

DOCUMENT OF THE INTER-AMERICAN DEVELOPMENT BANK

## **HONDURAS**

### **SOCIAL ENTREPRENEURSHIP PROGRAM**

#### **EXECUTIVE SUMMARY**

#### **NEW FINANCING MODELS FOR THE HIGH-VALUE AGRICULTURAL PRODUCTS *SECTOR* IN HONDURAS**

**(HO-S1019)**

#### **LOAN PROPOSAL**

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### **Information Available in the Project Technical Files**

DOC 1	Logical framework
DOC 2	Institutional analysis and execution of the operation with financial projections for the project
DOC 3	Plan of operations for the technical cooperation component
DOC 4	Performance indicators
DOC 5	Term sheet for loan negotiation
DOC 6	Summary of the project financial conditions
DOC 7	Milestones table
DOC 8	Minimum elements of the project credit regulations
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DOC 10	Financial statements for Del Campo 2007-2010
DOC 11	Procurement plan
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## **ABBREVIATIONS**

ACA	Programa de Acceso a Crédito para Agricultores [Access to Farm Credit Program]
EDA	Programa de Entrenamiento y Desarrollo a Agricultores [Farmer Training and Development Program]
GDP	Gross domestic product
MCA-Honduras	Millennium Challenge Account-Honduras
MIF	Multilateral Investment Fund
MSME	Micro, small, and medium-sized enterprises

## I. BASIC PROJECT INFORMATION

### A. Executing agency

- 1.1 Del Campo Soluciones Agrícolas, S.R.L. (Del Campo)

### B. Amount and source of financing

	IDB US\$	Counterpart US\$	Total US\$
Reimbursable financing:	700,000	400,000	1,100,000
Technical cooperation:	<u>250,000</u>	<u>107,000</u>	<u>357,000</u>
Total:	950,000	507,000	1,457,000

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

### C. Terms and conditions

Amortization period:	8	years
Grace period:	3	years for principal
Interest rate:	6%	annual
Currency:	dollars	United States
Disbursement period:	36	months

### D. Statement of no objection

- 1.2 The Ministry of Finance of Honduras has given its no objection to financing from the Bank for the project in a memorandum dated 29 October 2010.

### E. The problem to be addressed

- 1.3 **Agriculture in the Honduran economy and its financing.** Honduras is one of the least developed economies in Latin America. Following a decade of steady increases, in 2009, the country posted a GDP of US\$15.266 billion and a GDP per capita (purchasing power parity) of US\$3,743, both lower than the prior year by 2.1% and 3%, respectively. The Honduran economy has historically been dependent on banana and coffee exports, and although sources of national income have been diversified since the mid-1990s, agriculture continues to account for more than 12% of the national economic structure. The importance of agriculture is further corroborated by the fact that 35% of the country's labor force works in agriculture and 70% of the poor live in rural communities. However, one of the obstacles to agricultural development is bank financing. As of May 2010, only 3.5% of the US\$6.690 billion in bank loans to the private sector financed agricultural activities.<sup>1</sup> In addition, those resources are generally used to support agricultural export companies and large agricultural producers that employ technologies providing high yields per cultivated area and that have available collateral and the capacity for diversification at the level of their productive units.

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<sup>1</sup> Central Bank of Honduras. Statistical Bulletin. May 2010. [http://www.bch.hn/boletin\\_estadistico.php](http://www.bch.hn/boletin_estadistico.php)

- 1.4 **Farmers and access to credit under suitable conditions.** Honduran farming takes advantage of favorable conditions related to the country's climate, land, and location. Consequently, it has been identified as a high-value activity. The main products grown by Honduran farmers include tomatoes, onions, lettuce, sweet potatoes, jalapeño peppers, Swiss chard, and peppers. The market for horticultural products in Honduras has been favorable. For instance, commercial agents have emerged in the country that specialize in buying and selling horticultural products. One example is Hortifruti, a company specializing in the purchase, quality certification, logistics, storage, and distribution of fruits and vegetables. That company, which partners with several of the country's supermarkets, has established quality standards for many products and price ranges for the products based on that quality. In turn, that leadership has allowed other industry agents to assume the same strategy, a trend that has fostered the development of a specialized and segmented fruit and vegetable market.
- 1.5 However, as in the case with traditional agriculture, there is insufficient or inadequate access to financing for horticulture, as attested by the three modalities through which farm loans in Honduras have typically been provided: (i) lending terms similar to commercial terms offered to microentrepreneurs and wage employees, without adapting to the cash flows of horticultural producers; (ii) post-harvest financing that is not adapted to the cash flows of horticultural producers; (iii) financing of the farm or productive unit as a whole, which has proven to be more effective because it is better adapted to the cash flows of horticultural producers. However, the latter form of financing is the least used by financial institutions because it requires specific financial products that are tailored to farm capacity.
- 1.6 **Initiatives to promote credit for small and medium-sized farmers.** One of the most recent efforts to improve credit opportunities for micro and small farmers in Honduras was promoted by The Millennium Challenge Account (MCA-Honduras) program starting in 2007. MCA-Honduras implemented a technical assistance program for lending institutions (Access to Farm Credit, ACA) and a sister program for direct technical assistance for farmers (Farmer Training and Development, EDA), and created a trust to fund institutions interested in making loans to farmers. As of August 2010, the ACA Program reported that there were around 5,000 active loans to micro and small horticultural producers throughout Honduras from different lenders, including banks, microfinance institutions, cooperatives, exporters, and agribusinesses. The MCA-Honduras experience has been positive for the agricultural sector, and although it is in its final phase, it has demonstrated that financing for small farmers is possible, provided that good practices in commercial farm lending have been incorporated.
- 1.7 **The experience of Del Campo Soluciones Agrícolas.** Among the institutions making the most progress under the MCA-Honduras initiative is Del Campo Soluciones Agrícolas, a marketer of agricultural inputs that sells on a cash basis

and grants credit in kind to its customers, and also provides them with technical assistance and training as part of a comprehensive package of inputs. Del Campo, with support from the ACA Program, incorporated an innovative product in its 2009 commercial line that was tailored to the cash flows and emergency needs of small farmers: the “Agrofácil” credit card, which provides a credit line from US\$160 to US\$420 for a six-month term at a monthly interest rate of 2% and uses training certification rather than collateral. In other words, producers qualify for credit once they have obtained certification of basic training in horticulture management. The purpose of this credit product is two-fold: (a) to finance the input buying needs for any phase of production of micro and small farmers; and (b) to finance their emergency needs vis-à-vis the risk of disease, pests, and other phenomena.<sup>2</sup> At the end of the 18-month pilot, there were a total of 200 customers using the product in 20 communities in the Distrito Central municipio, with a delinquency rate of 0.26%. This demonstrates both the financial feasibility of extending credit to poor farmers and the potential for expansion to other regions.

- 1.8 **Limits on access to credit among small farmers and Del Campo Soluciones Agrícolas to continue and build on the experience.** Through its work with small horticultural producers, Del Campo has been able to identify other bottlenecks and limitations in terms of access to credit by this productive segment. Along these lines, in order to maintain a level of long-term sustainability and profitability, horticultural producers require basic equipment to control irrigation and fertilization. This equipment, while simple (motor pumps, filters, pipes, and fittings), would allow them to make the leap to more stable and profitable production in the long term. Without control over fertilization and access to controlled irrigation, producers work on a subsistence basis, failing to achieve the optimal levels of productivity and quality demanded by the market.
- 1.9 In order to continue serving the more disadvantaged sectors of the Honduran farming community, the company has endeavored to strengthen its structure, incorporate special credit policies and procedures, and train its staff in order to improve its products. However, it has come up against the following limitations on expanding its credit products:
  - 1.10 (a) Although Del Campo has access to financing from local commercial banks, this source of funding is limited with respect to suitable terms, amounts, and conditions. Commercial banks lend for terms of one year or more. However, payments are due monthly and interest rates do not allow for good development of new products, many of which require longer maturity periods.
  - 1.11 (b) Del Campo is also in the process of implementing products to complement its Agrofácil card. However, it does not have financing or technical assistance to

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<sup>2</sup> The card works as follows: Each customer with an approved credit line receives a card with their information, which they present at Del Campo stores to obtain inputs on credit that they then use to farm their plots. Customers can obtain inputs on credit repeatedly over the approved term, provided they make payments on prior transactions and do not exceed the approved limit.

develop those products. Sources of financing for development of new credit technologies are few or nonexistent. Although Del Campo already has experience with its Agrofácil product and the “traditional” 30-day loan, it requires proper systematization and support in shaping and adapting its experiences to new products geared toward horticulture.

- 1.12 (c) Lastly, small farmers have limited capacity in terms of managing sustainable and profitable farms. Although there are a large number of horticultural producers in the country, many of them plant and produce in an isolated manner with little or no technical support. They are not familiar with scaled production systems, seasonal rotation, or integrated pest and vector management, all of which are modern and necessary systems for efficient and environmentally-friendly production.
- 1.13 **Project beneficiaries.** The project will benefit farming families in four departments in Honduras, namely Francisco Morazán, Comayagua, Cortés, and El Paraíso. Specifically, it will benefit producers who are in close proximity to branch offices in the cities of Tegucigalpa, Danlí, Talanga, San Pedro Sula, and Comayagua. The producers are mostly families with between 0.35 and 3 hectares of land. Of that total available land, the large majority uses less than one hectare for horticultural production. Average annual incomes of producers range between US\$2,500 and US\$5,000. In most cases, agriculture is their largest source of income. Typically, a horticultural producer has a diversified farm, and “specialized” producers of a single crop are rare. The project beneficiaries are spread out over several regions of the country and are not organized into cooperatives, except those that are members of cooperatives of other products. Nearly all horticultural producers have production and sale contracts with brokers or companies that handle logistics and marketing of fresh products, which, in turn, are contracted by large supermarkets and food supply stores. Prices for horticultural products are determined by available supply at the regional level (with the inflow and outflow of products from neighboring countries), the quality of the product delivered, and the time of the year.

## II. THE PROJECT

### A. Objectives

- 2.1 The goal of the project is to increase the incomes of families of micro and small horticultural producers in Honduras. The purpose is to increase access to credit for approximately 1,500 micro and small producers by establishing an in-kind financing model for agricultural inputs and equipment. This financing will target the production, maintenance, and harvest of farm crops and will be tailored to the inflows and outflows of their productive units.
- 2.2 The specific objectives of the project are: (i) to improve the productivity of horticultural producers in Honduras through access to agricultural inputs and equipment, as well as specialized technical assistance; and (ii) to strengthen



Del Campo's lending processes in order to shore up and expand its financing program.

**B. Description**

In order to achieve the project objectives, two components will be financed: a reimbursable financing component for US\$1,100,000 (IDB: US\$700,000; Del Campo: US\$400,000) and a nonreimbursable technical cooperation component for US\$357,000 (IDB: US\$250,000; Del Campo: US\$107,000), both executed by the company Del Campo Soluciones Agrícolas, S.R.L.

- 2.3 The **reimbursable financing component** would provide funds to Del Campo in the amount of US\$700,000 to increase its loan portfolio for agricultural inputs through the company's different lines of business. The loan will be made in three disbursements. Del Campo will incorporate an additional US\$400,000 into its portfolio, which will come from local sources of financing, such as local banks and access to funds from the trust created by MCA-Honduras and managed by BAC Honduras. The loan proceeds will be used to expand and develop three credit products that respond to the specific financing needs of producers and their families. Those products are: (i) long-term loans for equipment and irrigation, with initial terms of up to 12 months and the possibility of an extension for up to 24 months, based on the experience obtained, and an initial rate of 15% on balances in local currency. These loans will have a maximum limit of US\$2,500; (ii) Agro Credi Movil loans, with terms of up to four months and a rate of 24% on balances in local currency, for an average amount of US\$1,000; and lastly (iii) the Agrofácil credit card, also with terms of up to four months, a rate of 24%, and a maximum limit of US\$300. These interest rates have been calculated to cover the various operating costs associated with the card, loss provisions, and the Bank's financing costs.
- 2.4 Long-term financing from the Bank will enable Del Campo to implement the mix of these three products in four regions of the country where the company has established branches. Implementation will be gradual, striving to reach a larger number of producers each year.
- 2.5 **Technical cooperation component.** The Bank will provide Del Campo with technical cooperation funding of up to US\$250,000. Those funds will be used to address four areas of need to complement the reimbursable financing component. The areas are: (i) improve the operating efficiency of Del Campo's lending processes, strengthening risk analysis capabilities and supporting its credit department in deploying a software module to monitor the portfolio and delinquency; (ii) develop a specialized technical assistance program for small horticultural producers that is tied to financing, with a view to improving their productivity; and (iii) develop environmental management manuals and processes that incorporate the appropriate use of agricultural inputs and personal care in the management and disposal of input containers. Lastly, the technical cooperation resources will also fund project evaluations and audits. The plan of operations for

the technical cooperation component, which provides a detailed account of all technical cooperation activities, can be found in the technical files. The resources provided by the Bank will be used to hire technical consultants to train small producers, and specialized financial consultants to improve credit monitoring systems. Those resources will also be used for project evaluations and audits. The counterpart resources will be used to cover transportation and logistics costs for training and consulting services, part of the costs of deployment of credit monitoring software, and various project management expenses.

### **C. Sustainability and results of the financial analysis**

- 2.6 The sustainability of the project comes, first and foremost, from the existence of extensive unmet demand from agricultural producers who still lack access to credit. It is estimated that the country still has approximately 15,000 small fruit and vegetable farmers without financing who, given their characteristics, do not have access to suitable products.<sup>3</sup> Those producers—in particular, those included in the EDA database—represent a significant unmet demand that enables Del Campo to expand its activities. Therefore, Del Campo's ability to offer its customers loan products with longer terms than traditional commercial loans gives it a competitive advantage compared to other agricultural input suppliers that do not have producer financing facilities.
- 2.7 Moreover, the project's financial projections indicate that the loan portfolio will grow steadily from US\$1.3 million in December 2010 to US\$2.3 million by end-2015, which means the loan volume will grow by a factor of 1.8. Although this projection includes the aggregate volume of operations related to Del Campo's credit products and not just the three products that will be supported by the Bank, it shows their contribution to the company's development. As for long-term liabilities, the projections indicated a reduction from US\$1.4 million in December 2010 to US\$0.8 million by end-2015, with Bank obligations steadily coming to account for a larger share of the total, primarily as a result of repayment of the BAC trust funds by Del Campo. Nonetheless, the reduction in liabilities will not stymie growth in the volume of operations, since most of the resources Del Campo will use to fund its loans in the future will come from equity by 2015.

### **D. Credit risk for the Bank**

- 2.8 The project presents risks for the Bank inasmuch as the loan amount is large compared to the company's liabilities and equity. However, it should be noted that Del Campo has loans and financing from local banks, principally HSBC Honduras, all of which are current. It has also had a good history and has maintained its eligibility with the trust managed by BAC Honduras. The company

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<sup>3</sup> ACA Program. Documentation of Experiences: Agrofácil credit card. 2010.

has not had to reschedule any liabilities. Its 2009 financial statements<sup>4</sup> show total assets of US\$3.3 million and total liabilities of US\$2.1 million, which is a good debt-to-equity ratio. The project's financial projections (in the technical files), while highly conservative, indicate that Del Campo will have modest earnings from project startup and on through the medium and long term. The Bank's loan to Del Campo will be disbursed in three annual tranches, enabling the Bank to analyze the company's growth prior to the release of each disbursement. In addition, the project team included a review of integrity and money laundering as part of its analysis of the operation in accordance with Bank guidelines (document CC-6093) and did not identify any risks to proper execution and management of the operation. Lastly, the two majority shareholders in the company will sign the loan contract with the Bank as personal guarantors of the operation.

#### **E. Expected outcomes and benefits**

- 2.9 By the end of this project, it is expected that both the producers and Del Campo will have obtained the following benefits: **1. Producers:** (i) there is an increase of up to 30% in the net incomes of small agricultural producers targeted by the project; (ii) 1,500 small farmers obtain financing through at least one of Del Campo's credit lines; (iii) there is a minimum increase of 30% in yields and productivity on the farms of small producers; and (iv) at least 90% of producers who receive technical assistance implement environmentally sustainable production systems. **2. Del Campo:** (i) the noncommercial loan portfolio increases from around US\$1.2 million to US\$1.9 million by the third year of the project; (ii) three types of farm credit products have been established within the company; (iii) loan delinquency remains relatively constant over the three years of the project at 3.5%, but no more than two percentage points above the banking system; (iv) the efficiency of credit operations has improved, with a 50% decrease in the metric equivalent to the total cost per loan over the total loan portfolio;<sup>5</sup> and (v) Del Campo's financing model is replicated by other commercial companies in the same industry.

#### **F. Bank and MIF strategy**

- 2.10 The project activities are consistent with the priorities of the Bank's country strategy with Honduras (document GN-2475 of 10 March 2008) because: (i) options will be created for access to credit in the productive sector by rural micro, small, and medium-sized enterprises (MSMEs), which is imperative to boosting competitiveness, one of the four areas targeted by the Bank; (ii) private sector participation is an engine of development and employment, permitting greater productivity through alternative sources of financing; (iii) given that the

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<sup>4</sup> Its 2008 financial statements were audited by the firm Grant Thornton. The 2009 financial statements are being finalized.

<sup>5</sup> This efficiency indicator will be defined with the initial consulting assignment for improvements in credit administration.

strides made in the financial system have not extended to the development of the market segment to which MSMEs would have access, the project will help address the gap in formal financial intermediation for the country's agricultural sector, while the institutional framework and other mechanisms needed to promote the efficient channeling of resources to this sector are defined.

- 2.11 **Integration with the MIF strategy (Access framework).** In addition to being consistent with the Bank's strategies as indicated, this project is consistent with one of the MIF's strategies, complementing its activities. In the access framework, under the microfinance heading, the agenda is to "expand and diversify the penetration of microfinance services to underserved and rural populations," the specific objective of which is to expand the scope of microfinance services to underserved rural and urban populations mainly through support (loans, technical cooperation funding, capital, etc.) for microfinance institutions. In this regard, although the proposed project would be implemented through a commercial company, instead of through a microfinance institution, the goal of the project is the same. Accordingly, the project falls within the MIF access framework and is in line with the objectives of the aforementioned agenda, inasmuch as it will serve micro and small low-income horticultural producers in rural areas who are linked to value chains.

**G. Cooperation with other international donor agencies**

- 2.12 This initiative is based on work that MCA-Honduras has been carrying out since 2007 in Honduras. In this regard, it is important to mention the trust fund that MCA-Honduras has made available to the commercial financial sector in Honduras, which is managed by BAC Honduras and is part of the local counterpart contribution for the project.

**H. Summary of the environmental and social review**

- 2.13 At a meeting held on 4 October 2010, ESR reviewed this operation and suggested that the technical assistance financed by the Bank should include training and advisory services on the use of integrated pest management and integrated vector management techniques. It also suggested the use of pesticides with less harmful effects on human health. Training in both of these areas has been incorporated into the project and is included in the budget and the description of the technical cooperation component that is provided in the technical files.

**I. Special conditions, disbursements, and procurement**

- 2.14 Before receiving the first disbursement of resources from the **reimbursable financing component**, Del Campo will present: (i) updated Credit Regulations that include the new credit products; (ii) its 2009 audited financial statements; and (iii) an institutional letter appointing the individuals responsible to the Bank for project monitoring.
- 2.15 For the first disbursement of resources from the **technical cooperation component**, Del Campo will present: (i) a work plan for the first 12 months of the

- project that includes a schedule of activities and a schedule for meeting the performance indicators, which will make it possible to monitor and supervise the status of the operation; (ii) the project coordinator selected; and (iii) the updated procurement plan.
- 2.16 **Disbursements.** In order to ensure that Del Campo has the capacity to absorb the total amount of the loan (US\$700,000) and maintain the quality of its portfolio, while improving its operating efficiency ratio during the projected expansion, the loan will be disbursed in three separate tranches as follows: (i) a first tranche of US\$250,000 upon fulfillment of the conditions precedent; (ii) a second tranche of US\$250,000, which will include an analysis of indicators to measure efficiency gains and fulfillment of the project indicators; and (iii) a final disbursement of US\$200,000. These tranches are expected to be released over a three-year period. In addition, release of the second and third tranches will be subject to Del Campo's adoption of a clear mechanism for analyzing and preventing the exchange rate risks to which it will be exposed with this loan.
- 2.17 Disbursements of the proceeds from the reimbursable financing component will be subject to Del Campo's fulfillment of the minimum institutional performance indicators agreed upon with the Bank, which Del Campo must fulfill both for disbursements and for the life of the loan. In exceptional cases, those indicators could be adjusted annually as part of the annual work plan. The indicators will include parameters related to the portfolio, return on assets, and debt.
- 2.18 Disbursements of funds from the technical cooperation component will be contingent on the achievement of milestones, which will be agreed upon by Del Campo and the Bank, along with their means of verification. Achievement of the milestones does not exempt Del Campo from the obligation to achieve the project objectives. Under the risk- and performance-based project management modality, the funds required to execute the project to achievement of the first milestone will be disbursed (up to 25% of the amount of the contribution) upon signature of the contract, appointment of the authorized representatives, and fulfillment of other agreed-upon conditions. In subsequent phases, funds will be disbursed upon presentation of evidence of achievement of the milestone, in accordance with the agreed-upon annual work plan. Disbursements will initially be reviewed ex post, on an annual basis. The type and frequency of reviews may be modified by the Bank based on the results of completed reviews and/or subsequent institutional analyses made during project execution.
- J. Reports, evaluations, and audits**
- 2.19 **Indicators and baseline.** Del Campo will be responsible for compiling and analyzing information relevant to monitoring the project performance indicators. At project startup, Del Campo will provide the Bank with an institutional baseline, including information on the number of customers, financial and portfolio indicators, etc. The baseline and logical framework indicators will be the benchmark for monitoring project performance. Del Campo and the Bank will use

- those indicators for periodic supervision of the project. They will also be used for the final evaluation of the project. The logical framework indicators may be modified by mutual agreement between the Bank and Del Campo.
- 2.20 During the first six months of execution of the technical cooperation component, Del Campo will hire consultants to establish a baseline for the socioeconomic and productive conditions of current and potential beneficiaries of the project.
- 2.21 **Reports.** Del Campo will deliver progress reports to the Bank's Country Office in Honduras on the last day of February and August of each year. Those reports will include an analysis of fulfillment of the performance indicators, any problems with execution, actions taken to remedy them, and projections for the next six months. At a minimum, they will also include: (a) **for the reimbursable financing component:** (i) number of producers and basic characteristics of the project participants; (ii) specific analysis of Del Campo's loan portfolio: loans placed, current loans, portfolio delinquency, etc.; (iii) the annual effective rate of loans placed compared to the average rate in the banking system for microenterprises; (iv) summary of Del Campo's cash contribution to the project; and (b) **for the technical cooperation component:** (i) summary of the work of consultants and of technical assistance provided; (ii) number of small farmers assisted; (iii) efficiency indicators for Del Campo's credit unit; and (iv) changes in procedural manuals and development of environmental policies at the company.
- 2.22 **Evaluations.** The project calls for two evaluations by individual consultants selected and hired by the Bank's Country Office in Honduras with resources from the technical cooperation component. A midterm evaluation will be commissioned 18 months after the first disbursement and a final evaluation will be commissioned at the end of the project. The first evaluation will measure, at a minimum, the following: (i) the progress made in raising producer incomes and improving the quality and productivity of production compared to the situation at project startup; (ii) the degree of fulfillment of the project performance indicators; (iii) lessons learned and recommendations to improve the project; and (iv) the institutional capacity of the executing agency.
- 2.23 In addition to the items indicated for the first evaluation, the final evaluation will measure and document the following: (i) the effects of the project on the groups targeted in the initial evaluation; (ii) the results of fulfillment of the project objectives; (iii) lessons learned; and (iv) project sustainability.
- 2.24 **Monitoring of the loan.** In order to facilitate monitoring of the reimbursable financing component, Del Campo will deliver the following to the Bank: (i) each year, its audited financial statements; (ii) every six months, its financial statements signed by its accountant and the legal representative; and (iii) every six months or to the extent that information is produced on relevant changes in the institution (e.g. in its Board of Directors or Management, or in its equity, financing, etc.).

- 2.25 **Audits.** Using its own financing, Del Campo will perform annual audits for the loan component as part of the audits of its financial statements, with special mention and analysis of the Bank's loan. Using proceeds from the Bank's loan, Del Campo will perform a final audit of the technical cooperation component at the end of its execution period.

**K. Project risks and mitigating factors**

- 2.26 **Nonrenewal or early termination of the MCA-Honduras financing fund.** One of the risks of the project is the possibility that the trust created by MCA-Honduras and managed by BAC Honduras will not be renewed or will be terminated. Del Campo has received 10 million lempiras from that trust, which according to information provided to the analysis mission team will increase by an additional 8 million, resulting in a portfolio of 18 million lempiras. Those amounts expire in August 2011 and August 2012, respectively. The project proposes to mitigate this factor through two actions: (i) maintain open channels of communication with the appropriate officers from BAC Honduras to identify potential contingencies in the trust funds that could affect Del Campo's lending operations; and (ii) schedule the disbursements of the loan such that they can generate liquidity and thus enable Del Campo to continue with its lending operations.
- 2.27 **Climate risks.** Honduras is a country where natural disasters in the past have affected agricultural production. This factor is always a risk for entities and companies that work with the farm sector. The mitigating factor is that Del Campo works in many parts of the country, and specifically, the project will be implemented in four different regions with a range of climates and conditions. This will permit diversification of crops as well as types of production so as to avoid a concentrated risk.
- 2.28 **Exchange risk.** Another possible risk for the project is the possible devaluation of the local currency (lempira) with respect to the U.S. dollar, which is the currency in which the Bank loan is denominated. In the event of inflation, the loans made by Del Campo in local currency would lose value and could present a risk for the company, which will make payments to the Bank in U.S. dollars. Although this currency risk is real, Del Campo is a commercial company that follows the policy of adjusting the prices of its products based on origin, most of which come from the United States. Moreover, the project loans will not have terms longer than 24 months, and in many cases will be for less than 18 months, which means that its exchange risk can be controlled with rate and fee adjustments as needed. In addition, the project's technical cooperation component will provide resources to help Del Campo develop mechanisms for analyzing exchange risk and systems for the effective management of these risks. Del Campo's adoption of these mechanisms will be a condition precedent for release of the second and third tranches of the loan.

**L. Exceptions to Bank policies**

2.29 None.