

DOCUMENT OF THE INTER-AMERICAN DEVELOPMENT BANK

EL SALVADOR

SOCIAL ENTREPRENEURSHIP PROGRAM

EXECUTIVE SUMMARY

**PRODUCTION OPPORTUNITIES FOR SMALL RURAL PRODUCERS
(PRORURAL)**

(ES-S1008)

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I. BASIC INFORMATION ON THE PROGRAM

A. Executing agency

- 1.1 Cooperative for Assistance and Relief Everywhere, Inc. (CARE), through its office in El Salvador.

B. Amount and source of financing

	IDB	CARE	Total US\$
Nonreimbursable financing	600,000	400,000	1,000,000
Nonreimbursable technical-cooperation	<u>150,000</u>	<u>150,000</u>	<u>300,000</u>
TOTAL	750,000	550,000	1,300,000

Source: Net income of the Fund for Special Operations (FSO).

C. Terms and conditions

- 1.2 **Periods:** The program will have an execution period of 36 months and a disbursement period of 42 months.
- 1.3 **Currency:** U.S. dollars.

D. Statement of no objection

- 1.4 In a communication dated 22 May 2006, the Technical Secretariat of the Office of the President of the Republic of El Salvador indicated its no objection to the Bank financing for the program.

E. The problem to be addressed

- 1.5 El Salvador has a population of 6.76 million inhabitants,¹ 43% of whom live in poverty. At least 28% of the population have left the country (2,660,000). In the last

¹ Household and multipurpose survey, 2004.

- 15 years, El Salvador has stood out as a leader in economic freedoms.² While the reforms have resulted in economic growth, wide disparities in growth between sectors persist, competitiveness has deteriorated, and inequitable situations make social capital formation difficult and favor emigration on account of the lack of opportunities. Sixty-seven percent of employed Salvadorans work in one of three branches of activity: crop and livestock farming, manufacturing, and commerce, hotels and restaurants. The new free trade agreements with the United States and Central America (CAFTA) that come into effect in 2006 present a good opportunity for the country's economic expansion and a challenge for small entrepreneurs and producers.
- 1.6 Despite the economic growth in recent years, small producers and microentrepreneurs in rural areas continue to be mired in poverty. Despite their productive potential, these groups experience financial, institutional, technological, and productive difficulties that prevent them from producing regularly the volume of goods of the quality and at a cost that would permit them to compete in a value chain. The economic and social exclusion in which these groups live hampers their access to basic, financial, and business development services. It is therefore necessary to develop mechanisms to allocate resources competitively to productive groups which, because they are marginalized and scattered, find it difficult to access services available on the market and are, therefore, unable to improve their managerial, technological, productive, or organizational skills in order to effectively provide services to different value chains.
- 1.7 **The IDB and the Social Entrepreneurship Program (SEP) in El Salvador.** From the time the SEP was established in 1978 until December 2005, the IDB has identified and supported 28 productive initiatives in El Salvador for more than US\$12.6 million, whose objective has been to increase economic opportunities and promote social equity in poor and marginalized groups, by providing technical assistance, financial, social, and/or community development services for the target population. The support was provided mainly in the areas of marketing, agricultural production, crafts, and manufactures. Over these 27 years of experience with the SEP, some of the main lessons learned include: (i) the need to promote the organization, collective development, competitiveness, and productivity of small entrepreneurs and producers with a view to securing greater market share and to linking them to trade and economic development policies, particularly in light of the greater commercial openness deriving from the free trade agreements; (ii) owing to the country's size, in the projects that have been identified, the problems of a large number of these collective development groups could be resolved with investments of between US\$30,000 and US\$120,000 and it is not efficient to address these initiatives individually through the SEP; and (iii) to

² The Index of Economic Freedom is composed of different variables, the principal ones being: tax burden, the regulatory framework for foreign investment, the tariff structure, financial system regulation, monetary policy, and the existence of black markets. The lower the value, the higher the level of economic freedom. Salvador has an index of 1.25, the lowest in Latin America and the Caribbean.

achieve greater effectiveness and impact of the resources channeled to these productive groups, reliable and efficient intermediary organizations need to be developed and strengthened to assist small rural and urban entrepreneurs and producers and support them closely in project execution.

- 1.8 **Productive initiatives with IDB contributions of under US\$100,000.** In 2004 and 2005, three instruments were introduced to finance projects that require investments of under US\$100,000. In El Salvador, the first instrument, the Synergy Facility, promoted SEP productive projects to benefit small producers and microentrepreneurs. To accede to this facility, they had to obtain cofinancing from private companies as part of their corporate social responsibility. The beneficiary areas included waste recycling, development of agricultural suppliers, strengthening of female microentrepreneur groups, economic integration of young people, productive restructuring, strengthening of the competitiveness of rural microenterprises, and ecotourism. The second instrument, the MIF small projects program delegated to the Country Offices, has financed projects to support competitiveness and productivity, particularly in agriculture, business, and tourism. Last, in Honduras, a third instrument was established that consists of an SEP facility (FAPES), which has financed projects for agricultural transformation and marketing, and support for the competitiveness and productivity of microenterprises and small businesses. In El Salvador alone, more than 50 financially viable proposals were identified through the first two instruments, although just 15 received assistance.
- 1.9 The Bank carried out a process of identification and assessment of entities that could serve as executing agencies for the program.³ Based on these assessments, Cooperative for Assistance and Relief Everywhere, Inc. (CARE) was identified as having the necessary experience to serve as executing agency through its office in El Salvador. It has been operating in El Salvador since 1979 and in 2005 it executed projects in the country worth more than US\$10 million in local development, productive projects, health care, education, and emergency assistance. Productive projects targeted to market access and local economic development account for 10% and projects with partnership-creation components for 40%. Both percentages are projected to grow through a program financed by CARE International UK for public-private partnerships in Latin America. Under a contract with the Ministry of Agriculture and Livestock (MAG), CARE is currently administering five of the country's 10 agribusiness centers, as part of the agribusiness restructuring program financed by the IDB, with satisfactory execution.

³ Five institutions were studied: Fortalecimiento Social [Social Strengthening] (FORTAS); CARE El Salvador, Fundación Salvadoreña para la Salud y el Desarrollo Humano [Salvadoran Foundation for Human Health and Development] (FUSAL); Sistema de Asesoría y Capacitación para el Desarrollo Local [Advisory and Training System for Local Development] (SACDEL); and Fundación para la Educación Salvadoreña Integral [Foundation for Comprehensive Education in El Salvador] (FEDISAL). The report on the identification, analysis, and selection of the executing unit performed by COF/CES, with support from SDS/MSM, can be consulted in the technical files of COF/CES.

- 1.10 With its seven offices outside the capital, CARE can provide national coverage and has also identified unmet demand for small-scale financing by associations and groups of small rural producers. Also, as El Salvador is the Central American headquarters of CARE, the organization has expressed interest in a partnership with the Bank that would permit it to systematize and replicate the experience in other countries of the region.
- 1.11 The program proposes an instrument administered and executed by the private sector, which will provide efficient and decentralized nonreimbursable financing for small-scale productive initiatives, through a deconcentrated execution mechanism that will offer close support for identifying and executing those projects and reducing their transaction costs. The nonreimbursable nature of the financing is justified by the poverty, marginalization, and exclusion of the beneficiaries who will have access to the funds. Also, the program design involves a system to monitor each project to ensure the investments and Bank's resources are used and applied properly.
- 1.12 **Beneficiaries.** The project beneficiaries will be productive groups living in poverty, marginalization, and/or social exclusion in the country's rural areas. Those groups can present their initiatives through nongovernmental organizations established as community improvement associations, foundations, or nonprofit associations, cooperatives, or any other legal entity that represents them. The eligibility criteria for the entities and proposals to access program funds are described in Annexes VII-A and B.

II. THE PROGRAM

A. Objectives and purpose

- 2.1 PRORURAL's main objective is to help improve the quality of life of families that live in rural areas by creating economic opportunities for poor, marginalized, and excluded productive groups in El Salvador. The purpose of PRORURAL is to create an instrument that poor groups can use to compete for nonreimbursable financing for production-oriented projects that will improve their standard of living.

B. Description

- 2.2 PRORURAL is a program to be executed and administered by CARE, which will be responsible for all the counterpart funds. Through PRORURAL, agricultural and nonagricultural production-oriented projects will be financed in rural areas, to help expand economic opportunities for productive groups at the base of the pyramid which, although they live in poverty and/or marginalization, have the potential to be competitive.

- 2.3 The production-oriented projects will need to comply with the following eligibility criteria: (i) demonstrate that they have a direct impact on poor and marginalized social groups that lack access to financial, business development, and other support services to improve their livelihood; (ii) create new employment opportunities, strengthen existing jobs, and/or improve the income and well-being of poor and marginalized groups; (iii) demonstrate their capacity to adequately generate income through the funded activities to ensure the viability of continuing to provide services for the end clients/beneficiaries after the project has ended; (iv) develop activities that are not harmful to the environment or human health and that do not lead to social exclusion. In the event that the project activities could have any adverse impact, mitigation measures must be included.
- 2.4 **Nonreimbursable financing component** (IDB: US\$600,000; CARE: US\$100,000; beneficiaries: US\$300,000). Resources under this component will fund small-scale production-oriented projects, selected on a competitive basis, that will have a positive impact on the incomes of poor and marginalized productive groups in the country's rural areas. These projects, in accordance with SEP policy, may involve commerce or services, or facilitate community development. The following are not eligible for financing under this component: (i) payment of dividends, debts, or recovery of equity investments; (ii) purchase of shares, bonds, or other personal property; (iii) consumer credit; (iv) leasing or purchase of land or commercial buildings as office space; (v) staff of the beneficiary organization who were already performing these functions before the project, although this item may be considered as a counterpart contribution in kind; and (vi) studies that are not directly related to the project's concrete productive activities.
- 2.5 The minimum amount to be financed with IDB and/or CARE resources will be US\$30,000 per project, and the maximum will be US\$120,000 per project. Bank and CARE resources may be used to finance up to 70% of each project. The counterpart funds may be provided by the project's beneficiary organizations and/or strategic partners. Since this program is a *pilot initiative*, two invitations for proposals will be issued and at least 10 projects are expected to be financed. The maximum execution period for projects financed under this component will be 18 months and the maximum disbursements period will be 21 months after the first disbursement of funds for the project.
- 2.6 The **evaluation criteria** to be used to select the projects to be financed with PRORURAL resources are: (i) capacity to create economic opportunities that contribute to local economic development and improve the quality of life, with priority being given to initiatives that promote equal opportunity in terms of gender and excluded groups; (ii) sustainability and financing; (iii) innovation in the use and application of technologies and methods; (iv) collective development and partnerships; (v) improvements in productivity and competitiveness; and (vi) corporate social responsibility, meaning that the proposal involves actions that will have an impact on employees and the community in which they work and promotes practices and behavior that favor health, the environment, and social

- inclusion. Annex IV-C describes how each of the criteria will be measured for the project proposals presented.
- 2.7 **Nonreimbursable technical-cooperation component (IDB: US\$150,000; CARE: US\$150,000).** Resources allocated to this component will be used to finance the activities and consulting services relating to: (i) program promotion, dissemination, and knowledge management; (ii) administration and execution of the processes of inviting proposals, analysis, selection, control, and monitoring of the projects to be financed with resources under the program's nonreimbursable financing component; and (iii) a launch workshop and program evaluations and audits.
 - 2.8 A program technical unit will be established at CARE in El Salvador for program execution.⁴ An evaluation committee of CARE representatives will be set up for project evaluation and competitive selection. At least three people from public or private institutions related to the business sector, business associations, and/or associations of Salvadorans living abroad, with experience in working with the rural productive sector, will be appointed to the committee as guest members. The Bank will review project eligibility and approve the projects for financing with Bank resources.
 - 2.9 The program Operations Manual explains in detail how each of the above-mentioned activities will be carried out.

C. Sustainability

- 2.10 The program is expected to be sustainable, based on CARE's strategic projections to continue leveraging funds from other multilateral and bilateral, public and private, national and international sources of development cooperation.
- 2.11 In terms of the sustainability of projects to be financed under this program, each project must demonstrate its capacity to generate value added in the activities carried out by the beneficiaries, without the support of funding. Also, they must demonstrate their capacity to distribute the project's benefits equitably among the groups of end beneficiaries and to promote the institutional and financial sustainability of the beneficiary organizations. The plans of operations for projects to be financed will contain indicators for sustainability/profitability of the activities and institutional sustainability. Lastly, workshops and other events will be held during the program execution period, whose objectives include planning project continuity and sustainability strategies. All of these aspects appear in the program Operations Manual (Annex V).

⁴ The plan of operations and details about the unit's organization are established in PRORURAL's Operations Manual (Annex V) and the other annexes that form part of the manual.

D. Expected outcomes and capture of benefits

- 2.12 To measure the program benefits captured by the target population, understood as poor and marginalized groups in rural areas, the following indicators have been established, which will be measured at program end: (i) at least 500 beneficiary rural families increase their net income compared to the baseline; (ii) the number of jobs in project areas (broken down by gender and excluded groups) have increased compared to the baseline; (iii) at least 10 initiatives that include the generation of direct benefits for poor and/or excluded groups, the creation of economic opportunities, the capacity for financial sustainability and continuity of gains, development of environmentally-friendly activities, health care, and social inclusion, are operating 36 months of program execution; (iv) at least \$1,000,000 will have been invested in a minimum of 10 initiatives by program end; (v) at least five beneficiary organizations have established partnerships that strengthen their administrative and/or business capacity by program end; (vi) two project selection processes have been held in 36 months, with at least 120 proposals submitted, at least 30 preselected, and at least 10 supported and financed; (vii) at least three local or international organizations act as partners in promoting and executing the program; (viii) at least five initiatives with innovative practices for working with companies, government, and civil society on behalf of poor communities and excluded sectors will have been documented and disseminated; and (ix) an effective plan will have been designed to systemize and track the learning objectives of a given initiative by program completion.

E. Bank strategy and related operations

- 2.13 The activities to be financed with program resources are consistent with the priorities of the Bank's strategy with el Salvador (CSP-ES), approved on 19 October 2005, whose main objective is to support poverty reduction in the country, through two strategic objectives: (i) to promote sustainable economic growth by increasing competitiveness; and (ii) to strengthen human capital and improve opportunities for the poorest segments of the population, particularly in rural areas and the most vulnerable groups. The facility: (i) will promote investments in the productive efforts of small rural producers and microentrepreneurs which will create opportunities for increasing family income; and (ii) will develop human capital and improve the opportunities of the very poor.
- 2.14 The activities to be financed with program resources will be coordinated with the activities of the project on public-private partnerships for local economic development in El Salvador (SP/SF-05-19-ES), with the agribusiness reconversion project (ES-0119, 1327/OC-ES), and with the project on rural consolidation of agroenterprises (ATN/SF-9476-SP/SF-05-12-ES), with a view to complementing efforts and obtaining information on productive groups that could be interested in acceding to PRORURAL resources. Also, the program will coordinate with the agribusiness centers financed by the Ministry of Agriculture to obtain information

on potential productive groups that would like to gain access to PRORURAL resources. One of those centers is administered by CARE.

F. Cooperation with other donors

- 2.15 Possibilities and opportunities for cooperation with other donors were identified during the program design phase, particularly with entities linked to CARE International (i.e. CARE UK and CARE USA). CARE UK has committed to provide the counterpart resources for project financing under the program. Partnerships will also be sought with development cooperation institutions that have projects aimed at the program target group, such as USAID, the German Technical Cooperation Agency (GTZ), the Spanish International Cooperation Agency (AECI) and the Japan International Cooperation Agency (JICA), among others.

G. Summary of the environmental and social review

- 2.16 The Committee on Environment and Social Impact (CESI) reviewed the program profile at its 21 April 2006 (meeting 16-06) and decided as follows: Projects that do not include activities considered harmful to the environment under El Salvador's environmental legislation will be eligible for financing with PRORURAL program resources. CARE will base its evaluation and selection of projects for financing with program resources on the "Guidelines for analyzing the environmental and social impact of IDB microenterprise operations." In any event, all projects that might have a controllable environmental impact must include financing for mitigation measures. Also, projects that promote sustainable and respectful management of the environment and the country's natural resources will be given favorable consideration.
- 2.17 The gender and social inclusion component will be actively promoted by encouraging projects that include methods for assuring equal opportunities and foster participation by women and excluded groups. This has been included in the eligibility, selection, and evaluation criteria of beneficiary organizations and projects (see Annexes V and VII). Specifically, the project evaluation criteria will examine whether the proposal will have a tangible social, economic, and environmental impact on the beneficiary groups. The eligibility criteria for the beneficiary organizations require them to present evidence of having made concrete contributions to or provided benefits for the community of a social, environmental, and/or employment nature. Projects that promote equal opportunities in terms of gender and excluded groups will be given priority.

H. Special conditions

- 2.18 As a condition precedent to the first disbursement of resources under the technical-cooperation component, CARE will provide, to the Bank's satisfaction, the cooperation agreement in which CARE International UK agrees to provide the

- counterpart funds for execution of the program's nonreimbursable financing component.
- 2.19 As a condition precedent to the first disbursement of resources under the nonreimbursable financing component, CARE will need to present to the Bank's satisfaction: (i) the final version of the Operations Manual; and (ii) the final version of the model agreement between the beneficiary organizations and CARE.
- 2.20 As conditions precedent to the disbursement of program resources to beneficiary organizations: (i) CARE may not disburse funds to beneficiary organizations under the nonreimbursable financing component until it obtains the Bank's no objection to the financing plans for each project approved, indicating the origin of the project funds (IDB, CARE, and other cofinancing sources, if any); (ii) not more than 30% of the resources under the nonreimbursable technical-cooperation component may be disbursed until the projects proposed in the first round under the program's nonreimbursable financing component have been approved.

I. Disbursements, reports, evaluations, and audits

- 2.21 **Mechanism for disbursement of Bank resources for the program.** Bank resources will be disbursed in accordance with Bank policies. To ensure that sufficient funds are available for disbursements for the approved projects, a revolving fund will be established not to exceed 30% of either the financing or technical-cooperation funds. Disbursements for project execution will be made directly by the Bank's Country Office in El Salvador into the account opened by CARE for the program. Disbursement requests will be submitted by CARE and payments will be made in U.S. dollars, depending on the specific needs of each project.
- 2.22 **Mechanism for disbursement of program resources to each project.** Disbursements for the PRORURAL projects will be made according to a justified disbursement schedule, and the first disbursement may not exceed 50% of the Bank's and/or CARE's resources.
- 2.23 **Procurement.** Procurements of goods and related services and services financed under the technical-cooperation component will be conducted in accordance with Bank procurement procedures, as set forth in documents GN-2349-7 and GN-2350-7 of February 2006. The procurement plan is attached as Appendix II.
- 2.24 **Indicators.** The program performance indicators are established in the logical framework, which is attached as Annex I. It will be verified that execution of each project and the specific cofinancing agreements between the beneficiary organizations and CARE comply with the objectives and contribute to the targets and indicators, as established. Also, each project financed with program resources will include performance indicators that are appropriate for the type of activity being carried out. Compliance with the indicators will be reviewed periodically by

- CARE and will form part of the examination performed by the external evaluator. The project indicators include preliminary *process indicators* such as: (i) improvement in processes, services, and outputs; (ii) efficiency in marketing and distribution processes, and (iii) partnerships established. The *outcomes indicators* include: (i) efficiency—operating expense ratio; (ii) increase in productivity—degree of production diversification, sales volumes, value added to production; (iii) increase in the number of jobs—jobs created and strengthened with the project; (iv) scope—number and characteristics of the beneficiaries and changes in their income; gender and social inclusion aspects, (v) increase in competitiveness; (vi) sustainability/profitability of activities and institutional sustainability; and (vii) training index and technical training coverage, among other possible indicators.
- 2.25 **Program reports.** CARE will deliver reports to the Bank’s Country Office in El Salvador within 60 days after the end of each six-month period. The initial report should include a business plan for the program for the first year of execution. The plan will be revised and updated semiannually during execution. The reports will also include the technical and financial implementation status for the program and the consolidated status of the individual projects. The reports will describe: (i) progress of each project and its budget performance; (ii) information on the status of each investment made with the funds for each project and the benefits being transferred to the beneficiaries; (iii) technical-assistance, promotion, dissemination, selection, evaluation, analysis, administration, and monitoring performed by CARE; (iv) results of the strategic partnerships achieved during program execution; (v) problems encountered and mechanisms to surmount them; (vi) compliance with the performance indicators for the projects and the program; and (vii) lessons learned in the process and recommendations to boost the effectiveness of the projects and the program.
- 2.26 **Monitoring and supervision of program projects.** CARE will use the following mechanisms for monitoring and supervision of projects financed with resources under the nonreimbursable financing component: (i) monthly reviews of technical and financial reports; (ii) recommendations on the use of the budget and activities compliance; (iii) reports on fields visits, which are to be paid at least once every two months during execution of each project; (iv) activities to strengthen internal processes for technical and financial control of each project; (v) disbursements against verification of compliance with the budgeted activities; and (vi) review and updating of the execution timetable and disbursements contingent on conditions in the project, sector, and the country; and (vii) support in establishing contacts and strategic partnerships.
- 2.27 **Program evaluations.** The cost of the midterm and final evaluations to be performed will be defrayed out of the Bank’s contribution. The *midterm evaluation of the program* will take place 12 months after the first invitation to submit projects. The evaluation will analyze the program execution mechanism as a whole and a representative sample of projects in execution. As for those projects, the evaluation

- will consider the following aspects: (i) the relevance of the evaluation criteria used for project selection and how well the projects meet those criteria in practice; (ii) the performance of the beneficiary organizations in using the funds disbursed and in executing the activities; and (iii) the level of compliance with the performance indicators of projects in execution.
- 2.28 With respect to CARE, the evaluation will examine its general performance in administering the program, which will include aspects such as promotion and dissemination, invitations for submissions, evaluation and selection of proposals, project monitoring, and financial management of program resources.
- 2.29 The *final evaluation of the program* will be done 15 months after the second invitation for submissions. This evaluation will focus on the program objectives and a representative sample of projects under way, looking in greater detail at the aspects broached in the midterm evaluation. It will also consider the effectiveness of the strategic partnership between the Bank and CARE and will offer the Bank inputs for decisions on whether the results indicate that the experience of financing initiatives using this modality may be satisfactorily replicated in the future.
- 2.30 **Audits.** During the operation and 120 days after the close of its financial year, CARE will present its own audited financial statements and audited statements for the nonreimbursable financing component. Also, the Bank's contribution will be used to commission a final audit of the technical-cooperation component, after it is completed.

J. Program risks and mitigating factors

- 2.31 The following risks have been identified. First, the performance by the technical unit to be set up in CARE for program execution may not be satisfactory. To mitigate this risk, the terms of the contract with the project coordinator will contain results-based performance indicators. Second, the beneficiary organizations may not have the minimum counterpart resources in cash. To mitigate this risk, the beneficiary organizations are required, as a condition, to contribute 30% of the total for each project financed with program resources, with just 10% of that amount in cash, while the rest may be in kind. This point was consulted and validated with a group of potential beneficiaries and will be stressed during promotion and dissemination. Third, natural disasters may affect the project areas. Although there is no mitigation for that risk, CARE has access to international institutional partners that offer funds to support regions affected by natural disasters.

K. Exceptions to Bank policy

- 2.32 An exception is requested to Operational Policy OP-706, "Social Entrepreneurship Program (SEP)," which requires the executing agency of an operation financed with SEP resources to be legally registered and established in the beneficiary country. The exception is requested because CARE, the entity proposed as program

executing agency, although it is a nonprofit institution organized and operating under the laws of the District of Columbia in the United States since 1979, has been authorized to operate in El Salvador, where it has a field office with the experience to manage projects financed by various international agencies.

- 2.33 The rationale for selecting CARE as the program executing agency is as follows: (i) it has the necessary experience for program execution and working with rural associations in El Salvador, where it has been active for more than 25 years; (ii) the program resources to be administered by CARE will be used in their entirety to assist the project beneficiaries, and CARE will provide a counterpart contribution of US\$250,000; and (iii) the legislation of the beneficiary country (El Salvador) presents no apparent obstacles to a foreign entity such as CARE serving as executing agency.