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MULTILATERAL INVESTMENT FUND

BRAZIL

**PROMOTION OF SOCIALLY RESPONSIBLE MARKET
OPPORTUNITIES**

(TC 01-11-04-2)

DONORS MEMORANDUM

This document was prepared by the project team consisting of: Fernando Campero (SDS/MSM), Project Team Leader; Daniel Shepherd (MIF); Gerardo Martinez (COF/CBR); Alberto Simões (LEG); and James Chapman (Consultant).

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ANNEX I Logical Framework

ABBREVIATIONS

AL	Alagoas
ATO	Alternative Trading Organizations
BNDES	Banco Nacional de Desenvolvimento Econômico e Social
CESI	Committee on Environment and Social Impact
FLO	Fair Trade Labeling Organizations International
FT	Fair Trade
FUNDAP	Fund for the Development of Family Sector Agriculture
GDP	Gross Domestic Product
IDB	Inter-American Development Bank
IFAT	International Federation for Alternative Trade
MIF	Multilateral Investment Fund
MSRP	Micro and small rural producers
NE	Northeast
NGO	Non-governmental organization
PE	Pernambuco
PEU	Project Execution Unit
PROMATA	Program to Support Sustainable Development in PE's Mata Region
RN	Rio Grande do Norte
SIPARN	Sociedade para Incentivo Ao Pequenho Artesao do Rio Grande do Norte
US	United States
WVB	World Vision Brazil

BRAZIL: PROMOTION OF SOCIALLY RESPONSIBLE MARKET OPPORTUNITIES

(TC 01-11-04-2)

EXECUTIVE SUMMARY

Beneficiary and Executing agency:	World Vision Brazil (WVB)
Beneficiaries:	Final beneficiaries will be at least 2,500 MSRP located in rural communities in the states of AL, PN and RN. The majority of MSRP will have monthly family incomes of US\$150-220 and will be organized into associations and cooperatives. The MSRP supported will have a fixed place of work and a tradition and experience in agricultural production. Approximately 80% will be microenterprises and 20% small enterprises.
Amount and source:	Modality: Grant – Small Enterprise Development Facility MIF: US\$ 975,000 Local: <u>US\$ 975,000</u> Total: US\$1,950,000
Terms:	Execution Period: 48 months Disbursement Period: 54 months
Objectives and Description:	<p>The general objective of the project is to increase the competitiveness of MSRP through improved productivity and access to domestic and international markets, particularly Fair Trade (FT) and organic markets. Its purpose is to improve MSRP marketing services via the institutional strengthening of a trading company, direct technical support to improve their production capacity, and the promotion and expansion of FT markets in Brazil.</p> <p>In order to achieve this objective, the project will include the following three components:</p> <p>(i) Component I: Improvement of MSRP marketing services. This component will allow MSRP to gain access to specialized marketing services, and to improve their ability to sell their products in domestic and international markets, particularly through FT market channels. To this end, the project will: (i) structure and build the capacity of a fair trading company specializing in serving MSRP needs; and (ii) conduct promotion and marketing activities to generate new market opportunities and transactions to facilitate the sale of MSRP's products. At least 2,500 MSRP are expected to benefit from these services during the life of the project. Both, the volume of MSRP's sales and their participation in the final sale price of their products should increase</p>

as a result of this component.

(ii) Component II: Strengthening of the productive capacity of MSRP. This component will provide training and technical assistance designed to transfer production and post-harvest skills and techniques to MSRP that will enable them to strengthen their production capacity and improve the quality and value of their products in order respond to market demand and meet quality standards in local and international markets.

(iii) Component III: Promotion of fair trade concepts and practices. This component seeks to promote the concept and practices of FT as a means to contribute to the expansion of formal domestic markets for products traded under this label in the higher income areas of Brazil, which would create an important market opportunity for the MSRP products in the Northeast as well as other parts of the country. In addition, the component will help establish a permanent FT certification entity in Brazil.

**Environmental/
social review:**

The Committee on Environment and Social Impact (CESI) reviewed and approved this project on February 1, 2002 and made the following recommendations for the project: (i) encourage the adoption of environmentally sustainable production techniques; (ii) include training and technical assistance to the MSRP in resource conservation, appropriate cultural practices and community resource use; (iii) design of an environmental monitoring system; (iv) consider the use of environmental certification programs in the project's activities; and (v) ensure that measures are in place to promote the participation of women and youth within the project.

The recommendations have been taken into account and are reflected in project design: the first and second recommendations about adoption of environmentally sustainable techniques and resource conservation training are addressed in paragraph 3.11. The third point regarding an environmental monitoring system is addressed in paragraph 8.1. The fourth issue about the use of environmental certification is covered in paragraph and 3.11. Participation of women and youth is addressed in paragraph 8.1.

**Special
contractual
conditions:**

The conditions prior to the first disbursement are presentation to the Bank's satisfaction of: (i) a detailed work plan and corresponding disbursement schedule for the first twelve months of activities, including quantitative and qualitative performance goals, signed by the Project Execution Unit's manager; and (ii) evidence of the agreement entered into by WVB and SIPARN for project implementation.

**Exceptions to
Bank policy:**

None

I. COUNTRY AND PROJECT ELIGIBILITY

- 1.1 Brazil was declared eligible for all forms of financing from the Multilateral Investment Fund (MIF) on September 16, 1994. This initiative is considered eligible through the Small Enterprise Development Facility (III-A), as it will seek to expand market opportunities for micro and smaller enterprises in the agricultural and artisan sectors in the northeast region of Brazil. Moreover, this project fits within the MIF environmental strategy in that it seeks to assist producers with improving access to environmentally friendly markets and encourages the sustainable use of natural resources, conditions that are an essential element of the marketing strategy proposed by the project to improve the competitiveness of rural producers in the Northeast (NE) of Brazil.

II. BACKGROUND

A. The Northeast region

- 2.1 The NE region concentrates around 30% of Brazil's population and contributes around 17% to its national income. About one third of its population lives in rural areas, with the agricultural sector generating an estimated 12.5% of the NE's internal product. The economic and social disparities of the NE and the rest of the country are high, with a per capita income equivalent to 46% of the national average. A similar situation is observed in its social indicators, which lag considerably behind the rest of the country. The region concentrates 55% of the Brazil's population living below the poverty line.
- 2.2 The NE is a vast semi-arid territory with low rainfall and precipitation that is distributed irregularly both temporally and geographically. Those regions with access to surface water, such as those located on the margins of the San Francisco River in Alagoas (AL) and Pernambuco (PE), or to ground water, as is the case in the western region of Rio Grande do Norte (RN), however, stand out as having favorable conditions for agriculture, particularly for annual and perennial fruit production.

B. The micro and small rural producers in the Northeast

- 2.3 The micro and small production units constitute the economic base of agriculture and the rural area in the NE. Recent estimates indicate that micro and small rural producers (MSRP) with medium, low and very low incomes represent around 85% of the region's productive units and absorb approximately 75% of the countryside's workforce. This segment represents nearly 30% of the gross agricultural production value. Its production is concentrated in traditional agricultural production, which has the characteristics of being homogeneous, low productivity, subject to significant price fluctuations, oriented mainly to the internal markets and generating low profit margins for producers.
- 2.4 Despite their relevance to the economy of the NE, MSRP face important difficulties that limit their business development capacity and their ability to increase their productivity and income levels. These include: (i) limited access to technical advice and production technologies that would allow them to improve their productivity and diversify their

production in response to market needs, and to increase their participation in the value chain through a better quality control, processing and packing of their products; and (ii) the absence of adequate marketing channels for their products that would enable them to link effectively with larger consumer markets.

- 2.5 Farm and rural productivity levels remain low when compared to more developed areas of the country, as technology transfer and extension services are limited, given the remote locations of many MSRP, and their limited ability to pay for such services. Farmers typically have to sell their produce at harvest times when prices are low, thus generating meager incomes, decreased potential for productive investment and continuation of the cycle of poverty. There are a limited number of intermediaries that collect produce at the farm gate, and pay prices that are too low to allow farmers to earn enough to be able to invest in agricultural infrastructure or productive inputs.
- 2.6 Brazil is rapidly becoming an important fruit exporter in international markets, with fruit exports increasing 36% in 1999 alone. Within Brazil, the NE boasts important fruit exports; particularly of melons from irrigated regions in PE and RN. Despite this growth potential and due to the low productivity and quality of their products—resulting, among others, from insufficient access to technical skills—, and the absence of sound marketing mechanisms, the MSRP currently represent only 1.7% of total exports and continue to show depressed income levels and a high incidence of poverty.
- 2.7 Participation in Fair Trade (FT) markets presents an opportunity for MSRP to increase their incomes. A commercial network whereby microenterprises in low-income areas of the world are able to increase the efficiency of their marketing and receive a higher proportion of the price paid by the final consumer is a concept that is increasingly winning the sympathy of international retail outlets.

C. Fair Trade

- 2.8 Fair Trade is an innovative concept that seeks to connect low-income producers and consumers in large markets in more equitable and sustainable ways. It originates in a growing interest among consumers in large markets in the development of socially responsible traders, that would allow for a “social value added” in their commercial transactions. This value added is generated when the purchase of a product, besides its intrinsic value, gives the final consumer the benefit of knowing that it contributes to improve the quality of life of a group of low-income producers. The FT movement is characterized for: (i) focusing on producers from low-income regions; (ii) seeking to improve the terms of exchange of producers in their relationship with large markets, through private marketing channels that operate efficiently and with social responsibility; (iii) promoting environmental sustainability and sound labor practices; and (iv) respecting market principles, seeking to create commercially sustainable operations and competing with conventional firms for the interest of consumers.
- 2.9 FT certification began in the Netherlands in 1988 as a response to plummeting prices in the world coffee market. A group of non-conventional Dutch traders formed the Max Havelaar Foundation, offering a FT label to any coffee company that was willing to trade a portion of their volume on FT terms. Third-party certification of FT products became a powerful mechanism for expanding FT beyond a relatively small core of socially conscious consumers and into the mainstream. Since the concept of FT was initially

developed, two key organizations have been formed. In 1989, following a conference of Alternative Trading Organizations (ATO) in The Netherlands, the International Federation for Alternative Trade (IFAT) was formed. IFAT is a worldwide network of Fair Trade organizations (at present it has over 160 members in more than 50 countries). In 1997, the various national FT labeling initiatives formed an umbrella organization called Fairtrade Labeling Organizations International (FLO). FLO is responsible for certifying and monitoring producers, accrediting a single organization to certify FT practices in each country and coordinating work among its members.

- 2.10 FLO is the only certification system in the world where producers do not pay for their certification. Different from other schemes, the consumer pays for the Fair Trade system. Traders pass on to consumers the higher FT price and premium that they pay producers. The financial resources flow all the way back from the consumer who buys the product, to the producer. The national entity in each country charges the Licensee a fee for using the Fair Trade label. This pays for all of FLO's certification and monitoring costs and for the National Initiatives marketing expenses. So the cost of the system is included in the retail price, making Fair Trade labelling sustainable.
- 2.11 Worldwide, FT sales are growing rapidly and total more than US\$400 million per year. Much of the experience to date related to FT has been in the coffee sector, which has been growing exponentially over the last several years. For example, in 1999, two million pounds of green coffee was FT certified in the US and in 2000, this amount doubled to over four million pounds. Moreover, according to a 1999 survey undertaken in Central America, non- FT coffee farmers received an average of about 38 cents per pound from the middlemen, whereas FT coffee cooperatives received a minimum of US\$1.26 per pound for their coffee, which is more than a three-fold increase. In the case of bananas, market shares of FT fruits have increased substantially in many European countries, reaching up to 15% in Switzerland.
- 2.12 While international FT markets have been growing rapidly, creating an important outlet opportunity for the products of MSRP in the NE, formal FT markets are nascent or non-existent in Brazil's large consumer centers, providing an important potential niche for MSRP's production, yet to be developed. Besides the lack of awareness, other factors such as the lack of a FT certification entity and a national network of organizations interested in promoting the concept have further dampened the growth potential of FT markets in Brazil.

D. The project

- 2.13 The present operation seeks to address the problems faced by MSRP in the semi-arid regions in NE Brazil, associated with low productivity and inadequate access to national and international markets, by: (i) assisting in: (a) the restructuring and strengthening of an existing trading company, to expand its operations in FT and organic markets; and (b) the provision of improved and efficient marketing services to MSRP; (ii) providing technical support and transfer appropriate technology to MSRP, through a network of local service providers,¹ to improve agricultural production² and strengthen producer associations,

¹ These include technical assistance providers that offer services in the areas of project intervention, which have expressed interest in participating in project-related activities: AACC, CACTUS, Terra Viva and others.

² The term agricultural production is used in a broad sense, encompassing not only fruit and vegetables, but livestock and arts and crafts derived from agricultural inputs (or other inputs originating mainly in rural areas).

aimed at taking advantage of the new market opportunities; and (iii) promoting and seeking to expand FT markets among Brazil's high-income consumers.

- 2.14 The project will contribute to generate market opportunities for MSRP by helping them to penetrate domestic and international markets, principally through FT distribution networks. This will be achieved through the structuring of a well-managed business-oriented trading company, with socially responsible objectives, which is expected to reach its break-even point within the project's life, thus, establishing a sustainable instrument for marketing the output of MSRP in the semi-arid regions in the NE. By trading in FT and other national and international markets with transparent accounting and management practices, the trading company will ensure that fair prices are paid and FT practices adhered to. The project will also support MSRP through the provision of technical assistance to improve products and production methods in order to improve quality and cost efficiency. This will help MSRP better understand the product requirements for various market niches, as well as help in the adjustment process needed for producing "for the market". All aspects of the project will feature environmentally sustainable production, processing and marketing processes, particularly entry into organic markets which by definition requires sustainable practices.
- 2.15 The project will focus activities in defined geographical areas of the states of AL, PN and RN. The target group will be MSRP organized into producer associations and cooperatives. The project will be strategically focused in areas that have the necessary elements and conditions for FT and organic market opportunities, where developmental synergy is assured and where there is potential for future replication by other communities. In order to leverage other resources, the project will coordinate with other initiatives, including Bank-funded operations such as the *Program to Support Sustainable Development in PE's Mata Region* (PROMATA) in the state of Pernambuco (BR0246).

E. MIF Strategy

- 2.16 In terms of MIF criteria, the proposed project is innovative in that it seeks to support commercial efforts of small-scale producers that will ultimately provide a higher margin for their products, allowing them to increase their overall return. Such an approach will demonstrate to other producers that market opportunities for FT exist and can serve as a lucrative market for their products. Project related activities are expected to be sustained over the long-run through continued actions and efforts of the strengthened fair trading company, which will continue to offer market opportunities to smaller enterprises interested in selling FT products.

III. PROJECT OBJECTIVES AND COMPONENTS

A. Objectives

- 3.1 The general objective of the project is to increase the competitiveness of MSRP through improved productivity and access to domestic and international markets, particularly Fair Trade and organic markets. Its purpose is to improve MSRP marketing services via the institutional strengthening of a trading company, direct technical support to improve their production capacity, and the promotion and expansion of FT markets in Brazil.

B. Components

- 3.2 The project consists of three components: (i) improvement of MSRP marketing services; (ii) strengthening of the productive capacity of MSRP; and (iii) promotion of FT concepts and practices.

Component 1: Improvement of MSRP marketing services (MIF US\$ 365,840; Local US\$ 458,020)

- 3.3 This component seeks to enhance MSRP access to specialized marketing services in order to improve their ability to sell their products in domestic and international markets, particularly through FT and organic market channels. To this end, the project will provide support for: (i) structuring and building the capacity of a fair trading company specializing in serving MSRP needs; and (ii) promotion and marketing activities to generate new market opportunities and transactions to facilitate the sale of MSRP's products.

1. Subcomponent A: Structuring and building the capacity of the trading company

- 3.4 The penetration by MSRP of specialized markets, such as those of FT or organic products, requires the presence of a modern trading company with a solid technical and institutional capacity that serves this clientele, which is currently lacking in the NE region. This subcomponent involves the institutional development and strengthening of an existing trading company, SIPARN, into one that efficiently and sustainably manages domestic and international marketing systems for the benefit of the MSRP in the geographic area of influence of the project. The process involves improving SIPARN's understanding of FT markets and its ability to successfully operate in them.
- 3.5 Based on the recommendations of an earlier consultancy, the trading company (currently registered as an NGO) will change its legal structure to that of a limited liability civil partnership, to facilitate the incorporation of new investors and strengthen its governance.³ The trading company will operate with its own organizational structure independently of that of the executing agency, WVB.
- 3.6 This subcomponent will finance the following activities: (i) legal services to adjust the legal structure and strengthen the governance of the trading company (through the modification of its legal form, the development of new statutes and board regulations, and training of its board members); (ii) specialized technical advisory services for development and implementation of marketing strategies and business plans; (iii) organizational and administrative structuring of the trading company (including the development of operational procedures for coordinating and trading with MSRP); (iv) provision of technical support through the contracting of specialized consultants for the efficient provision of specialized marketing services to MSRP; (v) training of trading company staff (in areas such as marketing principles, commercial practices and management, including FT and organic market operations, end-market trade regulations,

³ The legal figure to be adopted by the trading company is that of a non-profit limited liability civil partnership (Sociedade Civil Limitada), provided for by the Brazilian Civil Code.

etc.); and (vi) development and implementation of a marketing information system for the trading company, which will be continuously updated by its staff, to help expedite and track marketing operations.

2. Subcomponent B: Promoting and marketing products in FT markets

- 3.7 The activities included in this subcomponent are: (i) identification of new market opportunities in international and national markets, especially in formal FT markets in Europe and the US, through participation in fairs and other commercial events (such as the Produce Marketing Association in the US, as well as events held by FLO and IFAT related to FT markets); (ii) capacity building of MSRP to help them better understand marketing concepts and the requirements of meeting consumer demand and FT certification requirements; (iii) production of promotional materials and labels, and development of information mechanisms, to help the marketing products in FT and other markets; (iv) infusion with counterpart resources of US\$200,000 of working capital for trading company operations, through participation of WVB and other investors in the company's capital; (v) implementation of a monitoring and control system to ensure adherence by producers and the trading company to FT and organic production standards; and (vi) development of bar codes for product tracking. To promote dissemination of project benefits, training activities and the market studies carried out by the project will be made available to the public and other organizations in the region.
- 3.8 Execution of this component is expected to result in the sustainable and strengthened fair trading company—able to respond to the needs of MSRP and to operate in export and FT markets—is in place, and has: (i) modified its legal structure and adopted appropriate policies, governance, business practices and incentive structures to function both effectively and efficiently; (ii) adopted a viable marketing strategy, along with a concrete business plan, which is regularly updated; (iii) acquired appropriate patents and trade marks; (iv) reached financial self-sufficiency by the final year of the project; and (v) reached yearly sales of at least US\$3.1 million.

Component 2: Strengthening of the productive capacity of MSRP (MIF US\$ 229,000; Local US\$ 296,000)

- 3.9 This component will provide training and technical assistance designed to transfer production and post-harvest skills and other production techniques to MSRP that would enable them to strengthen their production capacity and improve the quality and value of their products, in order to respond to market demand and meet quality standards in local and international markets.
- 3.10 As an initial step, a consultant will be contracted to undertake a characterization of the existing productive capacity in the areas of project intervention as a means to: (i) identify strengths and weaknesses in organization and production; and (ii) develop concrete actions to correct production problems and improve efficiency and productivity. With this input, and market information originating in the trading company, the project will carry out participatory planning exercises with producer groups to set production goals and targets.
- 3.11 The project will fund specialized consultants and extensionists to transfer sustainable technologies to various MSRP groups within geographic regions of the project, aimed at

improving productivity, product quality and to adjust production to demand. Technical assistance will include: introduction of environmentally-sustainable production practices; adequate control of possible salinization and drainage problems in irrigated areas; organic farming systems (to help exploit this market niche), and recycling and treatment of post-harvest biomass. In addition, the project will contract a consultant to train MSRP groups in appropriate business practices and FT concepts to help them better manage their business. More specifically, the project will provide targeted technical assistance to those MSRP interested in implementing measures to obtain FT certification from a FLO accredited entity (see paragraph 2.10). This training will be supported by the development and dissemination of extension materials that facilitate technology transfer to MSRP and help ensure that the project impacts an even wider audience than just the direct project participants. Services will be available for all MSRP that are located within the geographic reach of the project and comply with the basic criteria set forth in the Project Operational Guidelines (see technical files). Beneficiaries will pay a portion of the costs of the technical assistance and training they are provided by the project. The costs recovered from technology transfer activities will be re-invested in training and technical assistance.

Component 3: Promotion of Fair Trade concepts and practices (MIF US\$ 164,760; Local US\$ 92,060)

- 3.12 This component seeks to promote the concept and practices of FT, in order to contribute to the expansion of formal domestic markets for products traded under this label in the higher income areas of Brazil, which would create an important outlet opportunity for the production of MSRP in the NE and as well as other parts of the country. In addition, the component will help establish a permanent FT certification system in Brazil.
- 3.13 As a first activity under this component, the project will finance an initial conference to launch the project and publicize the concepts of FT in Brazil, as well as to stimulate interest in this label among consumers and producers. This two-day event will be held in the northeast of Brazil and will include representatives from producer groups and national and international purchasers of FT products. The event will be part of a larger overall publicity campaign financed by the project in order to raise public awareness of FT practices and products. In addition, the project will finance the organization of a national FT exposition that will help promote the concept among consumers, marketers, producers, and socially responsible organizations.
- 3.14 As a means to improve the FT connections all across the country, the project will assist in the establishment of a Brazilian FT network, to include representatives of state and federal governments, NGOs, and private sector firms, especially sellers of FT goods. This network will help ensure that stakeholders concerns are being addressed in promoting FT markets in Brazil.
- 3.15 The project will also include assistance in the development of a FT certification organization accredited by FLO (see paragraph 2.11), which will also ensure that products with a “Fair Trade” label are consistent with internationally accepted standards. This assistance will help the entity with undertaking the necessary steps to be an internationally recognized and accredited FT certification body.

IV. PROJECT EXECUTION

A. Executing Agency

- 4.1 The executing agency for this project will be World Vision Brazil (WVB), a nonprofit organization established in 1975 to contribute to Brazil's sustainable human development. WVB has over 26 years of experience in community development work in northeast Brazil, particularly in the agriculture, microenterprise, education and health services sectors. WVB interventions include projects in microcredit, business development services and commercialization. Headquartered in Belo Horizonte, its operations in the NE are decentralized to an office in Recife, PE. WVB has 65 staff employees and its financial statements for 2001 show annual revenues of US\$6.6 million, expenditures of US\$6.5 million and assets of US\$1.4 million. WVB will lead the process of structuring and strengthening the trading company, as well as in the contracting of the technical services to MSRP, and the promotion of FT in Brazil. WVB has been able to establish an international network of commercial contacts in FT markets, both for fruit products, as well as for other agricultural and handicraft goods. It has launched an experimental FT export program in 1999-2001, an experience that will serve as a basis for the marketing activities of the project. (See project technical files for institutional analysis).

B. The trading company – SIPARN

- 4.2 SIPARN is an existing non-profit trading company established in 1991 with the purpose of promoting the development of rural microenterprises through the marketing of products originating from rural communities in the NE. Its current controlling members are two large NGO's operating in the NE and a group of local producer organizations. SIPARN's started exporting cashew in 1993 and has expanded operations in recent years to include other products. Recently (1999-2002) it entered into a partnership with WVB to export melons to European FT markets on an experimental basis, which in 2001 included the export of 75,000 boxes. At the end of 2001, SIPARN had assets of US\$128 thousand and a net worth of US\$70 thousand. SIPARN currently has a three-member Board and an administrative staff of two (see technical files for more details on SIPARN).

C. Execution mechanism

- 4.3 For the execution of the project, WVB will establish a **Project Execution Unit (PEU)**, which will be responsible for coordinating project actions, and managing and controlling project activities and budget. The PEU will execute the project according to the Project Operational Guidelines (POG) (see project technical files) and coordinate the activities necessary for the fulfillment of the project's objectives and performance indicators, as laid out in the logical framework (Annex I). The PEU will be made up of a project coordinator, a financial assistant and an administrative assistant, who will be selected and contracted through a competitive process. The PEU will report directly to WVB's Economic Development Manager. In addition, WVB will set up an internal project management committee, composed of WVB's Executive Director, its Economic Development Department Manager and two other senior members. The committee's

responsibilities will include: (i) supervising project implementation by the PEU; (ii) approving the POG; (iii) submitting the trading company's proposed new by-laws to WVB Board; and (iv) approving the project's annual implementation plans and budget.

- 4.4 The first component entails the trading company's institutional strengthening and the transformation of its legal structure and by-laws. For its execution, WVB will enter into an agreement with SIPARN, establishing the latter's responsibilities in the implementation of the project. The agreement will establish: (i) the process and timetable for the legal transformation of SIPARN into a limited liability civil partnership (*sociedade civil limitada*); (ii) the institutional obligations and rights of WVB and SIPARN in relation to the activities to be carried out by the trading company for this project; (iii) the terms and conditions for strengthening of the trading company, consistent with the activities defined in Component 1; (iv) the social objective, governance, ownership structure and characteristics of the transformed trading company; including the condition for providing trading services to all MSRP that meet the project's eligibility criteria, regardless of whether they are members of an organization holding shares in the trading company; (v) the mechanisms to coordinate the implementation of Component 1 of the project; (vi) appropriate safeguards to ensure that SIPARN does not undertake any measures or activities that would be detrimental to this project; and (vii) a provision for WVB to take a controlling position of SIPARN at the project outset, through a modification in SIPARN's by-laws allowing WVB to elect a majority of SIPARN's Board members during the transitional period, in order to ensure the proper level of coordination for project execution. WVB will be responsible for contracting the consulting and training services, required for the institutional strengthening of the trading company.
- 4.5 **The transformed trading company** will have the following characteristics: (i) its social objective will be the promotion of FT for the products of micro and small entrepreneurs of the NE; (ii) it will be established as a limited liability civil partnership; (iii) its net-income will be fully reinvested in the company or in the provision of services to MSRP (see paragraph 4.6); as an organization that does not distribute profits it will seek qualification as a public interest civil society organization (OSCIP⁴), which will enable it to apply for certain tax exemptions that will reduce its cost of doing business; (iv) voting rights in its governing body and administrative control will be legally established as a function of paid-in contributions to its capital; (v) during the life of the project, to facilitate project coordination, WVB will maintain a controlling stake of the company, holding 51% of its shares; and (vi) besides WVB, its main shareholders will be AACC⁵, a local NGO currently associated to SIPARN, as well as producer associations, the latter being restricted as a group to hold no more than 20% of the company's total shares. Social-minded private sector investors will be encouraged to join in the future, although the trading company's capitalization during the project does not depend on their

⁴ OSCIP, "Organização da Sociedade Civil de Interesse Público", established by Law 9.790/99, is a form of recognition granted by the Brazilian state to certain organizations that qualify as of public interest, which entails access to certain benefits granted to these organizations.

⁵ AACC, "Associação de Apoio às Comunidades do Campo do Rio Grande do Norte" was established in 1985 with the mission of promoting local sustainable development through strengthening grassroots and citizen participation. Its objective is to stimulate local-level actions through the provision of training, technical assistance and other means to improve the quality of life of individuals of rural areas.

participation. The trading company will establish incentives in its staff remuneration policy, linking them with trading operation's results, and will hire a general manager with extensive experience in the field (see Annex IV in the technical files). To ensure that the trading company maintains its operations focused on the intended segment of micro and small entrepreneurs, at least 80% of its clients will be MSRP that meet the criteria indicated in paragraph 6.3.

- 4.6 The net income of its operations will be distributed according to the following criteria: (i) 30% as reserves against losses; (ii) 50% will be reinvested in the company to be used as working capital; and (iii) 20% will be assigned to a fund to finance training and technical assistance needs of MSRP, complementing contributions made by MSRP.
- 4.7 The execution of the second component will be carried out directly by WVB, who will hire qualified specialized consultants and training services for the provision of technical services to the groups of producers in the project areas. To ensure that the technical services provided to producers are consistent with the requirements of consumer markets and criteria set forth by the trading company, WVB will conduct quarterly meetings with the participation of producer groups, trading company representatives and the participating consulting firms. The third component will be executed directly by WVB, who will carry out the activities and organize the events provided for directly or with the support of specialized consultants.
- 4.8 **Execution and disbursement periods.** Execution and disbursement periods of 48 and 54 months, respectively, are anticipated. A revolving fund will be set up for 10% of the MIF contribution, which will be disbursed and managed in a separate account. WVB will submit semi-annual financial reports on the status of the revolving fund to the Bank Country Office in Brasilia.
- 4.9 **Accounting and auditing.** WVB will maintain suitable internal accounting records and financial oversight of the project funds to allow for verification of transactions and to facilitate timely drafting of financial statements and reports. Project files will be arranged so that: (i) the sums received from the various sources can be identified; (ii) project expenses are reported in accordance with the chart of accounts approved by the Bank, with distinction made between MIF contributions and funds from other sources; and (iii) the necessary details are included to identify goods acquired and services contracted, as well as their use. The executing agency will open separate, specific bank accounts for managing MIF contribution and local counterpart funds. The executing agency will submit the final financial statement to the Bank, audited by an independent firm acceptable to the Bank.
- 4.10 **Status of project preparation.** The design, budget and activities planned under the project have been prepared by WVB with input from stakeholders and the Bank project team. The project team negotiated the project content, the POG and the draft WVB-SIPARN agreement with the executing agency. Counterpart funding has been negotiated and confirmed, and the detailed budget and project cash flow is available. The executing agency has pre-identified the communities where project beneficiaries will be selected from, who have already been working with WVB and SIPARN. This aspect should allow for a prompt commencement of project activities. Similarly, potential sources of funds to finance the trading company's working capital as well as the MSRP working

capital needs have been tentatively identified. A study to determine legal structure of the new trading company was completed during project preparation. SIPARN has all export licenses and experience with exporting melons to FT markets in Europe, giving valuable insights into this market and helping to develop initial commercial contacts that also add to the readiness of the project.

V. COST, FINANCING AND SUSTAINABILITY

- 5.1 **Cost and financing.** The cost of the project is estimated at US\$1,950,000. The MIF will contribute US\$975,000 on a non-reimbursable basis, and WVB will provide US\$975,000 as local counterpart contribution. At least 50% of the local counterpart will be in cash and the rest in-kind. (See project technical files for an itemized project budget).

ACTIVITIES	MIF	LOCAL	TOTAL	%
Improvement of small producer marketing services	365,840	458,020	823,860	42%
Strengthening productive capacity of MSRP	229,000	296,000	525,000	27%
Promotion of fair trade concepts and practices	164,760	92,060	256,820	13%
Project management	140,400	108,920	249,320	13%
Evaluations and baseline indicators	50,000	--	50,000	2%
Financial Audit	5,000	--	5,000	0%
Contingencies	20,000	20,000	40,000	2%
TOTAL	975,000	975,000	1,950,000	100%

- 5.2 The consulting fees of US\$4,300 (R\$12,000) for the study contracted by WVB in June 2002, during project preparation, to evaluate different legal structuring options for the trading company will be recognized as part of the counterpart contribution.
- 5.3 **Sustainability.** According to cash-flow projections, the trading company should reach operational sustainability during the fourth year of the project. Sustainability will be achieved through the efficient administration of the net income generated from the marketing intermediation margin, which is expected to be around 6% on average of the total value of the sales. This margin is significantly lower than that charged to MSRP by comparable traders. Sustainability should be achieved through continued operations of the trading company beyond the life of the project.
- 5.4 Sustainability of technical assistance services, in this case the technology transfer and extension work to be provided by the project, will occur by having the producers make a contribution to offset these costs by establishing a check-off system whereby a small percentage of the value of marketed produce is set aside for partial cost recovery. The project's contribution to these services will phase out gradually, reaching 50% of the cost of the extensionists by the end of the project. At the same time, WVB will seek to leverage public investment in government funded research and extension infrastructure by: (i) collaborating with public sector projects such as PROMATA; and (ii) by offering to pay variable costs such as fuel and per diems in order to assist public extension agents to reach project constituents after the project ends.

VI. JUSTIFICATION, BENEFICIARIES AND RISKS

- 6.1 **Justification.** This project will help improve the market opportunities for MSRP in the rural areas of NE Brazil, demonstrating the viability and profitability of selling products to FT markets. Moreover, by strengthening a trading company with specialized knowledge of FT markets, the project will ensure constant access for MSRP to markets in Brazil and abroad that include increased margins on their products. New markets will also include those for organic production. In addition, the project will strengthen the network of cooperatives, technical assistance service providers and other organizations that promote FT practices in geographic areas included in the project. By promoting new products and production techniques the project will help MSRP increase their production capabilities and diversify their products thereby allowing them to increase their income and better withstand adverse conditions that may impact their production. The project is expected to allow these MSRP to generate accumulated sales of at least US\$7.3 million during the project's life, of which more than 85% will originate from operations in FT and organic markets.
- 6.2 The project is also expected to expand the opportunities for alternative markets, such as FT for other enterprises beyond those participating in the project itself. By increasing awareness among consumers in the domestic market, demand for products that are prepared following sound environmental norms and practices is also expected to increase, creating further opportunities. Moreover, through support for the development of a Brazilian FT certification organization, other producers throughout the country will benefit from improved access to product certification. When the FT label is used on marketed goods, consumers will have confidence that the goods are in fact traded fairly and proceeds are used to help the poorer segments of the population.
- 6.3 **Beneficiaries.** Final beneficiaries will be at least 2,500 MSRP located in rural communities in the states of AL, PN and RN. The majority of MSRP will have monthly family incomes of US\$150-220 and will be organized into associations and cooperatives. The MSRP supported will have a fixed place of work and a tradition and experience in agricultural production. Approximately 80% will be microenterprises and 20% small enterprises.
- 6.4 **Risks.** The following risks have been identified: (i) Risk: During the early years of the project, MSRP will continue to grow highly perishable crops. While lucrative in the long-term, perishable produce are subject to price fluctuations, leading to producer price-risk and the potential for losses of profit and investment. There are also production and post-harvest loss risks due to inappropriate harvesting techniques, transport and other types of losses. Remedial actions include: (a) expanding production of non-perishable or processed products, such as dried fruit and vegetables; (b) providing technical assistance on post-harvest handling practices and facilities that minimize losses; (c) seeking to produce "off season," targeting market windows when product prices tend to be at their peaks; and (d) helping develop new domestic FT markets for perishable products that purchase at guaranteed or premium prices. (ii) Risk: Another risk facing the project is the possible delays in the trading company's legal transformation process arising from bureaucracy and longer-than-expected

paperwork. The project will mitigate this risk by providing expert legal assistance to help the trading company undertake this process. (iii) *Risk*: Disgruntled intermediaries currently operating with MSRP in the project region might try to boycott the trading company. WVB has devised a strategy that includes an active promotion of the FT concept and raising MSRP awareness as of the benefits of FT to mitigate this risk. Close monitoring of producer associations and participatory discussions will be used to counteract possible boycotts.

VII. MONITORING AND EVALUATION

- 7.1 **Monitoring.** The Executing Agency will prepare and submit to the Bank's Country Office (CO) project progress reports within thirty (30) days after the completion of each semester and a final report within 30 days from the final disbursement. These reports will follow a format previously agreed with the CO and will address project activities and finances, as well as results measured in terms of the indicators and benchmarks identified in the project's logical framework. The CO will utilize these reports to monitor project implementation progress and to prepare a Project Completion Report within three months of the last disbursement.
- 7.2 WVB will be responsible for gathering and analyzing relevant information for the continuous monitoring of the project's performance indicators. At the project's outset, WVB will contract a consultant to establish baseline parameters and design a system of indicators to monitor project activities and performance, which will complement those established in the logical framework. The baseline survey will establish initial measurements for all the indicators listed in the project logical framework as well as others that may be deemed necessary. WVB will submit the baseline parameters and the proposed monitoring indicators to the Bank's country office for approval, within three months of the project's initiation. Once agreed upon, these parameters and indicators, along those contained in the logical framework, will constitute the basis for project monitoring. WVB and the Bank will use the monitoring system and indicators for the supervision and evaluation of the project. These indicators will be considered in the project's progress reports, as well as in the intermediate and final evaluations. In the event that project performance exhibits significant unfavorable deviations (of over 20%) in the fulfillment of the key agreed upon indicators, the Bank may suspend disbursements of project funds. If it is found that project indicators have deteriorated, WVB will have 30 calendar days to agree with the Bank on measures to correct its performance. Once that period has expired, or if the situation has not improved to the Bank's satisfaction, the Bank may suspend or cancel future disbursements.
- 7.3 **Evaluations.** An intermediate and a final evaluation of the project will be undertaken by external consultants to be contracted directly by the Bank, through its country office. The mid-term evaluation will be prepared 24 months after program implementation or when 50% of the resources have been disbursed. A final evaluation will be conducted at the end of project execution or when 95% of the Bank's contribution has been disbursed. The evaluations will be paid for with the funds from the project budget. The executing agency will provide access to all the information and documentation needed to conduct these evaluations.

VIII. ENVIRONMENTAL AND SOCIAL VIABILITY

- 8.1 By design, this project will be low impact on the environment, using and promoting sustainable agricultural practices. In fact, given that the project's objective is to expand the opportunities for FT and organic products, which include norms and standards to improve social conditions of the producer groups and ensure that the products are developed utilizing environmentally-friendly methods, the project should actually result in a positive impact on both the environmental and social conditions in the geographic area of the project. WVB will also develop and implement a monitoring system that periodically takes measurements of environmental indicators that are relevant to the products included within this project. The project will promote equitable participation of women in all productive processes and specific working methodologies will respect the timetable of women in the NE region. The minimization of child labor in the production process will be promoted, consistent with emerging international norms.

IX. SPECIAL CONTRACTUAL CONDITIONS

- 9.1 The conditions prior to the first disbursement are presentation to the Bank's satisfaction of: (i) a detailed work plan and corresponding disbursement schedule for the first twelve months of activities, including quantitative and qualitative performance goals, signed by the PEU's manager; and (ii) evidence of the agreement entered into by WVB and SIPARN for project implementation.

X. EXCEPTIONS TO POLICIES AND PROCEDURES

- 10.1 No exceptions to Bank policies and procedures have been considered.

LOGICAL FRAMEWORK

DESCRIPTIVE SUMMARY	INDICATORS	VERIFICATION METHODS	ASSUMPTIONS
A. OBJECTIVE			
To improve competitiveness of the micro and small rural producers by improving productivity and access to domestic and international markets, especially fair trade (FT) markets.	<ol style="list-style-type: none"> At least 2,500 micro and small rural producers have benefited, with new sales totaling US\$7.3 million, US\$6.4 million of which are in the fair trade and organic markets. For 80% of the beneficiary micro and small rural producers, the average family/individual income from sale of agricultural products is up 40% over sales before joining the project. Stable channels were established to market the products in the beneficiary regions in fair trade markets. 	<ul style="list-style-type: none"> Financial reports on the trading company and the partner companies (of micro and small rural producers). Statistics from the federal, state and municipal governments. Surveys of micro and small rural producers, local merchants and control groups. Reports and statistics generated by the project through the World Vision Brazil monitoring system. Baseline and midterm and final project evaluations. 	<ul style="list-style-type: none"> Macroeconomic, foreign trade and local government policies affecting the micro and small rural producers and the trading companies do not change radically during the life of the project. Attitudes and participation levels remain positive for producers, companies, NGOs and local governments. Prices and demand in domestic and international fair trade markets do not change significantly. No unexpected commercial barriers are created in the major export markets.
B. PURPOSE			
To improve the micro and small rural producers marketing services through institutional strengthening of a trading company, technical support to improve micro and small rural producers' production capacity, and expansion of fair trade markets in Brazil.	<ol style="list-style-type: none"> There is a trading company with the capacity to work in fair trade markets, which is in a position to operate effectively and to provide marketing services to the micro and small rural producers. <ol style="list-style-type: none"> The trading company changed its legal structure, approved new bylaws and was recognized as a civil society of public interest (OSCIPI) within its first year. The trading company bylaws include clauses preventing differential treatment of clients depending on their belonging to trading company partner collectives. The trading company recognized capital contributions from the partners of US\$200,000 above the capital held by SIPARN (Society for Incentives to Small Craft Workers) at the beginning of the project, (capital contribution increase of US\$100,000 in year 1, US\$70,000 in year 2 and 30,000 in year 3). 	<ul style="list-style-type: none"> Audited financial statements from the trading companies. Records, reports and statistics generated by the project. Interviews with customers and other participants in the commercial system. Reports and records on training provided. Survey of prices paid to producers within and outside of the FT market. Records of the transactions of the Collectives (of micro and small rural producers) and the trading company. 	<ul style="list-style-type: none"> Resources from the government, private sector and World Vision Brazil are available as supplementary project resources (e.g., to financial working capital for producers and trading company). Local and state governments continue to support project activities. The micro and small rural producers maintain a positive attitude toward and interest in the project, and are able to acquire and apply new production and marketing techniques. Increased demand in market for high quality organic products and crafts and products sold on specialized fair trade markets.

DESCRIPTIVE SUMMARY	INDICATORS	VERIFICATION METHODS	ASSUMPTIONS																														
	<div>1.3 The trading company achieves financial sustainability (admin., financial and operational expenditures / financial and operational revenue = >1) at the end of project year four (50% in year 1; 60% in year 2; 80% in year 3; 100% in year 4).</div> <div>1.4 Number of micro and small rural producers participating in marketing network is up to 2,500 in year 4 (2005), (total of 800 in year 1; 1,200 in year 2; 1,800 in year 3; and 2,500 in year 4).</div> <div>2. Number of micro and small rural producers with extension services / trained in appropriate production techniques, post-harvest management and fair trade marketing has reached 1.440 by year 4. (total: 240 in year 1; 440 in year 2; 800 in year 3; and 1.440 in year 4). Proportion of low-income micro and small rural producers (with monthly incomes below US\$220 at the start of the project) is greater than or equal to 80%.</div> <div>3. Value of trading company products on FT market in Brazil increased at least 25% by the end of the project.</div>		<div>• There are no serious boycotts by displaced intermediaries against the trading company, or if there are any, they are counteracted sufficiently.</div>																														
C. COMPONENTS																																	
<div>I. To improve marketing services</div>	<div>1. Sustained increase in trading company annual sales: US\$0.8 million in year 1; US\$1.3 million in year 2; US\$2.1 million in year 3; and US\$ 3.1 million in year 4 (2005).</div> <table><tr><td></td><td>YEAR 1</td><td>YEAR 2</td><td>YEAR 3</td><td>YEAR 4</td></tr><tr><td>FAIR TRADE</td><td>56</td><td>200</td><td>422</td><td>604</td></tr><tr><td>FT CRAFTS</td><td>157</td><td>231</td><td>305</td><td>455</td></tr><tr><td>FT ORGANIC</td><td>379</td><td>675</td><td>1,154</td><td>1,801</td></tr><tr><td>TRADITIONAL</td><td>228</td><td>195</td><td>220</td><td>241</td></tr><tr><td>TOTAL</td><td>819</td><td>1,301</td><td>2,100</td><td>3,100</td></tr></table> <div>2. Average prices paid by the trading company for FT marketing to micro and small rural producers exceed average conventional market prices.</div> <div>3. Number of new international markets penetrated by micro and small rural producer products: 8; new FT customers: 12.</div>		YEAR 1	YEAR 2	YEAR 3	YEAR 4	FAIR TRADE	56	200	422	604	FT CRAFTS	157	231	305	455	FT ORGANIC	379	675	1,154	1,801	TRADITIONAL	228	195	220	241	TOTAL	819	1,301	2,100	3,100	<div>• Audited financial statements from the trading company.</div> <div>• Records and financial statements from the collectives.</div>	<div>• The legal records of the transformed trading company are obtained on a timely basis.</div> <div>• Indicadores macroeconómicos se mantienen estables.</div>
	YEAR 1	YEAR 2	YEAR 3	YEAR 4																													
FAIR TRADE	56	200	422	604																													
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DESCRIPTIVE SUMMARY	INDICATORS	VERIFICATION METHODS	ASSUMPTIONS
	4. Proportion of the trading company customers qualifying as low income micro and small rural producers (with monthly income below US\$220 at the start of the project) is greater than or equal to 80%. 5. There is a FT monitoring and control system.		
II. To strengthen the productive and entrepreneurial capacity of the producers.	1. Number of micro and small rural producers adopting new production techniques promoted by the project: 120 in year 1; 220 in year 2; 400 in year 3; and 720 in year 4. 2. Increase in proportion of nonperishable products compared to perishable products: 30% in year 1; 43% in year 2; 45% in year 3; 50% in year 4. 3. Increase in the percentage of production of the micro and small rural producers acceptable to markets in terms of quality and quantity: 65% in year 1; 70% in year 2; 75% in year; 80% in year 4. 4. Average organic certification of 120 ha./year in the six municipios. 5. Number of micro and small rural producers meeting the fair trade certification requirements reaches at least 1.440 in year 4.	<ul style="list-style-type: none"> • Production and quality control reports from the trading company and Collectives. • Survey and interviews with the microentrepreneurs. • Baseline and internal and external evaluations. • Records, reports and statistics generated by the project and by official agencies. 	<ul style="list-style-type: none"> • Micro and small rural producers maintain a positive attitude and are able to acquire and apply new production and marketing techniques.
III. To promote the concept of fair trade.	1. Increase in the number of microentrepreneurs aware of the fair trade concepts: 120 in year 1; 220 in year 2; 400 in year 3; 720 in year 4. 2. Increase in the number of government and private sector officials understanding and disseminating the concept of FT: 50 in year 1; 100 in year 2; 150 in year 3; 250 in year 4. 3. Existence of new institutional cooperation networks and nexuses among national and international groups supporting fair trade. At the end of the program, a Brazilian network of entities promoting FT was created, with the participation of more than 10 organizations from various regions. 4. A mechanism was created for fair trade certification in Brazil that covers sales on the domestic market.	<ul style="list-style-type: none"> • Records of participation in courses, seminars and workshops on fair trade. • Production and distribution of documents, leaflets and other mass media. • Records of organizations participating in the fair trade network. 	<ul style="list-style-type: none"> • There is a clear, generally accepted definition of the concepts of fair trade • There is a capacity to train and strengthen a fair trade network.

D. ACTIVITIES		
Component 1: Improve marketing services		
(a) Trading Company Structure and Management		
1.1 Legal structure of the trading company and strengthening of its governance structure	MIF	US\$
1.2 Creation and introduction of business plan and commercial strategy	Component 1	365,840
1.3 Organizational and administrative structure of the trading company	Component 2	229,000
	Component 3	164,760
1.4 Strengthening of provision of marketing services.	Project management	140,400
1.5 Training of trading company personnel	Evaluations	40,000
1.6 Development and implementation of management and marketing information system	Baseline	10,000
b) Promotion and marketing		
1.7 Identification of markets and business opportunities	Audit	5,000
1.8 Promotional activities and seminars with micro and small rural prod	Contingencies	20,000
1.9 Production of publicity and brand materials	Subtotal	975,000
1.10 Provision of working capital for marketing		
1.11 Provision of working capital for marketing (and capital contribution)	World Vision Brazil	US\$
1.12 Implementation of a fair trade monitoring and control system	Component 1	458,020
1.13 Development of bar codes	Component 2	296,000
Component 2: Strengthen producers' productive capacity		
2.1 Identification of productive capacity	Component 3	92,060
2.2 Participatory planning of production processes	Project management	108,920
2.3 Dissemination of sustainable production technology	Evaluations	-
2.4 Business management group training	Baseline	-
2.5 Development of technical assistance support materials	Audit	-
2.6 Acquisition of extension support equipment	Contingencies	20,000
Component 3: Promotion and dissemination of the fair trade concept		
3.1 National launch / workshop	Subtotal	975,000
3.2 Fair trade publicity campaign (among consumers)		
3.3 Creation of a regional fair trade network	Total	1,950,000
3.4 Involvement of other organizations related to FT		
3.5 Development of a national fair trade certification		
3.6 Organization of a national fair trade show		

- Biannual and annual reports from World Vision Brazil to the Bank
- Midterm and final evaluation
- Outside advisory support and preparation of pertinent report
- Inspection visits