Strategy to promote the microfinance sector in Alagoas | <ul style="list-style-type: none"> • By month 12, a diagnostic assessment and a market study on microlending in Alagoas have been performed. | <ul style="list-style-type: none"> - The diagnostic assessment and the market study on microlending | <ul style="list-style-type: none"> - Microfinance institutions are interested in developing services in the Alagoas region. |
| 2.2 Design of innovative products and their dissemination to microfinance institutions | <ul style="list-style-type: none"> • By month 18, innovative financial and microfinance products have been designed. | <ul style="list-style-type: none"> - The financial and nonfinancial products offered to AFAL's clients | |
| 2.3 Pilot microfinance initiatives and technical capacity building | <ul style="list-style-type: none"> • By month 20, training and/or technical assistance activities have been initiated with 3 microfinance institutions. • By month 20, 3 microfinance institutions have received support in entering the Alagoan market. • By month 38, 3 microfinance institutions have implemented the microlending methodology and evaluation system, the operating and risk control systems, and the financial/ accounting system. | <ul style="list-style-type: none"> - Training plan - List of participants in training courses - Market data. The microlending methodology and evaluation system, the operating and risk control systems, the financial/accounting systems implemented in the companies | |

| NARRATIVE SUMMARY | INDICATORS | MEANS OF VERIFICATION | ASSUMPTIONS |
|--|--|--|--|
| 3.1 Institutional development of local public and private entities | <ul style="list-style-type: none"> By month 12, 6 communities and their public and private entities are trained. By month 24, 8 communities and their public and private entities are trained. By month 36, 6 communities and their public and private entities are trained. | <ul style="list-style-type: none"> Agreements and training plans with the communities and public and private entities List of participants in training courses | <ul style="list-style-type: none"> The local entities have the political will and basic institutional capacity to participate in project activities. |
| 3.2 Development and dissemination of technical capacity to establish networks of companies | <ul style="list-style-type: none"> By the end of the project, 30 strategic partnerships are established. | <ul style="list-style-type: none"> Agreements between companies | |
| 3.3 Development of technical capacity for social empowerment initiatives | <ul style="list-style-type: none"> By the end of the project, 15 communities are supported with a minimum of 20 families per community. | <ul style="list-style-type: none"> Training methodologies and plans used List of participating families by community | |
| 4.1 Development of guidelines for the competitive project fund | <ul style="list-style-type: none"> By month 2, the guidelines for the competitive project fund are ready. | <ul style="list-style-type: none"> Guidelines and formats developed | <ul style="list-style-type: none"> The beneficiaries present business and economically feasible projects in line with the project objectives: local productive arrangements, production chains, economic regions and innovative initiatives targeted to the base of the pyramid; import substitution and/or the MSME integration. |
| 4.2 Dissemination of information on calls for applications to the competitive project fund | <ul style="list-style-type: none"> By month 4, at least six workshops (one per region) have been held to publicize the call for applications to the competitive project fund (first call). By month 14, at least six new workshops (one per region) have been held to publicize the call for applications for the competitive project fund (second call). | <ul style="list-style-type: none"> Calls issued Documents and notices | |
| 4.3 Subproject selection process | <p>First call:</p> <ul style="list-style-type: none"> By month 6, at least 50 profiles have been received. By month 8, the evaluation and preliminary selection of the profiles has been carried out. By month 10, the subprojects have been formulated. By month 11, 100% of the subprojects received have been evaluated. By month 12, between 6 and 8 subprojects have been selected. | <ul style="list-style-type: none"> Methodology used for the selection and evaluation of profiles and subprojects Profiles presented and evaluated Subprojects evaluated Subprojects approved | |

| NARRATIVE SUMMARY | INDICATORS | MEANS OF VERIFICATION | ASSUMPTIONS |
|---|--|--|--|
| | Second call: <ul style="list-style-type: none"> By month 14, at least 70 profiles have been received. By month 16, the evaluation and preliminary selection of the profiles has been carried out. By month 18, the subprojects have been formulated. By month 19, 100% of the subprojects received have been evaluated. By month 20, between 10 and 15 subprojects have been selected. | | |
| 4.4 Precursor subprojects | <ul style="list-style-type: none"> By month 3, at least 2 subprojects have commenced. | <ul style="list-style-type: none"> - Agreements signed with the beneficiaries - Financial reports by the PEU | |
| 4.5 Implementation of the subprojects | <ul style="list-style-type: none"> By month 12, the subprojects selected in the first call have commenced. By month 22, the subprojects selected in the second call have commenced. By month 46, all selected subprojects have commenced. | <ul style="list-style-type: none"> - Agreements signed with the beneficiaries - Financial reports by the PEU | |
| 5.1 Development and implementation of a project monitoring system | <ul style="list-style-type: none"> By month 6, the project monitoring system has been implemented and the baseline has been established. During the project, AFAL updates the information in the system. | <ul style="list-style-type: none"> - Monitoring system implemented - Baseline established | <ul style="list-style-type: none"> - Regional and national institutions are interested in the project outcomes. |
| 5.2 Documentation of the lessons learned from the project | <ul style="list-style-type: none"> In months 20, 36, and 46, an analysis document is produced to systemize the experience. By the end of the project, there are between 4 and 10 case histories of the subprojects completed. | <ul style="list-style-type: none"> - Publications and materials developed - Periodic reports by the PEU | |
| 5.3 National events to disseminate the project outcomes | <ul style="list-style-type: none"> By month 21, an event to disseminate the project outcomes has been held in the state of Alagoas. By month 47, at least two additional events have been held to disseminate the project outcomes—one regional and one national. | <ul style="list-style-type: none"> - Agenda and list of participants by event - Evaluation of the events by the participants | |

BRAZIL
SUPPORT FOR PROMOTING PRIVATE INITIATIVES IN THE STATE OF ALAGOAS
(BR-M1059)
ITEMIZED BUDGET

| Components | MIF | Local contribution | | Total | |
|--|------------------|--------------------|----------------|------------------|---------------|
| | | Cash | Kind | | |
| Component 1. Building technical capacity | 283,400 | 395,000 | 0 | 678,400 | 12.6% |
| Activity 1.1 Development of working methodologies | 92,200 | 0 | 0 | 92,200 | 1.7% |
| Activity 1.2: Updating the business plan and developing a strategic plan for AFAL | 14,700 | 12,700 | 0 | 27,400 | 0.5% |
| Activity 1.3 Training for AFAL's technical experts in project selection and management | 54,800 | 30,400 | 0 | 85,200 | 1.6% |
| Activity 1.4 : Exchange of experience and knowledge and mentoring | 92,100 | 66,900 | 0 | 159,000 | 2.9% |
| Activity 1.5 Marketing plan, and communications and promotion strategy for AFAL | 29,600 | 285,000 | 0 | 314,600 | 5.8% |
| Component 2. Support for innovation and sustainability in microfinance institutions | 29,200 | 626,800 | 0 | 656,000 | 12.1% |
| Activity 2.1 Strategy to promote the microfinance sector in Alagoas | 29,200 | 173,600 | 0 | 202,800 | 3.8% |
| Activity 2.2: Design of innovative products and their dissemination to microfinance institutions | 0 | 86,800 | 0 | 86,800 | 1.6% |
| Activity 2.3: Pilot microfinance projects and creation of technical capacity | 0 | 366,400 | 0 | 366,400 | 6.8% |
| Component 3. Building the local foundations for development | 204,400 | 362,600 | 0 | 567,000 | 10.5% |
| Activity 3.1: Institutional development of public and private local entities | 14,200 | 102,600 | 0 | 116,800 | 2.2% |
| Activity 3.2: Development and dissemination of technical capacity to establish networks of companies | 30,400 | 200,000 | 0 | 230,400 | 4.3% |
| Activity 3.3: Development of technical capacity for "social empowerment" initiatives | 159,800 | 60,000 | 0 | 219,800 | 4.1% |
| Component 4. Selection and implementation of pilot projects | 1,107,400 | 1,163,700 | 10,200 | 2,281,300 | 42.2% |
| Activity 4.1: Development of guidelines for the competitive project fund | 7,000 | 0 | 0 | 7,000 | 0.1% |
| Activity 4.2: Dissemination of calls to submit projects to the competitive project fund | 0 | 16,200 | 0 | 16,200 | 0.3% |
| Activity 4.3: Subproject selection | 0 | 67,500 | 0 | 67,500 | 1.3% |
| Activity 4.4: Precursor subprojects | 140,400 | 120,000 | 0 | 260,400 | 4.8% |
| Activity 4.5: Implementation of all subprojects | 960,000 | 960,000 | 10,200 | 1,930,200 | 35.7% |
| Component 5. Monitoring and systemization of the lessons learned | 74,000 | 100,300 | 0 | 174,300 | 3.2% |
| Activity 5.1: Development and implementation of a project monitoring system | 74,000 | 0 | 0 | 74,000 | 1.4% |
| Activity 5.2: Documentation of the lessons learned | 0 | 30,300 | 0 | 30,300 | 0.6% |
| Activity 5.3: National events to disseminate program results | 0 | 70,000 | 0 | 70,000 | 1.3% |
| Project executing unit | 277,200 | 396,000 | 105,600 | 778,800 | 14.4% |
| Annual evaluations | 50,000 | 0 | 0 | 50,000 | 0.9% |
| Annual financial audits | 68,000 | 0 | 0 | 68,000 | 1.3% |
| Contingencies | 95,400 | 39,800 | 0 | 135,200 | 2.5% |
| Impact evaluation account | 11,000 | 0 | 0 | 11,000 | 0.2% |
| TOTAL | 2,200,000 | 3,084,200 | 115,800 | 5,400,000 | 100.0% |