

## TECHNICAL COOPERATION PROFILE

Country	COLOMBIA		
Project Name	Expansion of locally-managed microloan funds to mitigate rural poverty		
Project Number	CO-S1002		
Project Team	Bernadete Buchsbaum (LEG), Christine Ternent (COF/CCO), Ana Lucía Muñoz (COF/CCO), Fermín Vivanco (SDS/MSM), Project Team Leader		
Date of Application	November 9, 2006		
Implementing Agency	Office of the Advisor to the Presidency for Special Programs (CPPE), attached to the Office of the President of the Republic of Colombia		
Funds	Korean Poverty Reduction Fund		
	Technical Cooperation	US\$400,000	80%
	Local Counterpart	<u>US\$100,000</u>	<u>20%</u>
	Total	US\$500,000	100%
Technical Responsibility	SDS/MSM and COF/CCO		
Tentative Dates	CRG (SDS)	May 2007	
	Final Approval	June 2007	
Implementation	24 months		

### I. RURAL POVERTY IN COLOMBIA

- 1.1 In Colombia about half of the population live below the poverty line (monthly per capita income of US\$118). However, this percentage increases to almost 70% in rural areas, where 42% of the population live<sup>1</sup>. Rural poverty has numerous underlying causes: the scarcity of formal employment and limited job qualifications limit economic growth in many small villages. As a result, empowering the rural population to achieve self-employed status and creating new income-generating activities are frequently regarded as the most effective ways to reduce poverty. Accordingly, entrepreneurial training and financing for the creation of new microenterprises are in high demand among the rural poor.
- 1.2 In this context, Colombia's Office of the Advisor to the Presidency for Special Programs (*Consejería Presidencial de Programas Especiales*, or CPPE) is applying a multidimensional approach to rural poverty reduction. This approach includes implementation of an initiative known as the Program for the Promotion of Rights and Constructive Networks for Peace (PDRCP) in 60 villages. In 50% of these villages, Banco Agrario is the only financial institution with a presence, while 40% are without a financial entity of any kind. In each municipality, the PDRCP program has established a special project called the "Municipal Social Support Network (*Red Social de Apoyo Municipal*, or RSAM)". Volunteers and representatives from community organizations and municipal and departmental agencies, for example, technicians from the National Training Service (*Servicio Nacional de Aprendizaje*, or SENA) participate in each RSAM are. Each of the 60 RSAMs has also established a Municipal Intervention Plan that seeks to reduce poverty and address social problems such as drug use, teenage pregnancy, juvenile delinquency, and other health and behavioral issues. Each Municipal Intervention Plan also includes microenterprise support activities, such as entrepreneurship training targeting women and youth, including training modules for business plan development. The Plans also include the establishment of self-managed microloan funds to finance new microenterprises. These activities have received a very positive response from the rural poor population. As a result, many new municipalities are taking steps to expand opportunities for entrepreneurship training and to increase the number of PDRCP microloan funds.

<sup>1</sup> Data from the National Planning Department (DNP).

- 1.3 At present, most of the families in these 60 municipalities are poor, with estimated household incomes of less than US\$200 per month<sup>2</sup>. Nationally, fewer than 20% of families with such low levels of income have access to financial services of any type, and fewer than 4% have access to credit<sup>3</sup>. The net result is that, in rural areas where extreme poverty prevails and where there is a total lack of formal businesses, physical infrastructure and financial institutions, opportunities for young people and their parents to gain access to financial institutions become critical.
- 1.4 **Locally-managed microloan funds.** As part of the Municipal Intervention Plans, and with a view toward helping to alleviate poverty, the PDRCP program established 60 rotating credit funds, with each fund receiving an initial capitalization of US\$4,500. The beneficiaries of these microloans are members of the various RSAM networks, i.e., parents of children up to age 25, and young men and women up to age 25 who meet certain requirements, such as school attendance for minor children, no use of child labor, and participation in at least 60% of RSAM activities. These activities, which are described in detail in the Municipal Intervention Plans, include training in the areas of entrepreneurship, basic business management, basic accounting and other activities focusing on strengthening the businesses launched by program beneficiaries. The RSAMs elect three institutional representatives to make up the credit committee, which is in turn charged with monitoring and following up on all microloans granted. To date, financing has been made available for 963 business plans, which in turn generate benefits for some 3,500 low-income individuals. These funds have enjoyed strong demand from new income-generating enterprises such as stores, tailor shops, service establishments, and restaurants, as well as crop production, food transformation and handicraft activities. Seventy percent of the borrowers are women.
- 1.5 **Graduation from the microloan funds.** Beneficiaries of PDRCP microloans who have satisfactorily paid off their initial loan receive RSAM support in submitting a business proposal to Banco Agrario, thereby obtaining access to the only formal banking institution having a presence in rural areas, an achievement that would be impossible without support of the type received from the RSAM. Banco Agrario is the only bank in many of the municipalities in which an RSAM has been established. This activity, which has been designed to transform members of the rural population into bankable credit subjects, requires support from trained community specialists with the ability to guide entrepreneurs in their efforts to secure funding from Banco Agrario.
- 1.6 **Development of productive projects for the poor rural.** Unlike most microlending programs that require micro entrepreneurial borrowers to have been in operation for more than a year, PDRCP microloans are focused primarily on the launching of new productive activities, a significant challenge in municipalities where economic activity is minimal. In addition, despite the existence of viable ideas for profitable businesses among the vulnerable population of the rural beneficiary municipalities served by the Program, these municipalities lack trained personnel to provide borrowers with appropriate project development and implementation guidance. Logically, this situation limits the implementation of income-generating projects and, in some cases, even leads to business failures.
- 1.7 **Operating challenges of the PDRCP national microlending network.** The work carried out by local credit committees, together with the support they receive from personnel working out of PDRCP headquarters (three staff members in Bogotá, plus nine volunteers), has served to ensure the satisfactory operation of the funds as regards the distribution of resources and the recovery of outstanding loans. However, credit committee members and RSAM personnel that support the local operation of rotating funds are in need of training to improve their microcredit management

<sup>2</sup> Strata 1 and 2; in most of the beneficiary municipalities, more than 80% of residents fall into these two strata.

<sup>3</sup> Survey of Financial Services in Colombia, World Bank 2002.

skills. In some municipalities, this unmet need for trained local staff and operational support is impacting negatively on microloan fund performance.

- 1.8 **The need for technical assistance in the network.** Since microenterprise support activities are managed autonomously at the local by RSAMs, the latter require strong technical support to ensure positive results in terms of both loan performance and training for new entrepreneurs. Technical support is currently provided by local volunteers who receive training from the PDRCP staff. Technical support includes advisory assistance for credit committees; implementation of systems for the various loan processes, such as disbursement, accounting, and collections; and general training in the various aspects of setting up a new business, with a particular focus on women entrepreneurs, as they comprise a majority of training and microloan applicants. However, local volunteers often lack the necessary qualifications to provide the training and technical assistance requested of them. Moreover, in those cases where their qualifications are sufficient, the network risks losing them to salaried job offers.
- 1.9 **Financial challenges facing the PDRCP national microlending network.** Based on the positive response to the rotating funds and the strong demand from municipalities, current plans call for an expansion of the microlending network to an additional 180 municipalities. Toward this end, the PDRCP program will need to put in place a standardized lending methodology since, at present, the methodology varies from one municipality to another. In addition, it will need to improve its accounting and financial information systems, in order to increase its ability to monitor the financial progress of the funds and prevent financial performance problems. Until this situation has been resolved, the PDRCP will be unable to grow financially, with the result that the financing and technical assistance needs of thousands of rural families will remain unmet and opportunities to develop income-generating activities will continue to be limited.
- 1.10 **Institutional needs.** The PDRCP program is impacting positively on the income of those members of the poor rural population that benefit from the loans: some 3,500 families in 60 municipalities. This impact will increase significantly when the program is expanded to include an additional 180 municipalities. Toward this end, the PDRCP requires technical support to enable it to: (i) train personnel in the management of both existing microloans and new undertakings; (ii) provide institutional strengthening to the microlending program network by standardizing loan management and administrative management processes and improving network information and reporting systems; and (iii) develop a viable and sustainable institutional solution that will make it possible to provide support to the program, expand it to the national level, and generate a scalable solution to the low levels of income among the rural population.

## II. OBJECTIVES AND DESCRIPTION

- 2.1 The project goal is to improve the living conditions of the rural poor by providing technical and financial support for the creation of new income-generating activities. The project purpose is to strengthen the strategy for reducing rural poverty currently being implemented by the Program for the Promotion of Rights and Constructive Networks for Peace (PDRCP).
- 2.2 The project focuses on strengthening the program's income-generating strategy through application of the following:
- 2.3 **Hiring and training of community specialists:** This component will ensure the availability of 15 trained community specialists for the 60 program municipalities (each trainer will operate in an average of four municipalities) that are currently working with resources made available by the rotating funds, while providing for the monitoring of the income-generating initiatives of young women and/or their families and ensuring the provision of support for the development of their businesses. These community specialists will strengthen the efficiency and effectiveness of the credit committees, the accounting-administrative management of the lending programs, and the

monitoring of income-generating initiatives and processes for recovering outstanding loans. In addition, the community specialists will work with those program beneficiaries that have successfully paid off their initial loan and refer them to Banco Agrario, where they will be able to obtain financing in greater amounts.

- 2.4 **Technical assistance to strengthen the RSAMs:** The income-generating strategy is being carried out under the direction of the credit committee, as a result of which ongoing training and monitoring of their work will be required. In this regard, it will be necessary to conduct two 1½-day workshops for each department. These training activities will improve the performance of locally-managed microlending funds and help the program to grow while keeping credit risk at an acceptable level. This component will also include updating training modules for rural women entrepreneurs and mechanisms to support the creation of associations of rural women-owned microenterprises. For this particular training module, support will be provided by a Korean organization, to be identified in coordination with the Korea International Cooperation Agency, having appropriate expertise.
- 2.5 **Institutional strengthening:** The project will support the PDRCP program in developing an institutional plan that will be effective, efficient and sustainable and that in addition will make it possible to scale up operations from the 60 current rural municipalities to a total of 240. This plan will be carried out with support provided by international technical personnel with expertise in the development of sustainable financial plans for grassroots organizations, through the establishment of one or more savings and loan cooperatives (SLC), one or more SLC networks, a nongovernmental organization (NGO) or NGO network, or some other viable institutional structure that would lead to the institutional consolidation of the program.
- 2.6 A study has recently been conducted on the achievements recorded by organizations such as the German Cooperative Confederation (DGRV) with the establishment of co-ops growing out of grassroots organizations in Mexico under the Patmir Program implemented by that country's Ministry of Agriculture, and the plan involving semi-autonomous funds from community banks or Community Credit Enterprises (CCE) currently being implemented by FINCA Costa Rica. In this regard, the project will provide financing to commission a feasibility study and to hire a team of experts that will be responsible for implementing a strategy for endowing the program with an institutional infrastructure that will ensure the sustainability and permanence of the locally-managed funds, by taking advantage of best international practices in this area. This technical assistance component could include cooperation to be provided by the National Federation of Credit Unions of Korea, or some other Korean institution specialized in rural finance and rural lending through grassroots organizations, as a component of the study and exchange activities.
- 2.7 **Projected results:** The direct beneficiaries of this project will be 2,000 vulnerable rural families. The projected results of the project are: (i) access by 2,000 new families to locally-managed loan funds, with support to be provided by the project's 15 community specialists; (ii) transformation of approximately 500 new entrepreneurs into bankable credit subjects who will successfully pay off their loans, receive advisory assistance and cooperation for their businesses, and obtain financing for their businesses in increased amounts from Banco Agrario; (iii) increase in the technical and institutional capacity of the PDRCP program, which will have the ability to generate performance reports and which will receive cooperation from a team of experts to assure satisfactory program performance, not only as regards its celerity in disbursing loan funds but also in terms of the quality of its loan recovery efforts, and (iv) the institutional consolidation of the PDRCP program's locally-managed funds, which will operate on a locally-managed and sustainable basis in the 60 initial municipalities, with the latter to be subsequently expanded to include 180 new municipalities.

- 2.8 **Long-term impact and sustainability.** The PDRCP Program will continue at least until the year 2010 in the above-referenced 240 municipalities. However, given the successful implementation of the program to date and the evidence of strong demand for the PDRCP intervention from many rural municipalities, it is conceivable that the locally-managed microloan funds will continue in operation for the long term, together with the training activities, which will be assumed by local governments. Toward this end, the third component of the project will help define the long-term sustainability of the locally self-managed microloan funds. Specifically, the project will provide financing to design and begin implementation of a sustainable institutional structure that will ensure continuation of the microloan funds beyond the conclusion of the PDRCP program.

### **III. Cost and Funding**

- 3.1 The project will have a total cost of US\$500,000, of which the Korean Poverty Reduction Fund will provide US\$400,000. The local counterpart of US\$100,000 will be provided by the PDRCP program. Annex I includes a preliminary budget. The terms for implementation and disbursement activities will be 24 and 30 months, respectively. Approximately 10% of the Koreana Poverty Reduction Fund contribution will be used on activities for exchanging knowledge with Korean institutions in the area of entrepreneurship for rural women and the creation of association of rural microenterprises in rural areas (component 2) and co-op models for rural finance (component 3).

### **IV. Implementing Agency and Implementation Mechanism**

- 4.1. The Office of the Advisor to the Presidency for Special Programs (CPPE) is an entity created in 2003 and attached to the Office of the President of the Republic of Colombia. CPPE's objective is to support the national government in building social equity. Toward this end, CPPE will make appropriate use of the advantages it enjoys as an entity operating at the highest level of government: credibility, ability to convene parties, management of cooperation resources, inter-institutional coordination, and channeling of the various types of aid for implementing programs and projects designed to benefit vulnerable population groups. CPPE carries out its programs in four priority areas: Promotion of Rights and Constructive Networks for Peace (which includes the rotating loan funds that will receive support under this technical cooperation), Community Health and Care, Early Childhood, and Community Participation and Social Mobilization. CPPE operates under the responsibility of the Advisor for Special Programs and has access to staff from the Office of the President of the Republic. CPPE has contacted the Korean Embassy for its other programs, and has received from the embassy a grant to work with disabled individuals. In some regions and municipalities, CPPE locally-managed funds began to operate with resources provided by cooperation received from the Government of the United States (USAID), the International Office for Migration (IOM), and the Andean Development Corporation (CAF), among other organizations. Agreements to govern the use of these resources have been signed with regional operators with the backing of CPPE, which is responsible for making the initial disbursement.
- 4.2. From the perspective of the Office of the President of Colombia, it has been observed that CPPE locally-managed funds serve to complement the policies and activities of Banca de las Oportunidades<sup>4</sup> since they reach population strata that, as a result of their level of poverty and their lack of access to formal banking services, are not served by financial institutions of any sort. In this same context, CPPE is also viewed as an incubator for future clients of formal financial institutions such as Banco Agrario, to whose microlending program CPPE members are referred

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<sup>4</sup> Banca de las Oportunidades is not a specific financial institution, but rather the sum total of a series of policies being implemented by the government and a number of instruments managed by Bancoldex, the government's public development bank, for the purpose of promoting access to financial services by low-income individuals, micro and small enterprises, with the ultimate goal of achieving social equity.

after successfully amortizing their initial loan. This alliance between the microloan funds and Banco Agrario will help ensure that the income-generating activities will become viable microenterprises, by facilitating access to Banco Agrario financing as a first step toward moving their microbusinesses into the economic mainstream. To become eligible for graduation to Banco Agrario credit, microloan beneficiaries will need to satisfactorily complete their training and loan repayments. During the Banco Agrario loan application process, which includes submission of a business plan, beneficiaries may receive support from the PDRCP community specialists, from the local SENA or, where agricultural or livestock activities are involved, from the municipal agro-specialists present in many towns. With this Bank-provided institutional support, CPPE locally-managed funds have the potential to evolve into a high-impact institutional network for promoting entrepreneurial activities in areas affected by rural poverty, as well as to generate income at the country's lowest socioeconomic levels.

#### IV. ENVIRONMENTAL AND SOCIAL STRATEGY

- 4.3. **Special issues.** The project team will focus particularly on the following special issues: (i) design of processes for selecting and training the community specialists to be hired with program resources; (ii) promotion of opportunities for technical collaboration and the exchange of experiences in rural finance between CPPE and at least one Korean organization; (iii) access to additional counterpart resources that will make it possible to further consolidate the rotating funds; and (iv) the environmental and social impacts of program activities and their subsequent mitigation.
- 4.4. **Environmental and social impacts and proposed next steps.** The project will be implemented in accordance with the IDB's Guidelines for Analyzing the Social and Environmental Impact of Microenterprise Operations. The rotating funds will provide resources for launching new undertakings by very low-income individuals and socially excluded groups in rural areas which in most cases lack the presence of functional financial entities. According to the Safeguard Screening Report, this project has been classified "C".
- 4.5. It is estimated that the project will proceed in accordance with the following schedule:
- Approval of the Profile: May 2007
  - CRG: May 2007
  - Final Approval: June 2007

Approved: May 8, 2007