

DOCUMENT OF THE INTER-AMERICAN DEVELOPMENT BANK

COSTA RICA

SOCIAL ENTREPRENEURSHIP PROGRAM FINANCING AND TECHNICAL COOPERATION PROGRAM

SUPPORTING THE INTEGRATED ORGANIC PRODUCTION SYSTEM FOR SMALL-SCALE FARMERS IN TALAMANCA

(SP/TC-02-04-01-4)

~~This document was prepared by the project team consisting of: Fernando Campero (SDS/MSM), Team Leader; Eduardo Cucinelli (consultant); René Cajina (COF/CCR); Kevin McTigue (LEG/OPR); and Leyda Fajardo (LEG/OPR).~~

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EXECUTIVE SUMMARY

Executing agency: Asociación de Pequeños Productores de Talamanca [Talamanca Association of Small-scale Farmers] (APPTA)

| | | | |
|-------------------|----------------------------|---------|---------|
| Financing: | European Commission | US\$* | Euros |
| | Financing: | 415,000 | 368,520 |
| | Technical cooperation: | 200,000 | 177,600 |
| | Local | 100,000 | 88,800 |
| | Total: | 715,000 | 634,920 |

The resources will come from the European Community Special Fund for Microenterprises, which is administered by the Bank. The Bank's commitment will be denominated in euros.

* Exchange rate: US\$1.00 = €0.888 (as of 14/VIII/2003)

| | | |
|------------------------------|----------------------|-----------|
| Terms and conditions: | Amortization period: | 12 years |
| | Grace period: | 60 months |
| | Execution period: | 48 months |
| | Disbursement period: | 54 months |
| | Interest rate: | 2% real |

The grace period will apply solely to amortization of the financing, not to the interest. Maintenance of value will be added to the two-percent interest rate and will be determined based on the annualized producer price index (PPI) from the last six months, using the Dirección General de Estadística y Censos [Statistics and Census Bureau] or another official agency as the source. The debt will be denominated in local currency.

Problem the project seeks to resolve: The Talamanca region of Limón province in southeast Costa Rica has a predominantly rural population of indigenous origin with low levels of socioeconomic development and high indices of poverty (49.7% of the population lives in poverty). In all, 97% of the population works in agriculture, and small-scale farming is the main economic activity for many of the region's inhabitants.

Small-scale farmers in this region face many weaknesses and obstacles, which prevent them from better developing their economic potential, aspiring to boost their income, and beginning to overcome poverty. These obstacles are associated with: (i) low productivity and low-quality production in farms; (ii) difficulty gaining access to credit for working capital and productive investments; (iii) the absence of infrastructure and working capital for marketing; and (iv) insufficient business organization and inadequate capacity in institutions offering sustained, efficient marketing and production support services to small-scale farmers.

APPTA, which operates in the area and has obtained organic certification for more than 2,000 hectares of crops, does not have sufficient working capital and needs to strengthen its business structure and organization, to enable it to fully develop the market potential for organic products from the region.

Objectives:

The project's **general objective** is to improve the socioeconomic conditions of small-scale farmers in the Talamanca region, by helping to consolidate and expand their integrated organic production system through increased farm productivity, improvements to the quality of their organic crops, and better product marketing.

The **specific objectives** are to: (i) improve organic crop quality and productivity; (ii) help small-scale farmers gain access to credit for production and marketing; (iii) promote and improve the marketing of various organic products, through financing for collection infrastructure and working capital; and (iv) strengthen the executing agency's (APPTA) institutional capacity to provide efficient marketing services and production support to small-scale farmers.

Description:

The project is divided into two components: (i) one reimbursable financing component; and (ii) one nonreimbursable technical cooperation component.

1. Financing component (US\$415,000). These funds will finance three subcomponents: (i) a credit program for small-scale farmers in Talamanca; (ii) a working capital loan for APPTA to market organic products; and (iii) investments to facilitate collection and the logistics of crop marketing operations.

- a. *The credit program for small-scale farmers* (US\$117,000) will finance working capital needs (such as organic fertilizers, seeds, and pheromones) and investment (small-scale infrastructure for post-harvest processing) for organic crop production (primarily banana and cacao) for 95 to 115 small-scale farmers. It will be administered as a trust by a specialized financial institution with experience in rural credit.

- b. *The working capital loan for marketing* (US\$278,000) will finance the marketing and exportation of organic products grown by small-scale farmers in the region. It will promote the marketing of cacao, banana for consumption as fresh fruit or for purée, and the sale in domestic and foreign markets of roughly 20 organic horticultural products grown by some 850 farmers.
- c. *Investments in marketing infrastructure and equipment* (US\$20,000) will be used to equip a cacao processing plant laboratory and to purchase small laboratory equipment and equipment for transporting crops from remote farms to final loading points.

2. Nonreimbursable technical cooperation component (US\$200,000). These funds will be used to improve organic production by small-scale farmers and strengthen APPTA's administrative, management, and business capacity. They will finance: (i) direct training for farmers on organic production of cacao, banana, and other crops, providing training materials and instructors; (ii) the hiring of experts, field workers, and specialists on a temporary basis; (iii) the hiring of a marketing expert to draft a comprehensive marketing plan; (iv) the hiring of a business expert to help APPTA organize the marketing process; (v) implementation of promotional activities stemming from the business plan; (vi) the hiring of an environmental specialist; (vii) the hiring of an accountant to build APPTA's administrative capacity for project execution; (viii) small communications, transportation, and computer equipment for APPTA; and (ix) the hiring of a finance expert to advise APPTA on selecting and negotiating with a specialized financial institution to administer the small-scale farmer credit program. Technical cooperation proceeds will also finance a workshop to kick off the project, two evaluations (midterm and final), and four annual external audits.

Environmental and social review:

The Committee on Environment and Social Impact (CESI) reviewed this operation at its 31 May 2002 meeting. Its recommendations were taken into account in preparing the financing and technical cooperation proposal.

Beneficiaries:

The direct project beneficiaries will be roughly 850 low-income small-scale farmers in the canton of Talamanca and their families. Nearly 80% of this group is made up of Bribris and Cabecar indigenous ethnic groups. Some 25% of the farmers are women. The farmers will benefit through increased marketing of their organic products, particularly banana for consumption as fruit, for purée, and for other uses; cacao; and 20 other diversified products for the domestic market. Nearly 70 organic banana farmers and 45 farmers who grow both banana and cacao will also receive technical support

and financing to boost product quality and plot yields, producing a demonstration effect that could later be replicated by other farmers in the region.

Risks:

There are three main risks: (i) that the farmers do not assimilate the technological innovations enough to sustain ongoing quality production in the quantities sought to fulfill and develop business commitments; (ii) that APPTA, which has been downsized as a result of financial cuts, would be overburdened by a multiplicity of tasks, negatively impacting its business function and affecting market development and consolidation of its current client base; and (iii) that natural risks could damage production and affect repayment of the loans.

The risk of inadequate assimilation of technological innovations will be mitigated by APPTA's experience with training and direct technical assistance in the field using proven methods. Nonetheless, this experience will be supplemented by the support of experts selected from among qualified professionals in Costa Rica who have experience working with communities of small-scale farmers.

The risk that APPTA will be overburdened by a multiplicity of tasks and insufficient business organization will be mitigated through the work of a business officer, contracted under the project for two years. In addition, nonreimbursable technical cooperation proceeds will be used to hire a business planning and marketing expert to bolster APPTA's business area and produce a marketing plan that encompasses all the products. These measures will not only strengthen that specific area, but will also relieve the current general manager and production director of some of their work, allowing for a better distribution of tasks and boosting the efficiency of APPTA's human resources. They will have a direct positive impact on market development and will allow for better integration of the Association's production and business procedures. Lastly, APPTA will provide technical assistance and training on cultivation and handling methods to minimize the potential adverse impact of pests.

**The Bank's
country
strategy:**

The Bank's strategy with Costa Rica (described in document GN-2263, 16 June 2003) supports the objectives the Government of Costa Rica sets out in its National Development Plan (PND), i.e. reducing poverty in the long term and achieving sustainable growth driven by increased competitiveness in the medium term. The proposed project is consistent with both of those objectives. To help boost productivity in the country, the strategy provides for supporting the transformation of existing production models to allow for sustainable rural development and better use of natural resources, particularly in border regions. This operation was listed in the Bank's

2003 Operation Program for Costa Rica, which is attached as an annex to the country strategy (GN-2263).

**Coordination
with other
official
development
institutions:**

The project complements national and international cooperation initiatives and projects under way in Costa Rica. The executing agency receives technical support in areas that complement the project from the Tropical Agronomic Center for Research and Training (CATIE) program, with Dutch cooperation and World Bank funds, through the Global Environment Facility (GEF). The project is also within the scope of a biodiversity project being executed by Conservation International.

Rationale:

The project is justified because: (i) it will have a major impact on the income of rural families, by consolidating an integrated system that encompasses cultural ethnicity, ancestral agricultural tradition, biodiversity, and organic production sustainability; (ii) it creates development in one of the poorest sectors in the country, with the additionality of benefiting 36 communities of two indigenous ethnicities; (iii) it strengthens an innovative, one-of-a-kind institution for the development of small-scale farmers in Talamanca; and (iv) it will support APPTA's effort to establish market niches for organic products from the Talamanca region, with more stable prices and premiums for the social value added by the Association (fair trade and respect for biodiversity and indigenous culture), through improvements to farm production and marketing.

**Special
contractual
clauses:**

As a condition precedent to the first disbursement of funds from the **financing component**, APPTA must present the following to the Bank's satisfaction:

- a. For funds in the **credit program for small-scale farmers subcomponent**: (i) a trust agreement signed by APPTA and the specialized financial institution selected to administer the credit program; (ii) the final Credit Regulations governing the program, duly approved by APPTA's Executive Board and agreed to with the specialized financial institution; (iii) a brief technical report showing: (a) the technical and economic feasibility of the small farm infrastructure that will be financed for processing organic banana for consumption as fruit; and (b) satisfactory progress in the training and preparatory technical assistance activities for farmers on issues related to investments made with credit program proceeds; and (iv) evidence that an escrow account has been opened in a commercial bank that will accumulate, in advance, the equivalent of the next repayment installment in the credit component;

- b. For funds in the **working capital loan subcomponent**, evidence that the Association's Executive Board has approved: (i) the final regulations governing management of the working capital loan; and (ii) APPTA's business plan;
- c. For funds in the **subcomponent for investments** in marketing equipment and infrastructure, the technical and budget breakdown of the equipment that will be procured with these resources.

For the remaining funds in the financing component, the Bank and APPTA will agree on a disbursement schedule, at least on an annual basis. Disbursements will be contingent on the progress exhibited in the performance indicators and adequate execution of the technical cooperation component.

As a condition precedent to the first disbursement of funds in the **nonreimbursable technical cooperation component**, APPTA will present to the Bank's satisfaction the terms of reference of the consultants to be hired during the first six months of the project, including the business officer.

After the general conditions precedent have been met, an advance of up to US\$5,600 in technical cooperation funds will be authorized to: (i) hire a consultant to help APPTA select the specialized financial institution to administer the credit program and negotiate the corresponding trust agreement; and (ii) hold a workshop to kick off the project. For over 40% of the technical cooperation funds to be disbursed, disbursements under the financing component must have begun.

Revolving fund:

The Bank will establish a revolving fund with up to 20% of the total project financing component, for prompt, timely provision of funds from that component.

Reports and evaluations:

Reports. APPTA will submit to the Bank, within 30 days of the end of each six-month period, *reports on project progress* and use of Bank funds. They will include: (i) a description of the progress made in implementing the project execution plan and project indicators, together with a list of the main achievements and difficulties encountered in meeting project goals and objectives; (ii) updated performance indicators and an updated project execution plan for the following 12 months, including steps for overcoming the hurdles identified; (iii) information on the benefits small-scale farmers have obtained in economic terms and in terms of training and technical assistance on production and marketing issues; (iv) information on

strengthening APPTA and its achievements; (v) a statement on the use of Bank funds and counterpart contributions; (vi) information on the operation of the trust and the performance of the specialized financial institution and the loan portfolio; and (vii) information on APPTA's financial statements. The final report must contain a summary of achievements, based on the original objectives and indicators.

Within 120 days of the end of each fiscal year, APPTA will present a report to the Bank containing the financial statements for both project components and the activity of the special accounts, audited by an independent auditor acceptable to the Bank. The budget includes funding for that purpose. APPTA will also present its annual financial statements signed by a certified public accountant.

Evaluations: To ensure that project execution is adequate and the proposed objectives are met, the Bank will use technical cooperation funds for two evaluations to be conducted. A midterm evaluation will be conducted when 50% of the financing component has been disbursed. It will measure, *inter alia*, the performance of the executing agency and the specialized financial institution, progress made in fulfilling the performance indicators, the performance of the loan portfolio (credit program for small-scale farmers) put in a trust in the selected financial institution, to be able to make recommendations to improve handling of loan proceeds, if necessary, and the level of the project's impact on the environment. The final evaluation will be performed when 100% of the financing component has been disbursed. The Bank's Country Office in Costa Rica will directly hire and supervise the persons conducting the evaluation.

The Bank will review the findings and recommendations emanating from the progress reports and evaluations. If significant shortcomings in project execution are detected, the Bank may suspend disbursements until APPTA has taken satisfactory steps to remedy them.