

# Report and Recommendation of the President

RRP: BAN 33224

## Report and Recommendation of the President to the Board of Directors on a Proposed Loan and Technical Assistance Grant to the People's Republic of Bangladesh for the Agribusiness Development Project

October 2005

Asian Development Bank

## CURRENCY EQUIVALENTS

(as of 22 September 2005)

Currency Unit	–	taka (Tk)
TK1.00	=	\$0.0153
\$1.00	=	TK65.51

## ABBREVIATIONS

ADB	–	Asian Development Bank
ASA	–	Association for Social Advancement
ATDP	–	agro-based technology development project
BASIC	–	Bangladesh Small Industries and Commerce
CAR	–	capital adequacy ratio
DAM	–	Department of Agricultural Marketing
DFI	–	development finance institution
GAP	–	gender action plan
GDP	–	gross domestic product
MFI	–	microfinance institution
MOA	–	Ministry of Agriculture
MOF	–	Ministry of Finance
MOFL	–	Ministry of Fisheries and Livestock
NCB	–	nationalized commercial bank
NCDP	–	Northwest Crop Diversification Project
NGO	–	nongovernment organization
NPSSEB	–	National Private Sector Survey of Enterprises in Bangladesh
PCB	–	private commercial bank
PIC	–	project implementation committee
PIU	–	project implementation unit
PKSF	–	Palli Karma-Sahayak Foundation
PPMS	–	project performance management system
PRA	–	participatory rural appraisal
PRSP	–	poverty reduction strategy paper
PSC	–	project steering committee
SMESDP	–	Small and Medium Enterprise Sector Development Program
TA	–	technical assistance
TMSS	–	Thengamara Mohila Sabuj Sangha

## NOTES

- (i) The fiscal year (FY) of the Government ends on 30 June. FY before a calendar year denotes the year in which the fiscal year ends, e.g., FY2005 ends on 30 June 2005.
- (ii) In this report, "\$" refers to US dollars.

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## LOAN AND PROJECT SUMMARY

<b>Borrower</b>	People's Republic of Bangladesh
<b>Classification</b>	Targeting Classification: General intervention Sector: Agriculture and natural resources Subsector: Agriculture production, agroprocessing, and agribusiness Themes: Sustainable economic growth, private sector development Subthemes: Developing rural areas, private sector investment
<b>Environment Assessment</b>	Category FI
<b>Project Description</b>	The Project will promote agribusiness activities to generate employment and help alleviate poverty. Specifically, it will (i) promote small-scale agribusiness activities by channeling credit through reputable, experienced nongovernment organizations (NGO), and by providing technical and marketing support to small-scale agribusinesses throughout the rural areas of the country; (ii) strengthen participating NGOs and wholesale banks to ensure efficiency of the credit implementation and management; (iii) strengthen agribusiness associations for policy dialogue on the enabling environment, agribusiness promotion, and information dissemination; and (iv) improve the enabling environment for agribusiness development through legislative and regulatory changes, as well as reorientation training for the staff of public sector agencies.
<b>Rationale</b>	Bangladesh has few mineral resources, almost no forest resources, and severe infrastructure limitations. Productive agricultural land and a hardworking rural population are among the country's few resources and assets. Thus, future economic growth will require stimulating commercial activities within, and based on, the agriculture sector. Since almost all cultivable land is in use, increased growth in the agriculture sector must be derived from (i) diversification of agriculture production to higher value crops; (ii) intensification of production around homestead areas; (iii) provision of services to the agriculture sector (upstream links); and (iv) value addition through further processing, storage, and transport of agricultural commodities (downstream links). In other words, future economic growth will require an expansion of agriculture-based enterprises or agribusiness.
<b>Impact and Outcome</b>	The impact of the Project will be reduced poverty in Bangladesh through agribusiness growth that generates income and employment in the rural areas. The outcome of the Project will be expanded activities of rural enterprises engaged in commercial agriculture production, input supply, marketing, processing, and transportation. These will generate employment in rural and peri-urban areas, raise the value added of nontraditional crops and commodities, and increase rural incomes.

Specifically, the Project will target small-scale agribusinesses that do not have the wherewithal to mobilize the financing they require to expand, or the capacity to open up new downstream markets. This will be undertaken with the assistance of NGOs experienced in providing credit and support to rural enterprises at the grassroots level. The rural poor will be the ultimate beneficiaries of these actions through enhanced employment opportunities, income generation, and agricultural production.

### Cost Estimates

The project cost is estimated at \$60.0 million equivalent, comprising a foreign exchange cost of \$6.9 million equivalent and a local currency cost of \$53.1 million equivalent.

### Financing Plan

Source	(\$ million)		Total Cost	Percent
	Foreign Exchange	Local Currency		
Asian Development Bank	6.9	35.6	42.5	70.7
Government	0	2.0	2.0	3.4
Subborrowers	0	15.3	15.3	25.5
Contracted Service Providers	0	0.2	0.2	0.4
<b>Total</b>	<b>6.9</b>	<b>53.1</b>	<b>60.0</b>	<b>100.0</b>

Source: Asian Development Bank estimates.

### Loan Amount and Terms

The proposed Asian Development Bank (ADB) financing from ADB's Special Funds resources is equivalent in various currencies to Special Drawing Rights 28,910,000 (\$42.5 million equivalent). The loan will have a maturity of 32 years, including a grace period of 8 years, with an interest rate of 1.0% during the grace period and 1.5% thereafter, and such other terms and conditions set forth in the loan and project agreements.

### Allocation and Relending Terms

For the agribusiness credit line, the Ministry of Finance (MOF) will provide funding to Bangladesh Small Industries and Commerce (BASIC) Bank and Eastern Bank through subsidiary loan agreements on terms and conditions satisfactory to ADB. BASIC Bank and Eastern Bank will lend to the participating NGOs through onlending agreements on terms and conditions satisfactory to ADB. Participating NGOs will lend the loan funds to eligible subborrowers at their usual market rate.

### Period of Utilization

Until 30 June 2011

### Estimated Project Completion Date

31 December 2010

### Executing Agencies

Ministry of Agriculture (MOA), MOF

<b>Implementation Arrangements</b>	MOA will be responsible for all aspects of the Project, except the agribusiness credit line, which will be the responsibility of MOF. A project implementation unit (PIU) will be set up in the Department of Agricultural Marketing (DAM) to carry out day-to-day operations of the Project. MOF will be responsible for managing and overseeing the agribusiness credit line. BASIC Bank, Eastern Bank, and participating NGOs will implement the credit line component.
<b>Procurement</b>	The procurement of goods and related services will follow ADB's <i>Guidelines for Procurement</i> (the Guidelines). The procurement of equipment and machinery by small-scale entrepreneurs will be in accordance with para. 3.08 of the Guidelines (Purchase of Equipment for the Use of Small Private Sub-borrowers). A few vehicles and some office equipment for PIU will be procured, though no large purchases are required. Thus, PIU will purchase these items using methods specified in <i>Public Procurement Regulation 2003</i> , which are acceptable to ADB.
<b>Consulting Services</b>	The Project will require 652 person-months of consulting services, including 93 person-months of international consulting services and 559 person-months of domestic consulting services. Consultants will be recruited following the ADB's <i>Guidelines on the Use of Consultants</i> and other arrangements satisfactory to ADB for engaging domestic consultants. Consultants will be recruited as firms under three packages following quality- and cost-based selection procedures.
<b>Project Benefits and Beneficiaries</b>	<p>The Project is to stimulate commercial activities in the agriculture sector ranging from preproduction support to production to post-production handling, processing, transport, storage, and marketing. An expansion of these activities and increases in the value added to agricultural produce are expected to generate economic growth and employment, primarily in the rural areas. A review of sample enterprises shows that agribusiness investment is profitable, and generates substantial and permanent employment.</p> <p>The cumulative impact of the Project on the economy also will be significant through direct increases in production, expanded value added, and employment generation. Economic benefits will include an increase in employment opportunities of about 70,000 jobs. Additional indirect economic benefits will result from (i) higher production generated by the availability of better support services; (ii) heightened demand for agricultural produce for processing and urban sales, raising producer prices and increasing quantities of produce marketed; and (iii) a multiplier effect generated through greater demands for on-farm labor, transport, storage, and handling. Disadvantaged segments of the rural community, where 53% of the population lives in poverty, will benefit from the increased labor demand and increased demand for farm produce. The promotion of intensive agribusiness activities (such as dairy, poultry raising, and fish farming), which do not require significant land, also will benefit these poor segments directly.</p>

## **Risks and Assumptions**

NGOs will handle the majority of the investment under the Project by providing credit and support to small-scale agro-enterprises. Risks include (i) increased financial risks to NGOs due to the larger subloans to be provided to each borrower; (ii) increased credit risk to BASIC Bank and Eastern Bank in making larger-than-normal loans to NGOs, and (iii) the possibility that NGOs will not follow sound procedures in providing subloans.

The increased financial risk to NGOs will be dealt with in three ways. First, only NGOs with sound track records and a substantial financial base will be chosen. Second, the Project will provide substantial technical training and support to NGOs and the borrowers. Third, by focusing on subborrowers who have experience and some success based with previous microcredit borrowing or microenterprise experience, the Project will select low-risk, experienced clients. The increased credit risk to wholesale banks will be handled by following prudent practices, including (i) increasing loan size deliberately and steadily based on repayment performance of prior tranches, coupled with initial short-term lending followed by longer terms based on proven performance; (ii) limiting credit exposure to any one NGO borrower to less than 15% of the net worth through the use of two wholesale banks; and (iii) viewing all assets and liabilities of each NGO borrower and expected operating surpluses, rather than considering only project-related activities. This latter practice will be linked to a set of indicators (and action triggers) to keep the mix of assets and liabilities balanced. To address the risk of NGOs not following sound procedures, PIU will undertake a strong project performance management system, complemented by the wholesale banks' rigorous review of loan applications from the NGOs and the performance of their loan portfolios.

## **Technical Assistance**

The technical assistance (TA) of \$600,000 equivalent, financed from TA Special Fund, is to assist MOA and DAM in establishing a project supervisory and monitoring capacity in DAM. The TA also will guide and advise DAM and PIU personnel in agribusiness promotion and project management. The aim is to set the stage for an expansion of agribusiness activities in the future by establishing a focal point within the Government for agribusiness promotion.



## **I. THE PROPOSAL**

1. I submit for your approval the following report and recommendation on a proposed loan to Bangladesh for the Agribusiness Development Project (the Project).<sup>1,2</sup> The report also describes proposed technical assistance (TA) for Strengthening Project Management, and if the Board approves the proposed loan, I, acting under the authority delegated to me by the Board, will approve the TA.

## **II. RATIONALE: SECTOR PERFORMANCE, PROBLEMS, AND OPPORTUNITIES**

### **A. Performance Indicators and Analysis**

2. The economy of Bangladesh has a large rural population engaged in agriculture on increasingly fragmented landholdings. Given the country's extensive landlessness and almost total dependence on agriculture as a source of raw materials, Bangladesh must look to agribusiness development as a generator of employment, as well as a means of adding value to its main economic resources. The agribusiness sector covers (i) commercial production<sup>3</sup> of agricultural commodities, including crops, livestock, fisheries, and forestry; (ii) processing of agricultural commodities into products; (iii) provision of inputs for the production of agricultural commodities, including planting and genetic material, agro-chemicals, and equipment; and (iv) storage, marketing, and distribution of agricultural commodities and products. Expanding agribusiness and increasing business opportunities in rural areas could create an important source of employment for a labor force that grows by about 2 million people each year. The overwhelming majority of employment generated by agribusinesses is in rural areas, where 53% of the population lives in poverty.

3. Demand-driven agribusiness activities are critically important to the Bangladesh economy. Agribusiness accounts for about 10% of the country's gross domestic product (GDP), according to estimates.<sup>4</sup> Because the market demand is income-elastic (para. 5), the growth of agribusiness is much higher than the growth of agricultural production. While agricultural production grew by about 37% during the 1990s, agribusiness grew by about 66%—or roughly 5.2% annually over a decade. The growth of agribusiness, though faster than the 3.2% annual expansion in agriculture in that period, still was insufficient to generate the employment and income growth required to reduce poverty significantly and accelerate the overall growth of the rural economy. With proper support, however, agribusiness growth could accelerate to an estimated 7% a year or more, which would speed progress toward achieving the Millennium Development Goals.

### **B. Analysis of Key Problems and Opportunities**

#### **1. Development Potential**

4. Bangladesh has few mineral resources, almost no forest resources, and severe infrastructure and location limitations. Productive agricultural land and a hardworking rural population are among the country's main resources and assets. Thus, future growth will require stimulating commercial, value-adding activities within, and based on, the agriculture sector to generate the employment needed to help pull the bulk of the country's population out of poverty.

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<sup>1</sup> Project preparatory technical assistance (PPTA) was provided. ADB. 2003. *Technical Assistance to the People's Republic of Bangladesh for Preparing the Agribusiness Development Project*. Manila.

<sup>2</sup> The Design and Monitoring Framework is in Appendix 1.

<sup>3</sup> A commercial producer sells at least 75% of the agricultural goods.

<sup>4</sup> Agrico Limited. 2004. *PPTA Final Report on the Bangladesh Agribusiness Development Project*. New Zealand.

5. **Market Demand.** Bangladesh offers opportunities for agribusiness growth, because of its comparative advantage in producing a range of agricultural commodities<sup>5</sup> and the growing demand for a variety of quality, convenient, and high-value products. In the 1990s, the country achieved rice self-sufficiency. Increased food security has created greater opportunities for agricultural and nonfarm diversification. Growth of the economy has increased purchasing power, especially in urban areas, with the consequent rise in demand for nonstaple foods and more processed items.<sup>6</sup> The domestic market for safer, higher-quality, and more convenient and processed foods is potentially large.

6. **Small-Scale and Agro-Based.** A notable feature of Bangladesh's agribusiness sector is the dominance of small-scale units in production, processing, and distribution. The *National Private Sector Survey of Enterprises in Bangladesh*<sup>7</sup> (NPSSEB) reflects the overwhelming preponderance of small enterprises with less than 10 employees. Of the 6 million micro-, small, and medium enterprises (100 or fewer employees) in Bangladesh employing approximately 31 million people,<sup>8</sup> 90% have less than 10 workers, and 36% have only one worker. About 48% of the small enterprises (10 or fewer employees) are engaged in commercial agriculture; or provide forward and backward links through the supply of inputs and the processing, storage, and transport of agricultural produce. About 2.6 million small-scale agribusinesses are scattered throughout Bangladesh, and this number is growing 5.1% annually.<sup>9</sup>

## 2. Government Policies

7. Market reforms in the 1980s and 1990s provided a policy framework that was increasingly supportive of private sector involvement in agribusiness, which the public sector previously had controlled. This included private sector distribution of agricultural inputs and exports. The *National Agriculture Policy 1999*<sup>10</sup> strongly emphasized the commercialization of agriculture. Key proposals for developing an enabling environment for agribusiness included (i) promoting a competitive market with easy access for private sector traders, processors, and exporters to supply inputs and purchase outputs; (ii) ensuring comparable conditions for the Government, nongovernment organizations (NGOs), and the private sector; and (iii) monitoring and enforcing laws and regulations.

8. Despite the encouraging policies for agribusiness development, few concrete measures have been taken to improve the enabling environment in which agribusinesses operate. The policies lack consistency in defining the key objectives and strategies for agribusiness development. Policies often are established in very general terms, while the details needed to make a policy effective (e.g., specifying responsibilities and mechanisms of implementation) are often missing. Confusion about regulations affects the users, as well as the authorities responsible for enforcing them.

9. The Government lacks a focal point for agribusiness promotion. Agribusiness involves crosscutting issues related to production, commerce, and industry. However, the organization of ministries in Bangladesh is fragmented, which constrains the formulation and implementation of crosscutting policies. The Ministry of Agriculture (MOA) and Ministry of Fisheries and Livestock

<sup>5</sup> Agricultural commodities with comparative advantage and export potential include shrimp, fish, jute, tea, vegetables and fruits (fresh and processed), herbs and spices, and medicinal plants (Supplementary Appendix A).

<sup>6</sup> Demand estimates indicate that income elasticities are much higher for almost all of non-cereal agricultural products than for staple crops, particularly for fruits, vegetables, livestock, and fish (Appendix 2).

<sup>7</sup> Daniels, Lisa. 2003. *National Private Sector Survey of Enterprises in Bangladesh National Private Sector Survey of Enterprises in Bangladesh*. Department for International Development, et al.

<sup>8</sup> In contrast, Bangladesh has less than 1,000 large-scale enterprises employing more than 100 workers.

<sup>9</sup> World Bank. 2004. *Promoting the Rural Non-Farm Sector in Bangladesh*. Washington DC.

<sup>10</sup> Government of the People's Republic of Bangladesh. 1999. *National Agriculture Policy*. Dhaka.

(MOFL) are involved mainly in production issues at the farm level. The Ministry of Commerce looks mainly at trade issues, while the Ministry of Industry focuses on industry issues. In the absence of a lead agency responsible for agribusiness, the coordination needed for efficient development of this sector is difficult to achieve.

10. Most of the work of public sector line agencies associated with the agriculture sector is production-oriented. As such, most staff of these agencies do not understand the importance of downstream and upstream links, or the need to add value to primary produce. The Department of Agricultural Marketing (DAM) of MOA is the agency with the closest mandate to promote agribusiness. DAM has focused mainly on providing price information, collecting market levies, and registering traders. However, MOA wants to enhance DAM's capacity to provide broader services for market-led commercial agriculture development.

### **3. Rural Finance**

11. A critical constraint facing agribusiness entrepreneurs is their difficulty in mobilizing finance. NPSSEB, which indicated that most enterprises are small-scale and agro-based (para. 6), found that half identified availability of finance as the most important problem when starting up and during operations. Small-scale agribusinesses constitute a "missing middle"<sup>11</sup> market that is underserved by the commercial banking system and the country's microfinance NGOs.

12. Two development finance institutions (DFI), Bangladesh Krishi Bank and Rajshahi Krishi Unnayan Bank, and nationalized commercial banks (NCB) handle most of the agricultural credit. The bulk of this is for crop finance, with relatively little lending to rural agribusinesses. DFIs and NCBs are insolvent, failing to meet the prudential requirements set by Bangladesh Bank. They charge an artificially low interest rate, which is below cost on agricultural loans, and have a poor recovery rate. Moreover, the programs for rural credit channeled through DFIs and NCBs are unable to meet the growing demand from rural enterprises for a broader range of financial services. Rural deposits flow into urban credit, which undermines the business climate in the country, as well as the availability of inputs and technology for rural enterprises.

13. In contrast, a few private commercial banks (PCB) charge higher interest rates, have a better loan recovery rate, and maintain a healthy debt-equity financial structure needed for balanced growth. These institutions are viable and sustainable. Unlike DFIs and NCBs, however, PCBs lack rural coverage and are not interested in providing the small loans that most of Bangladesh's agribusinesses require. Moreover, potential small-scale investors usually lack the collateral that PCBs require to secure a loan, and cannot deal with the complex loan application procedures. NPSSEB data suggest that less than 15% of enterprises received formal credit from commercial banks.

14. Like the better PCBs, many of the country's larger NGOs that have developed loan portfolios for more than 5 years with financial and technical assistance from Palli Karma-Sahayak Foundation (PKSF) are well-managed, and have demonstrated their sustainability. In addition to microcredit, they provide a wide range of group and community training, as well as support services. However, NGOs generally have targeted the poorest rural groups, and would have difficulty mobilizing funds for small-scale commercial and agribusiness lending. Apex funding agency PKSF, the main source of funds for NGOs, has funded only programs that provide poverty-targeted microloans of less than \$500 each. NGOs interested in providing larger loans to commercial enterprises have had to find funding elsewhere, either from their own

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<sup>11</sup> As discussed in paras. 12-14, the investment of small-scale agribusinesses requires higher amount of financing than the microcredit provisions from NGOs, but is considered too small and risky by the commercial banks.

earnings or from commercial loans from banks. Since NGOs cannot provide large amounts of collateral, the latter option is limited.

15. In recent years, recognizing the potential for their successful microcredit clients to expand their operations to a commercial level, some experienced and reputable NGOs began to provide support to small rural enterprises. BRAC, which began lending to entrepreneurs through its *progoti* ("progress") program in 1997, has extended \$164.0 million equivalent to 140,000 enterprises. The Association for Social Advancement (ASA) will disburse \$8.0 million this year to about 12,000 enterprises through its small enterprise loan program. In 2002, Thengamara Mohila Sabuj Sangha (TMSS) initiated its own microenterprise loan program, which has an outstanding portfolio of \$2.0 million to about 2,000 borrowers. Microfinance institutions (MFI) are keen to scale up lending to microenterprises that are capable of expanding their operations, if suitable financing and business support is available.

#### **4. Constraints to Efficient Marketing and Technology Transfer**

16. The country's poor infrastructure is another key constraint to agribusiness growth. The problems include (i) poor road, rail, and water transport connections; (ii) inadequate and poorly maintained markets; (iii) lack of electricity connections (only about 30% of rural households have electricity, and the supply is unpredictable); (iv) poor port and airport facilities, which limit access to export markets; and (v) lack of storage facilities. Planned and ongoing projects on rural infrastructure and rural electrification are addressing many of these constraints. Still, infrastructure constraints to agribusiness expansion remain significant. Moreover, deficiencies in the management and operation and maintenance of markets prevent the available infrastructure from being used optimally.

17. A further constraint is the widespread lack of awareness of technologies for agribusiness development. For example, the handling and packaging of agricultural commodities are underdeveloped, resulting in considerable losses in quantity and quality. Few traders and processors, and even fewer farmers, use contractual arrangements for the sale or purchase of agricultural commodities. Most entrepreneurs do not use the information available through media, publications, and the internet due to lack of awareness, capacity, or initiative. Although awareness campaigns about new technologies exist, they are infrequent and often do not reach areas outside major cities.

18. The dissemination of agricultural technologies by public organizations is still largely focused on self-sufficiency targets and increasing staple crop yields at the farm level. It does not seek to improve post-harvest technologies, management systems, and processing technologies that could enhance competitiveness and add value. While research and extension programs focus on improving traditional smallholder systems of crop and animal production, they largely ignore the agribusiness dimensions. The design of research and extension programs does not emphasize sufficiently the link between farmers and markets.

#### **5. Opportunities for Project Support**

19. Reaching rural enterprises and providing them with support and encouragement to expand is difficult. No agency in the Government is tasked specifically with agribusiness promotion (paras. 9–10). Small rural enterprises constitute a "missing middle" market that is inadequately served by the formal financial system (paras. 11–14). Nonetheless, considerable opportunities for project support is provided by (i) the market demand for agribusiness products; (ii) the existence of a sustainable microfinance sector with the capacity and interest in scaling up its lending; and (iii) the country's well-established NGOs that provide a wide range of client

support services, in addition to credit. The uniformly small-scale and labor-intensive rural enterprises provide the opportunity for broadly based, pro-poor growth. Finally, the country's nascent private agribusiness trade associations, as well as the Government's willingness to consider policy reforms to support agribusiness and small, private sector enterprise development, offer further scope for project support.

20. **Meeting the Unmet Rural Finance Demand.** The Project must address the strong unmet demand for financial services from existing and potential enterprises. Few formal means for these agribusinesses to access finance are available (paras. 12–13). The NPSSEB found that 39% of the 2.6 million small-scale agribusinesses (or about 1 million enterprises) would like to get credit support, and are confident about paying it back.<sup>12</sup> Most of the credit demand is estimated to be for loans of \$500–\$5,000. If small-scale agribusiness need on average \$2,500 equivalent for short-term investment and operations, the total unmet credit demand would be far more than any project can offer.

21. **Working Through Experienced NGOs with Grassroots Contacts.** NGOs are a strategic entry point for the Project. Throughout the rural areas in Bangladesh, NGOs, especially the large ones, have significantly greater representation than commercial banks. They also have close links with farmers and rural entrepreneurs. Experienced and reputable NGOs, which previously have focused their development on nonagriculture activities, increasingly are becoming involved with agriculture-based activities, as well as with producers and entrepreneurs—individually and in groups—above the microcredit level. This change of focus is reflected by such initiatives as BRAC's progoti program, ASA's small enterprise loan program, and TMSS's microenterprise program (para. 15). These three programs, in particular, specifically target enterprises larger than those at the traditional microfinance level. However, these enterprises are smaller than those that PCBs lend to.

22. **Strengthening Agribusiness Associations for Policy Dialogue and Technology Dissemination.** The many agribusiness-related associations in Bangladesh provide an opportunity for partnership with the Project. With varying degrees of success, these associations have lobbied and engaged in business promotion. They have been less successful, however, in providing other services to their members, particularly in marketing and market-promotion. If strengthened and properly organized and managed, the associations can be an important tool for industry development, as they represent one of the more important links in the agribusiness value chain. For the Project, the associations can represent the interests of private sector entrepreneurs of all sizes in policy dialogue on the enabling environment for agribusiness development and rural finance. In addition, they can disseminate information and technical advice among their members, as well as among NGOs and their borrowers.

## 6. External Assistance

23. The Project will be the largest in Bangladesh directly focused on agribusiness. Of the projects relevant to agribusiness (Appendix 3), the most notable examples are the two agro-based technology development projects (ATDP) funded by the United States Agency for International Development. ATDPs facilitated the emergence of new agribusiness ventures and strengthened existing ones. ATDPs also formed many commodity-based associations, most of which are still functioning. With its much larger coverage, the Project will disseminate the ATDPs' success in promoting privately owned agribusinesses and enhancing their competitiveness.

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<sup>12</sup> An additional 20% need credit, but are concerned about not being able to pay it back.

24. Earlier and ongoing projects assisted by the Asian Development Bank (ADB) and other aid agencies confirm the value of working through credit-based project lending to reach the agriculture sector and agribusiness. Further, working with and through NGOs in Bangladesh generally has been very successful. Such projects include the first and second Participatory Livestock Development Projects<sup>13</sup> and the Northwest Crop Diversification Project (NCDP).<sup>14</sup> By the midterm review in 2004, NCDP had provided crop production credit through NGOs to farmers, with repayment of credit at about 100%. However, the progress of the NCDP pilot agribusiness credit line channeled through one NCB, Rajshahi Krishi Unnayan Bank, has been slow due to the bank's requirements that farmers provide collateral and possess landed property. The NCDP experience validates the use of reputable NGOs, rather than NCBs, to channel credit to the small-scale agribusinesses.

25. The Project will complement directly the Small and Medium Enterprise Sector Development Program (SMESDP),<sup>15</sup> and benefit from the SME policy reform. SMESDP is to lend to small- and medium-sized enterprises through PCBs. However, because of the restrictions on PCB lending (para. 13), most agribusinesses will be unable to borrow from SMESDP. By focusing on small-scale enterprises in rural areas, many of which lack the collateral that PCBs require, the Project will help the clients that SMESDP cannot reach.

26. The Project is consistent with the poverty reduction strategies of the Government and ADB, which recognize that the development of viable agribusinesses is essential to poverty reduction in rural areas. The National Strategy for Economic Growth, Poverty Reduction and Social Development<sup>16</sup> states that "the rapid growth of agriculture would require agroprocessing and agribusiness development to facilitate access of farmers to modern inputs and ensure increased demand for agriculture products." The ADB Country Strategy and Program<sup>17</sup> stresses the need to "transform agriculture from a subsistence to a commercial orientation and promote agribusiness development" as a means to "improve the livelihood of 76% of the country's population (and 85% of the poor)." To foster a vibrant and diversified rural economy, ADB assistance will contribute to (i) intensification, diversification, and value addition of the crops to boost agricultural productivity, improve food security, and foster rural enterprise development; (ii) strengthened farm-to-market links; and (iii) sustained growth of agriculture and agribusiness, which generate productive on-farm and off-farm employment to raise rural incomes.

## 7. Lessons Learned

27. The design of the Project takes into consideration lessons learned from ADB and other aid agencies' projects in the agriculture, micro and rural finance, horticulture, aquaculture, and livestock sectors in Bangladesh and other countries. The key lessons learned are:

- (i) The sustainable development of horticulture (agribusiness) depends heavily on private sector participation. Although the potential for horticulture (agribusiness)

<sup>13</sup> ADB. 1997. *Report and Recommendation of the President to the Board of Directors on a Proposed Loan to the People's Republic of Bangladesh for the Participatory Livestock Development Project*. Manila; ADB. 2003. *Report and Recommendation of the President to the Board of Directors on a Proposed Loan to the People's Republic of Bangladesh for the Second Participatory Livestock Development Project*. Manila.

<sup>14</sup> ADB. 2000. *Report and Recommendation of the President to the Board of Directors on a Proposed Loan to the People's Republic of Bangladesh for the Northwest Crop Diversification Project*. Manila.

<sup>15</sup> ADB. 2004. *Report and Recommendation of the President to the Board of Directors on Proposed Loans and Technical Assistance Grant to the People's Republic of Bangladesh for the Small and Medium Enterprise Sector Development Program*. Manila.

<sup>16</sup> Economic Relations Division, Ministry of Finance, Government of Bangladesh. 2003. *A National Strategy for Economic Growth, Poverty Reduction and Social Development*. Dhaka.

<sup>17</sup> ADB. 2005. *Country Strategy and Program 2006–2010, Bangladesh*. Manila.

- development is sufficient in Bangladesh, much more needs to be done, particularly for extension and processing.<sup>18</sup>
- (ii) Enhanced private sector roles in agricultural input and output markets are crucial for realizing the potential of agriculture production. While market liberalization has increased private demand for commercial credit, commercial banks are unprepared to serve the emerging needs of agriculture.<sup>19</sup>
  - (iii) The performance of public banks catering to rural areas has been poor. In contrast, the outreach of the MFIs and microcredit programs of NGOs has grown considerably. But they still need strengthening and support to meet the need of an important segment of rural entrepreneurs, i.e., the middles (footnote 11).<sup>20</sup>
  - (iv) Channeling a credit line requires a rigorous examination of the capacity of the participating banks and NGOs to act as effective financial intermediaries. The credit line should provide flexibility to participating banks and NGOs in setting their interest rates to reflect credit risks of the respective clients. Further, recycling should be monitored to prevent the use of the credit facility for purposes other than those intended by the Project.<sup>21</sup>

### III. THE PROPOSED PROJECT

#### A. Impact and Outcome

28. The impact of the Project will be reduced poverty in Bangladesh through agribusiness growth that generates income and employment in rural areas. The outcome of the Project will be expanded activities of rural enterprises engaged in commercial agriculture production, input supply, marketing, processing, and transportation. These will generate employment in rural and peri-urban areas, increase the value added of nontraditional crops and commodities, and increase rural incomes. Specifically, the Project will target small-scale agribusinesses that do not have the wherewithal to mobilize the financing they require to expand, or the capacity to open up new downstream markets. This will be undertaken with the assistance of NGOs experienced in providing credit and support to rural enterprises at the grassroots level. The rural poor will be the ultimate beneficiaries of all of these actions through enhanced employment opportunities, income generation, and agricultural production.

#### B. Outputs

29. The Project outputs include (i) establishment, expansion, and successful operation of agribusinesses by small-scale entrepreneurs; (ii) strengthened capacity of participating NGOs and wholesale banks in agribusiness lending; (iii) strengthened capacity of agribusiness associations in policy dialogue and agribusiness information and technology dissemination; and (iv) improved policy environment enabling private sector participation. The outputs will be delivered through the following components.

##### 1. Credit for Small-Scale Agribusinesses

30. This component is designed to capture the economic potential of the small-scale enterprises that make up the overwhelming majority of agribusinesses in the country. The Project will provide about 28,000 small-scale agribusinesses with credit through participating reputable NGOs. The total credit line is \$36 million. Each enterprise will determine its

<sup>18</sup> ADB. 2001. *Project Completion Report on the Horticulture Development Project in Bangladesh*. Manila.

<sup>19</sup> ADB. 1996. *Program Completion Report on the Food-Crops Development Program in Bangladesh*. Manila.

<sup>20</sup> World Bank. 2004. *Promoting the Rural Non-Farm Sector in Bangladesh*. Washington DC.

<sup>21</sup> ADB. 2003. *Project Performance Audit Report on Second Aquaculture Development Project in Bangladesh*. Manila.

investment and/or expansion needs, depending on the entrepreneur's assessment of the market and physical resources, and apply to the participating NGOs for assistance. Subloans will usually be \$500–\$5,000 equivalent each, with terms of 6 months to 3 years for working capital and fixed asset purchases. The Project will provide up to 70% of the envisaged cost of the investment, with the subborrower providing the balance (i.e., 30% or more). Activities to be financed will include (i) the provision of upstream agribusiness services, such as the provision and servicing of agriculture equipment or the sale of inputs (seed, seedlings, saplings, fingerlings, chicks, calves, and fertilizers); (ii) downstream activities, such as the collection, storage, processing, and transport of agricultural produce; and (iii) high-value commercial production itself, especially for nontraditional commodities.

31. Beneficiary entrepreneurs will include those who have participated successfully in NGO-sponsored microcredit programs and would like to scale up their activities to a more commercial level. Their microcredit activities provided these individuals with experience in commercial production and/or processing. They also have proven their entrepreneurial skills by operating successfully microventures, and meeting all loan repayment obligations. Many would like to access to larger amounts of financing to increase the scale of their economic activities. They already have links with NGOs that can attest to their skills and creditworthiness, and thus are prepared to lend to them for scaling up. However, the programs are not limited to former microcredit borrowers and can accommodate any potential small-scale entrepreneurs who meet the NGO's appraisal criteria.

32. The participating NGOs and wholesale banks must meet the eligibility criteria specified in Appendix 4. Bangladesh Small Industries and Commerce (BASIC) Bank and Eastern Bank have been identified as the wholesalers, because they (i) are financially sound, (ii) have a satisfactory return on equity and on total assets, and (iii) have low administration costs on their lending. The larger subloans that will be provided to each subborrower will increase the financial risks to NGOs, which had concentrated on traditional microfinance loans. To reduce these risks, the Project will begin with three large- and medium-scale NGOs: BRAC, ASA, and TMSS.<sup>22</sup>

## **2. Technical and Marketing Support for Agribusinesses**

33. This component aims to (i) provide technical and marketing assistance to the project subborrowers to ensure that small-scale entrepreneurs successfully operate and market their agribusinesses; and (ii) promote agribusiness in general, as well as specifically promote synergistic interaction among the service providers involved in agribusiness.

### **a. Training and Support for Small Entrepreneurs**

34. The participating NGOs will provide the subborrowers with services normally provided in their small enterprise lending programs. The NGO support will include training and guidance in business planning, small business financial control and reporting, and credit management. In addition, the NGOs will provide technical training in (i) livestock management and health; (ii) processing; (iii) product storage and transport; (iv) fisheries; (v) agronomy; (vi) marketing of high-value crops, such as fresh fruit, vegetables, and flowers; and (vii) nursery management.

35. The Project also will provide direct technical and marketing support to agribusiness entrepreneurs through an array of services that will (i) identify agribusiness opportunities involving large numbers of entrepreneurs through reviews of subsectors and NGO borrower

<sup>22</sup> Due diligence reports on the participating NGOs and wholesale banks, prepared following the ADB's *Operational Manual on Financial Intermediation Loans*, are in supplementary Appendixes C–G.

profiles; (ii) assist the formation of producer groups and associations to improve production output, timing, quality, and sales; (iii) facilitate and promote private sector links between entrepreneurs at each level of the value chain; (iv) hire specialists to provide technical expertise, as required, to clusters of similar entrepreneurs; and (v) arrange field trips to lead farmers, agribusinesses, and NGO staff.

36. Small-scale women entrepreneurs, who have demonstrated basic enterprise management skills and profitability, will receive special attention. They could play a vital role in linking producers, especially those supported by NGOs, with consumer markets. Guided by an international gender advisor and a domestic women's entrepreneur promotion specialist, the Project will help (i) identify opportunities for developing commercial links with producers, (ii) advise on packaging and market promotion, (iii) develop bankable business plans, and (iv) identify institutional sources of finance. As a result, the women entrepreneurs will be able to market and access raw materials on a regular basis and expand their businesses.

#### **b. Strengthening of Agribusiness Associations**

37. Agribusiness associations are playing a key role in the promotion of agribusiness in Bangladesh (para. 22). To help build up their capacities to provide effective services to their members and to agribusiness entrepreneurs in general, the Project will provide training, workshops, and domestic study tours on a cost-sharing basis. The Project will provide two thirds of the financing, while the associations will cover one third. The participants in this subcomponent will be selected on proposals submitted by the associations to improve their capacity based on a commitment to delivering reciprocal services to their members and agribusiness entrepreneurs.

#### **c. Agribusiness Information and Technology Dissemination**

38. This subcomponent will consist of publicity drives, trade fairs, seminars, and other awareness-raising and TA activities that will (i) inform stakeholders of income-earning opportunities in agribusiness; (ii) disseminate agribusiness technologies; (iii) bring together diverse stakeholders in agribusiness, including private sector, NGOs, and relevant line agencies and research bodies; and (iv) provide a venue for the promotion of the Project. Dissemination and TA activities will be selected based on proposals made by parties interested in promoting agribusiness. They will be contracted on a cost-sharing basis, with the Project financing two thirds and the service providers financing one third.

### **3. Strengthening Capacity of Participating NGOs and Wholesale Banks in Agribusiness Lending**

39. The Project will help participating NGOs (i) improve business plans with a focus on financing and supporting small-scale agribusinesses; (ii) strengthen their institutional capability in accessing and managing funds for agribusiness lending; (iii) enhance their management of the agribusiness loan portfolio and associated risks; and (iv) scale up their system of technical support to become more relevant to project-intended subborrowers. NGO staff will be trained to improve their capabilities on agribusiness promotion, loan appraisal (including assessing environmental and social impacts of the supported small-scale enterprises), loan review, and management. The Project will strengthen the participating NGOs in preparing and delivering the supporting services to subborrowers (para. 34) through workshops for NGO staff (training of trainers and senior staff) on ways to commercialize agriculture and improve value chain links; and reviews of NGO facilities devoted to technical support, as well as recommendations and financial support for scaling up these facilities for a more commercial and project-relevant focus.

40. Loan recovery will be monitored continually. Monitoring and reporting systems will be installed in each participating NGO to track project inputs and outputs, and to provide key performance indicators. Indicators to be monitored include (i) type of agribusiness being financed; (ii) amount of total investment, and lending by amount and terms provided under the Project to each subborrower; (iii) amount of agribusiness lending of the NGO as a proportion of its loan portfolio; (iv) number of borrowers financed through the Project; and (v) classification of the project-financed agribusiness loan portfolio in comparison with the total loan portfolio. Information will be disaggregated by gender. These indicators will complement the social and financial indicators that NGOs, PKSF, and Bangladesh Bank already monitor. The Project also will conduct sample checks of subborrowers to ensure that agribusiness is being financed, and that funds are not being diverted.

41. The Project will improve the capacity of BASIC Bank and Eastern Bank in managing NGO loan portfolios, while increasing their knowledge of agribusiness lending opportunities and management of associated risks. The Project will work with these banks to develop new guidelines and procedures, or streamline the existing ones, for evaluating and processing NGO proposals and administering commercial loans to NGOs. It also will establish performance and benefit indicators, and a process for monitoring these regularly through NGOs.

#### **4. Improving the Enabling Environment for Agribusiness**

42. This component is to help in removing inefficiencies in the policy environment, and to make entry into agribusiness more attractive for private sector entrepreneurs.

##### **a. Identifying and Correcting Major Policy Constraints**

43. The Project will assist MOA and other relevant government agencies in (i) identifying regulatory impediments to private sector operations in agribusiness; (ii) conducting workshops, seminars, conferences, and consultations with public and private sectors on required policy changes; and (iii) redrafting key regulations and legislative acts, as necessary. These activities will be transparent and public.

44. To encourage improved management of market infrastructure and wholesale centers, including expanded private sector roles and reinvestment of market income in improving market facilities, the Project also will (i) assess public market management and revenue distribution, (ii) assess the results of NCDP pilot market improvement efforts, and (iii) assist MOA in making necessary changes.

##### **b. Strengthening Public Sector Agencies in Agribusiness Governance, Support, and Promotion**

45. To enhance understanding of agribusiness, the Project will prepare, implement, and finance training programs on agribusiness to orient personnel of the relevant public sector line agencies (MOA, MOFL, others) to the characteristics and needs of this relatively new sectoral emphasis. The training courses will provide an overview of agribusiness in the country and its opportunities, and also introduce public service personnel to representatives of the private sector and NGOs operating in agribusiness.

#### **5. Project Implementation Support**

46. A project implementation unit (PIU) will provide implementation support. This will consist of physical facilities, staff, transport, and consulting services required for project activities on (i)

technical and marketing support to subborrowers; (ii) agribusiness promotion; (iii) training; (iv) accounting; (v) monitoring and evaluation; and (vi) liaising where necessary with BASIC Bank, Eastern Bank, and NGOs. MOA will set up and staff a permanent agribusiness cell, which will be responsible for (i) developing agribusiness policy and regulations; (ii) guiding agribusiness operations; and (iii) liaising with other ministries, PIU, and ADB.

### **C. Special Features**

47. The Project focuses on the “missing middle” of small-scale rural entrepreneurs, a key group with substantial economic growth potential that has been underserved by the rural financial system and by most aid agency-financed projects in Bangladesh. Agribusiness investments undertaken by these small-scale enterprises are expected to generate substantial direct employment opportunities and increase the demand for agricultural products. In turn, this will translate into demand for a broader range of produce, higher prices, additional employment, and increased rural incomes. The Project also will focus on working with the key public and private sector agencies to improve the enabling environment for agribusiness activities, thereby stimulating increased investments.

48. The demand of the subborrowers will determine the supports that the Project will provide. Short- to medium-term credit will be provided through qualified, reputable NGOs to enable the project target groups to invest in agribusinesses. In addition, assistance will be provided to help ensure that proposals for credit are viable, properly presented, and ultimately profitable. The Project, a pioneering initiative aimed at financing rural enterprises through NGOs, fits with the corporate goals of the proven NGOs to scale up to efficient MFIs.

### **D. Cost Estimates**

49. The estimated project cost is \$60.0 million equivalent, including physical and price contingencies, taxes and duties, and interest and service charges during construction. The estimated foreign exchange cost is \$6.9 million equivalent, or about 11.5% of the total cost. Local currency cost is estimated at \$53.1 million equivalent, or about 88.5% of the total project cost. The local currency cost will include an estimated \$0.3 million equivalent for taxes and duties to be paid by the Government. Summary project cost estimates are in Table 1. A project cost summary by expenditure account is in Appendix 5.

### **E. Financing Plan**

50. In response to the Government’s request, ADB decided to provide a loan of \$42.5 million equivalent from ADB’s Special Funds resources to finance 70.7% of the project cost. The ADB loan will fund the entire foreign exchange cost of \$6.9 million, as well as \$35.6 million equivalent of the local currency cost (67% of the total local currency cost). The Government is to provide \$2.0 million equivalent in the form of incremental staff salary, vehicle rental, overheads and operational cost, and taxes and duties. Subborrowers will finance \$15.3 million equivalent (in the form of asset contribution). Contracted service providers will finance \$0.2 million equivalent of the project cost on agribusiness promotion activities.<sup>23</sup>

51. Table 2 summarizes the financing plan. The Borrower will be the Government of Bangladesh. The high level of local cost financing is justified given that the Project is poverty-oriented and meets the financing demand for small-scale agribusiness investment, which has

<sup>23</sup> Cofinancing, which is not envisioned now, might be mobilized from commercial sources in the future to complement ADB financing for the facility. Such cofinancing could benefit from ADB credit enhancement, including guarantee instruments, and will be presented separately for consideration by ADB’s Board of Directors when it arises.

low foreign exchange inputs. The ADB loan will have a maturity of 32 years, including a grace period of 8 years. The loan will carry an interest charge of 1.0% during the grace period and 1.5% per year thereafter. The interest on the loan will be capitalized during the grace period.

**Table 1: Cost Estimates**  
(\$ million)

Item	Foreign Exchange	Local Currency <sup>d</sup>	Total Cost
<b>A. Base Cost<sup>a</sup></b>			
1. Credit for Small-Scale Agribusinesses			
a. Agribusiness Credit	3.6	32.4	36.0
c. Subborrower Investment Contribution	0.0	15.3	15.3
2. Technical and Marketing Support	0.7	1.5	2.2
3. Strengthening Capacity of Participating NGOs and Wholesale Banks in Agribusiness Lending	0.3	0.8	1.1
4. Improving the Enabling Environment for Agribusiness	0.9	0.9	1.8
5. Project Implementation Support	0.4	1.8	2.2
<b>Subtotal (A)</b>	<b>5.9</b>	<b>52.7</b>	<b>58.6</b>
<b>B. Contingencies</b>			
1. Physical Contingencies <sup>b</sup>	0.0	0.2	0.2
2. Price Contingencies <sup>c</sup>	0.1	0.2	0.3
<b>Subtotal (B)</b>	<b>0.1</b>	<b>0.4</b>	<b>0.5</b>
<b>C. Interest Charge During Implementation</b>	<b>0.9</b>	<b>0.0</b>	<b>0.9</b>
<b>Total</b>	<b>6.9</b>	<b>53.1</b>	<b>60.0</b>

NGO = nongovernment organization.

<sup>a</sup> In June 2005 prices.

<sup>b</sup> Physical contingency is 5% for training, workshops, surveys and studies, equipment, and vehicles.

<sup>c</sup> Estimated at foreign price escalator 2.8% in the first year, 1.9% in the following years, and domestic price escalator 5% per year.

<sup>d</sup> Includes taxes and duties of \$0.3 million.

Source: Asian Development Bank estimates.

**Table 2: Financing Plan**  
(\$ million)

Source	Foreign Exchange	Local Currency	Total Cost	Percent
Asian Development Bank	6.9	35.6	42.5	70.7
Government of Bangladesh	0	2.0	2.0	3.4
Subborrowers	0	15.3	15.3	25.5
Contracted service providers	0	0.2	0.2	0.4
<b>Total</b>	<b>6.9</b>	<b>53.1</b>	<b>60.0</b>	<b>100.0</b>

Source: Asian Development Bank estimates.

52. The Government will relend the designated credit line portion of the loan, equivalent to \$36 million in local currency, to BASIC Bank and Eastern Bank, in accordance with the subsidiary loan agreements with the terms and conditions and implementation arrangements satisfactory to ADB. The wholesale banks will lend to participating NGOs under onlending loan agreements upon terms and conditions satisfactory to ADB. The NGOs will provide these funds to qualified subborrowers under subloan agreements for investments within the scope of the Project. Details on the relending and onlending terms and conditions for the credit line are discussed in Appendix 7 (paras. 3–4).

## **F. Implementation Arrangements**

### **1. Project Management**

53. The project management structure is in Appendix 6. MOA and the Ministry of Finance (MOF) through its Finance Division will be the executing agencies. MOF will be responsible for managing and overseeing the flow of funds for the agribusiness credit line (component 1). It will be assisted by BASIC Bank, Eastern Bank, and participating NGOs whose financial management was found to be satisfactory for project implementation and whose long-term financial outlook is considered sustainable.

54. MOA will be responsible for implementing all aspects of the Project, except for component 1. The agribusiness cell will identify and correct major policy constraints (components 4a). If necessary, a joint committee will be set up to consider the recommended amendments to the policy issues that are beyond MOA's mandate. DAM will be responsible for the implementation of the rest of the Project, except for the provision of funds to NGOs. To help DAM and the agribusiness cell fulfill their roles, capacity building assistance will be provided under a grant-financed TA (paras. 67–68).

55. PIU, headed by a project director satisfactory to ADB, will be set up to carry out project implementation. A full-time project manager will assist the project director with project management and liaising with implementing agencies daily. The project manager, whose qualifications and experience will be satisfactory to ADB, will be hired on a commercial basis as a domestic consultant. Long-term domestic consultants, backed up by intermittent inputs from international consultants, will support PIU. In particular, an accounting specialist will be engaged to ensure the financial soundness of project management and the use of noncredit part of the project funds. PIU will rent premises outside MOA and DAM.

56. To oversee and guide the Project and resolve policy issues, a project steering committee (PSC) will be established<sup>24</sup> and will meet semiannually. A project implementation committee (PIC) will be established<sup>25</sup> to provide a venue to coordinate project activities and discuss (and resolve) project implementation issues transparently. Detailed implementation arrangements for the Project are in Appendix 7.

### **2. Project Implementation Period**

57. A project implementation schedule is in Appendix 8. The Project will be implemented over 5 years starting in January 2006. Initially, the agribusiness cell and PIU will be set up and the required staff will be recruited. This period will be followed by a preparatory phase, which will entail (i) formulating training programs; (ii) assessing the range of agribusiness services available; (iii) assessing the needs and capacities of the trade and industry organizations, as well as financing agencies; and (iv) disseminating information about the Project. Full implementation will begin by the fourth quarter of the first year and continue until the last year of the Project.

<sup>24</sup> The PSC, which will be chaired by the principal secretary of the Prime Minister's Office, will consist of secretaries of Economic Relations Division and the Finance Division of MOF, Planning Commission, Agriculture, Fisheries and Livestock, Commerce, Industry, and the representatives of Bangladesh Bank, BASIC Bank, Eastern Bank, and participating NGOs. A secretariat for the PSC will be established in the agribusiness cell. An additional secretary of MOA, as the head of the agribusiness cell, will be the member secretary of the PSC.

<sup>25</sup> The PIC will consist of representatives of MOA, MOF, Implementation Monitoring and Evaluation Division, Planning Commission, DAM, BASIC Bank, Eastern Bank, participating NGOs, and agribusiness organizations. The PIC will be chaired by the secretary of MOA, and the project director will be the member secretary of the PIC.

### 3. Procurement

58. The indicative procurement packages are in Appendix 9. Goods and related services will be procured following ADB's *Guidelines for Procurement* (the Guidelines). The procurement of equipment and machinery by small-scale entrepreneurs will be in accordance with para. 3.08 of the Guidelines (Purchase of Equipment for the Use of Small Private Subborrowers). A few vehicles and a small amount of office equipment for PIU will be procured, though no large purchases are required. PIU will purchase these items using methods specified in *Public Procurement Regulation 2003*<sup>26</sup> that are acceptable to ADB.

### 4. Consulting Services

59. The Project will require 652 person-months of consulting services, including 93 person-months of international consulting services and 559 person-months of domestic consulting services. Consultants will be recruited following ADB's *Guidelines on the Use of Consultants* and other arrangements for recruitment of domestic consultants acceptable to ADB. Consultants will be recruited as firms under three packages (Appendix 10) following quality and cost-based selection procedures. Appendix 10 outlines the estimated consulting service schedule, and Supplementary Appendix H gives the detailed terms of reference for consulting services.

### 5. Disbursement Arrangements

60. To ensure effective project implementation and timely disbursement, the Government will establish two project imprest accounts in the name of the Project immediately after loan effectiveness. One account will be for the credit line, while the other will be for the noncredit components. The imprest accounts will be held in Bangladesh Bank on behalf of the Government. Each imprest accounts will be established, managed, and liquidated in accordance with ADB's *Loan Disbursement Handbook*, and other detailed arrangements agreed to by the Government and ADB. The initial deposit into each imprest account will not exceed the estimated ADB-financed expenditures for the next 6 months for relevant components, or 10% of the relevant loan amount, whichever is lower. The statement of expenditure procedure will be used for reimbursing eligible expenditures and liquidating the imprest account for any individual payment transaction up to \$50,000 equivalent.

61. BASIC Bank and Eastern Bank each will establish and manage a revolving fund in their banks for the refinancing of participating NGOs. NGOs will repay loan principal into the revolving funds. Revolving loans to NGOs, based on their prior repayments, will be disbursed out of the revolving funds. BASIC Bank and Eastern Bank will initiate the Government's requests to ADB for replenishment of the imprest account. Further tranches of the credit line will take into account the balance remaining in the revolving fund, and requests from NGOs for loan finance based on their 6-month business plans. The subsidiary loan agreements between the Government and wholesale banks will establish a revolving fund mechanism, acceptable to ADB. Participating NGOs will use the revolving funds exclusively for small-scale agribusiness lending. The revolving funds will be maintained until ADB, in its discretion, requires the revolving fund to be dissolved. That decision will be made before project completion (para. 65). Balances available in such revolving funds will be credited to appropriate entities that the Government, in consultation with ADB, designates.

62. Each participating NGO will establish project accounts for the credit line within 1 month of loan effectiveness. NGOs will request BASIC Bank and Eastern Bank for advance funding for

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<sup>26</sup> Government of Bangladesh. 2003. *Public Procurement Regulation*. Dhaka.

their lending programs in local currency. BASIC Bank and Eastern Bank will decide on the amount of each loan to be sanctioned and disbursed, and then apply to the imprest account for these funds. When received, BASIC Bank and Eastern Bank will disburse funds within 3 working days to project accounts opened by each NGO in a reputable bank. The Government will ensure that disbursements from the imprest account to BASIC Bank and Eastern Bank, and from PIU for the noncredit activities, will be made within 5 working days of receipt of the disbursement applications.

## **6. Accounting, Auditing, and Reporting**

63. MOA, MOF, BASIC Bank, Eastern Bank, and the participating NGOs will maintain separate accounts and financial statements for funds provided to the Project. These accounts and related financial statements will be audited annually in accordance with appropriate auditing standards consistently applied by independent auditors acceptable to ADB. The executing agencies and implementing agencies will furnish ADB with the audited accounts and statements not later than 6 months after the end of the related fiscal year. PIU, through MOA, will submit to ADB diagnostic semiannual reports detailing project progress to date, problems encountered, measures taken to overcome them, and expected progress over the next 6 months period as well as any major or serious issues which need to be expeditiously addressed. Six months before the completion of the Project, PIU, through MOA, will submit to ADB a project completion report, detailing the utilization of loan proceeds, project implementation analysis, and the socioeconomic impact of the Project on the intended participants and ultimate beneficiaries, with special attention to poverty reduction.

## **7. Project Performance Monitoring and Evaluation**

64. Planning and monitoring of project progress will be scheduled, reviewed, and reported quarterly to ADB. A project performance management system (PPMS) will be established within 6 months of project commencement. A monitoring team will be established within PIU, and each of the implementing agencies, to ensure the operation of the PPMS throughout the Project. Within 3 months of project inception, PIU will identify baseline indicators in discussions with wholesale banks and participating NGOs. The main focus will be on the expansion of agribusiness investment, employment, and sales generated by the Project. In terms of benefit monitoring for component 1, information will be maintained concerning the amounts and numbers of loans disbursed to, and repaid by, subborrowers. They will be categorized as input suppliers, primary producers, and processors and marketing. To assess incremental benefits from the Project, basic household data for subborrowers will be kept concerning the number of family members, people employed, and estimated total revenues and net income. In addition to their usual financial and physical reporting, NGOs will classify and report to PIU, through wholesale banks, on their agribusiness loan portfolio each 3 months, and the proportion of agribusiness to total lending. Information will be maintained on the number of staff associated with agribusiness lending, as well as the number of staff participating in agribusiness courses and workshops. Information will be disaggregated by gender. Project lending and borrowing will be reviewed against total lending and the liability structures of each NGO, and against the overall financial performance of each NGO. The NGOs' performance will be measured by indicators such as (i) capital adequacy ratio, (ii) return on equity, (iii) average revenue on loans outstanding, (iv) administration expenses on lending, and (v) expenses to revenue ratio. During preparation of the project completion report, this data will be used to evaluate the impact of the Project on income and employment generation, and on improvements in the quality of life, especially for women and underprivileged groups. The ability of NGOs to continue to serve small agribusinesses also will be evaluated.

## **8. Project Review**

65. MOA, MOF, and ADB will carry out a project review twice a year. A midterm review will be undertaken not later than 2 years and 6 months after project commencement. This review will include a comprehensive evaluation of the project implementation arrangements and project progress, as well as consultations with the stakeholders. Recommendations will be made for adjustments, as appropriate, to the project scope, cost estimates, and implementation arrangements, including the feasibility of involving additional NGOs under the credit line component. Six months before project completion, ADB will arrange, in consultation with concerned parties, for operating the revolving funds after project completion.

## **9. Measures to Enhance Governance and Prevent Corruption**

66. The independent Anti-Corruption Commission, created with ADB support and constituted on 21 November 2004, will investigate all cases of irregularities. This includes financial irregularities, as well as corruption of government officials and officers and employees of autonomous bodies. The project design incorporates additional project-specific measures to enhance governance and prevent corruption during implementation (Appendix 11). Good governance measures, designed with the stages of project implementation and the disbursement chain in mind, include (i) providing consultant support and an associated advisory TA for project management and implementation training to staff of PIU, particularly in consultant recruitment and procurement; (ii) identifying beforehand the wholesale banks and participating NGOs; (iii) establishing transparent procedures for financial transactions; (iv) requiring implementing agencies to enter each amount of disbursed funds into an accounting system; (v) monitoring and reporting of NGO activities by PIU; (vi) appointing an NGO liaison officer within PIU to deal specifically with NGO concerns; and (vii) establishing the PIC.

## **IV. TECHNICAL ASSISTANCE FOR STRENGTHENING PROJECT MANAGEMENT**

67. The TA is to assist MOA and DAM in (i) establishing a project supervisory and monitoring capacity in DAM, and (ii) guiding and advising the personnel of DAM and PIU in agribusiness promotion and project management during the first 4 years of the Project. The aim is to set the stage for an expansion of agribusiness by establishing a focal point within the Government for agribusiness promotion. Capacity will be built through direct experience in administering and implementing the Project, guided by experienced consultants. As a result, DAM can develop a staff force familiar with (i) implementing aid agency-financed projects; (ii) characteristics of agribusiness promotion; (iii) NGOs and their programs; and (iv) other institutions contributing to agribusiness, such as agribusiness associations and enterprises.

68. Appendix 12 discusses terms of reference, cost estimates, and financing plan for the TA. The estimated TA cost is \$800,000 equivalent, with an ADB grant from the TA Special Fund covering \$600,000 equivalent. The Government will finance \$200,000 equivalent to cover workshops and training, office accommodation, additional vehicle rental and transport, and remuneration of counterpart staff. The TA will need an international project management training advisor with experience in project management and agribusiness promotion (12 person-months) on an intermittent basis. It also will need a full-time senior domestic project management training specialist (48 person-months). They will be recruited individually in accordance with ADB's *Guidelines on the Use of Consultants* and other arrangements for recruitment of domestic consultants acceptable to ADB. A vehicle and a set of office equipment will be procured using direct purchase following ADB's *Guidelines for Procurement*.

## V. PROJECT BENEFITS, IMPACTS, AND RISKS

### A. Benefits and Impacts

#### 1. Economic and Financial Benefits

69. Details of the Project Justification and Financial Analysis are in Appendix 13. The Project will stimulate commercial activities in the agriculture sector ranging from preproduction support through commercial production to postproduction handling, processing, transport, storage, and marketing. An expansion of these activities, and increases in the value added to agricultural produce, will generate economic growth and employment, primarily in the rural areas, though also in urban centers to some extent. Direct project beneficiaries will comprise the owners and employees of about 28,000 small agribusinesses. Each venture will employ 1–10 persons, more than half of which will be poor. Additional indirect benefits will come from (i) increased production, resulting from the availability of better support services; (ii) greater demand for agricultural produce for processing and urban sales, raising prices and augmenting the quantities of produce marketed; and (iii) a multiplier effect generated through greater demands for labor, transport, storage, and handling. Disadvantaged groups will benefit from higher labor demand, and through the promotion of intensive agribusiness activities (such as dairy, poultry raising, and fish farming) that do not require significant land.

70. An assessment of market demand indicates that sufficient bankable subprojects exist to justify the size of the agribusiness credit line. A review of sample enterprises shows that agribusiness investment is profitable, and generates substantial and permanent employment for the rural poor. Financial projections (Appendix 13 and Supplementary Appendixes C–G), prepared in accordance with ADB's *Guidelines on Financial Governance and Management of Investment Projects*, indicate that the NGOs will be in compliance with prudential financial indicators throughout the Project. The projected financial statements, together with the financial management assessments, suggest that NGOs and wholesale banks have sufficient financial and managerial capacity. The Project is considered financially viable and sustainable.

#### 2. Poverty Reduction and Social Impacts

71. Appendix 14 presents the Summary Poverty Reduction and Social Strategy. The Project will have significant direct and indirect impacts on poverty reduction. Direct impacts will come from employment created by new or expanded enterprises. Indirect impacts will come from employment and higher incomes generated by increased demand for produce and services, such as transport, handling, and storage needed for the operation of the new enterprises. Each small enterprise assisted by the agribusiness credit is to generate on average 2.5 new jobs. The average wage paid to staff is Tk115–130 per working day, well above the average of Tk65 for rural workers. The poverty ratio in rural areas, where most of these enterprises will be located, is 53%, and the demand will be for mostly semiskilled and unskilled labor. Thus, a high proportion of those employed will be poor. In addition, some indirect impacts will be generated through the expanded demand for raw materials. This will stimulate production, creating further employment and income-earning opportunities. The poverty reduction impact of the Project goes beyond the simple provision of a daily wage, however. Full-time employment also can provide sustained economic and social betterment. Previously unskilled laborers will have the opportunity to learn skills and develop a craft, and semiskilled workers will have the opportunity to perfect their skills.

72. As shown in Appendix 15, the Gender Action Plan (GAP) discussed specific actions to ensure that women receive as many of the project benefits as possible. Women's entrepreneur

associations will be provided with strengthening assistance under component 2, and their members will be encouraged to use the services provided under the same component. Some of the NGOs providing credit are focusing their efforts to a large extent on women borrowers, which will continue under the Project. A significant number of borrowers will be women, as demonstrated by the existing borrowers from NGOs such as TMSS, especially for dairy, poultry, fish-culture, fruit, vegetable, and flower cultivation, as well as small-scale processing.

### **3. Environmental and Resettlement Aspects**

73. The Project will involve many small-scale investments (\$500–\$5,000 equivalent) around the country. As such, any single activity under the Project is unlikely to have anything other than a minor localized environmental impact, or require any involuntary displacement of local populations. Public sector entities will not expropriate or acquire any land under the Project. Nevertheless, the project design has incorporated safeguards to minimize potential negative effects. Environmental and social impact specialists will be engaged to ensure that the environmental and social concerns of ADB and the Government are incorporated into work planning and monitoring of the Project. Through training, NGO staff will learn about potential negative impacts that might result from the economic activities they will be promoting, as well as the means to avoid or mitigate such impacts.

#### **B. Risks**

74. The majority of the investment under the Project will be for component 1. Risks include (i) increased financial risks to NGOs due to the larger subloans to be provided to each borrower, (ii) increased credit risk to BASIC Bank and Eastern Bank in making larger-than-normal loans to NGOs, and (iii) the possibility that NGOs will not follow sound procedures in providing subloans. The increased financial risk to NGOs will be addressed in three ways: (i) only NGOs with sound track records and a substantial financial base will be chosen; (ii) the Project will provide significant technical training and support to NGOs and the borrowers; (iii) by focusing on borrowers who have experience and some success with previous microcredit borrowing or microenterprise experience, the Project will select low-risk, experienced clients. The increased credit risk to wholesale banks will be handled by following prudent practices, including (i) increasing loan size to NGOs deliberately and steadily based on repayment performance of prior tranches, coupled with initial short-term lending followed by longer terms based on proven performance; (ii) limiting the lending to any single NGO in a year to less than 15% of the wholesale bank's net worth by engaging two wholesale banks; (iii) viewing all assets and liabilities of each NGO borrower and expected operating surpluses, rather than considering only project-related activities. This latter practice will be linked to a set of indicators (and action triggers) to keep the mix of assets and liabilities balanced.<sup>27</sup> To address the risk of NGOs not following sound procedures, PIU will undertake a strong PPMS, complemented by the wholesale banks' rigorous review of loan applications from NGOs and the performance of their loan portfolios.

75. Another risk is that vested interests in the Government might delay, or refuse to make, recommended and needed changes to legislation or regulations governing the sector. The project design has provided for this eventuality by allowing for an extensive series of public consultations, seminars, and workshops after the initial studies. Through these measures, the transparency of the consultation and reform process will make it difficult for parties with special interests to affect the outcome of regulatory reform.

<sup>27</sup> The set of triggers could be that the capital adequacy ratio is always greater than 20%, return on equity more than 12%, total borrowings less than 50% of loans outstanding, and expenses to revenues less than 90%.

## VI. ASSURANCES

### A. Specific Assurances

76. In addition to the standard assurances, the Government, BASIC Bank, and Eastern Bank have given the following assurances, which will be incorporated in the legal documents:

- (i) The Government will establish within DAM the PIU, which will be headed by a project director. The Government will ensure that, throughout project implementation, the PIU is staffed adequately with competent full-time personnel, according to the staffing schedule agreed with ADB. A full-time project manager will assist the project director in managing PIU on a day-to-day basis. The project manager, with qualifications and experience acceptable to ADB, will be hired on a contract basis from the open market as a domestic consultant.
- (ii) The Government will set up within MOA the agribusiness cell. Qualified staff from within MOA will be assigned to the cell. The Government will ensure that the agribusiness cell, which will be headed by an additional secretary of MOA, will be adequately staffed throughout project implementation.
- (iii) The Government will establish the PIC to be chaired by the secretary of MOA. The PIC will consist of representatives of MOA, MOF, Implementation Monitoring and Evaluation Division, Planning Commission, DAM, BASIC Bank, Eastern Bank, participating NGOs, agribusiness organizations, and the project director.
- (iv) The Government will establish the PSC to be chaired by the principal secretary of the Prime Minister's Office. The PSC will consist of secretaries of the Economic Relations Division and the Finance Division of MOF, Planning Commission, Agriculture, Fisheries and Livestock, Commerce, and Industry, representatives of Bangladesh Bank, BASIC Bank, Eastern Bank, and participating NGOs.
- (v) The Government will ensure adequate financing is made available in DAM's annual budget for the operation of PIU throughout project implementation.
- (vi) The Government will not plan or grant any debt amnesty, or forgive loan repayment obligations of subborrowers under the Project's credit line.
- (vii) The Government will ensure that throughout the project implementation and operation of the revolving fund BASIC Bank and Eastern Bank will be required to comply with prudential financial indicators set by Bangladesh Bank, including, among others, (a) classified loans less than 10% of total loans outstanding, (b) a capital adequacy ratio of at least 9%, (c) a loan deposit ratio of not more than 1.0. In addition, the participating NGOs will have to satisfy the agreed eligibility criteria.
- (viii) The Government, BASIC Bank, and Eastern Bank will ensure that no material organizational changes (financial, operational, or structural), or any changes in ownership of the project facilities, will be approved or implemented without prior approval of ADB, if such changes would affect their ability to perform their respective obligations under the Project.
- (ix) The Government, BASIC Bank, and Eastern Bank will establish and maintain separate accounts under the Project, and will cause the participating NGOs to do the same. Independent auditors acceptable to ADB will audit such accounts and related financial statements. The auditors' reports, with the audited accounts and financial statements, will be submitted annually to ADB through PIU.
- (x) The Government, BASIC Bank, and Eastern Bank will ensure that satisfactory procedures and operational policies for supervision and monitoring subloans will be established and maintained to ensure the achievement of the project objectives, and will cause the participating NGOs to do the same.

- (xi) The Government, BASIC Bank, and Eastern Bank will ensure compliance with all applicable environmental laws and regulations of Bangladesh and ADB's *Environment Policy 2002* and the established environmental assessment and review procedures, and will cause each participating NGO to do the same. Any project activities that harm the environment will not be utilized for financing.
- (xii) The Government, BASIC Bank, and Eastern Bank will ensure that no project activity will entail land acquisition or any involuntary resettlement impact including relocation, and will cause each participating NGO to do the same.
- (xiii) The Government, BASIC Bank, and Eastern Bank will adopt and fully carry out the GAP, and will cause each participating NGO to do the same. The GAP implementation will be documented in the PPMS and reported to ADB.

## **B. Condition for Loan Signing**

77. The Government will have countersigned and delivered to ADB a TA letter for the associated advisory TA for strengthening project management.

## **C. Conditions for Loan Effectiveness**

78. Before loan effectiveness, three conditions must be met:
- (i) The Government will have approved the Project's development project proposal.
  - (ii) PIU, the agribusiness cell, PIC, and PSC will have been set up and made operational in a manner satisfactory to ADB.
  - (iii) The subsidiary loan agreements between MOF and BASIC Bank, and between MOF and Eastern Bank, will have been signed and delivered to ADB in a form and substance satisfactory to ADB. These agreements will have become effective and binding upon the parties, in accordance with their terms, subject only to the effectiveness of the Loan Agreement.

## **D. Condition for Disbursement**

79. Withdrawals will not be made from the loan account for the credit line component of the Project until ADB has received at least two executed onlending agreements, in a form and substance satisfactory to ADB: one between BASIC Bank and one of the ADB recommended participating NGOs (BRAC, ASA, and TMSS), and one between Eastern Bank and one of the same participating NGOs.

## **VII. RECOMMENDATION**

80. I am satisfied that the proposed loan would comply with the Articles of Agreement of the Asian Development Bank (ADB) and recommend that the Board approve the loan in various currencies equivalent to Special Drawing Rights 28,910,000 to Bangladesh for the Agribusiness Development Project from ADB's Special Funds resources with an interest charge of 1% per annum during the grace period and 1.5% per annum thereafter; a term of 32 years, including a grace period of 8 years; and such other terms and conditions as are substantially in accordance with those set forth in the draft Loan and Project Agreements presented to the Board.

Haruhiko Kuroda  
President

4 October 2005

## DESIGN AND MONITORING FRAMEWORK

Design Summary	Performance Targets/Indicators	Data Sources/ Reporting Mechanisms	Assumptions and Risks
<b>Impact</b> Reduced poverty in Bangladesh through agribusiness growth that generates income and employment in rural areas.	<p>Agribusiness grows at an annual rate of 2 percentage points above the annual growth rate of GDP by 2010.</p> <p>Agribusiness contribution to GDP increased from the 10% to 15% by 2020.</p> <p>At least 40,000 small-scale agribusinesses start up or expand, and generate at least 100,000 jobs by 2020.</p>	<p>Government statistics on employment, agriculture production and productivity, trade, import and export, household income, and expenditure surveys</p> <p>Bangladesh Bank banking statistics</p>	<b>Assumptions</b> Government policies and actions support leading roles of NGOs and private sector in agribusiness.  GDP annual real growth of 5%, agribusiness annual growth rate of 7%.  Rural infrastructure developed and/or improved and sustained.  Government develops and monitors proper statistical framework for agribusiness.
<b>Outcome</b> Expanded activities of rural enterprises engaged in commercial agriculture production, input supply, marketing, processing, and transportation.	<p>Investment in agribusiness activities by participating entrepreneurs more than doubles by project completion review.</p> <p>Sales of agribusinesses increase by 30% by project completion review.</p> <p>Number of women agribusiness entrepreneurs increases by 50% by project completion review.</p> <p>Number of employees in agribusinesses increases by about 30% by project completion review.</p> <p>The value added per unit of commodities increases by about 20–30% by project completion review.</p> <p>Post-harvest losses drop by 20–30% of value of product production by project completion review.</p>	<p>NGO records</p> <p>Investment, purchasing, and production figures of downstream agro-industries</p> <p>Project benefit monitoring surveys</p> <p>Project progress reports</p> <p>Project completion report</p>	<b>Assumption</b> No serious macroeconomic and/or banking crises.  <b>Risks</b> Market fluctuations.  Natural disasters such as flooding.

Design Summary	Performance Targets/Indicators	Data Sources/ Reporting Mechanisms	Assumptions and Risks
<b>Outputs</b>			
1. Establishment, expansion, and successful operation of agribusinesses by small-scale entrepreneurs.	<p>The number of small rural entrepreneurs borrowing and receiving technical support from NGOs increases by about 28,000 during the project period.</p> <p>On-farm and off-farm employment opportunities increase directly by at least 350,000 person-years over 5 years.</p> <p>Each beneficiary enterprise receives subloans of \$500–\$5,000.</p> <p>30% of the beneficiary entrepreneurs are women.</p> <p>PIU and participating NGOs provide continual technical and marketing support to subborrowers.</p> <p>Subsector survey conducted in the first 4 years to identify agribusiness opportunities.</p> <p>Over 5 years, about 200 borrower training courses and 60 women entrepreneur training courses offered, field trip offered to 2000 agribusiness entrepreneurs, 18 new producer and marketing associations formed, and 18 value chain link promotion contracts formed.</p> <p>90% of agribusiness ventures still operating by project completion review.</p> <p>Subborrowers earning profits; classified loans are less than 5%.</p>	<p>NGO records and financial statements</p> <p>NGO loan classification data</p> <p>Monitoring by PIU</p> <p>Periodic project reviews</p> <p>Project progress reports</p> <p>Project completion report</p>	<p><b>Assumptions</b> NGOs can maintain high portfolio quality.</p> <p>Entrepreneurs are expanding enterprises or investing in complementary enterprises.</p> <p><b>Risks</b> Government sets restrictive limits (interest caps) on NGO lending.</p> <p>Government levies high income tax rate on NGOs that become microfinance institutions.</p>
2. Strengthened capacity of participating NGOs and banks in agribusiness lending.	<p>The project credit line (\$36 million equivalent) fully disbursed with classified loans to NGOs less than 5% at project completion.</p> <p>Lending by NGOs to agribusinesses expands by at least 2.5 times over 5 years.</p>	<p>NGO records and financial statements</p> <p>Wholesale bank records</p> <p>Monitoring by PIU</p> <p>Periodic project reviews</p> <p>Project progress reports</p>	<p><b>Assumptions</b> Qualified NGOs and wholesale banks participate as planned</p> <p>Agribusiness entrepreneurs are properly identified and supported.</p>

Design Summary	Performance Targets/Indicators	Data Sources/ Reporting Mechanisms	Assumptions and Risks
	<p>About 30 NGO staff training courses, 20 NGO liaison workshops, and 5 training courses on the monitoring and reporting system offered over 5 years.</p> <p>About 19 training courses on agribusiness, entrepreneurship and NGO orientation, and NGO loan appraisal and management offered to wholesale bank staff over 5 years.</p> <p>NGO staff trained on tapping women's potential and addressing gender-based needs.</p> <p>With all information disaggregated by gender, monitoring and reporting systems installed in each participating NGO by year 1.</p> <p>NGO lending to agribusiness grows annually at 20% and share of total portfolio increases 50% to become 6% of total loan portfolio by December 2011.</p> <p>NGOs sustainably implementing agribusiness programs and attracting commercial financing after project completion.</p>	<p>Project completion report</p>	<p>Effective training provided.</p> <p><b>Risk</b> Government sets restrictive limits (interest rate caps) on NGO lending.</p>
<p>3. Strengthened capacity of agribusiness associations in policy dialogue and agribusiness information and technology dissemination.</p>	<p>About 40 agribusiness association strengthening proposals financed.</p> <p>Membership of associations (including women chambers and associations) expands; regular meetings are held and officers are elected by open membership vote.</p> <p>About 30 workshops and seminars held.</p> <p>About 8 semiannual agribusiness promotion fairs held at throughout the country.</p>	<p>Annual reports of associations</p> <p>Regular project monitoring by PIU</p> <p>Regular project progress reports</p> <p>Project disbursement and/or withdrawal applications</p> <p>ADB review missions</p> <p>Project progress reports and project completion report</p>	<p><b>Assumptions</b> Interest exists among potential agribusiness entrepreneurs.</p> <p>Members perceive that agribusiness associations can play a meaningful leading role.</p> <p>Services provided are valuable and attract entrepreneur and association contributions.</p>

Design Summary	Performance Targets/Indicators	Data Sources/ Reporting Mechanisms	Assumptions and Risks
	<p>About 460 paraprofessionals trained in agribusiness promotion.</p> <p>All campaign messages are gender friendly.</p>		<p><b>Risk</b> Agribusiness association leaders concentrate on their own agenda instead of representing the views of a majority of association members, and the industry.</p>
<p>4. Improved policy environment enabling private sector participation.</p>	<p>Regulatory and marketing studies successfully completed with participation of NGOs, wholesale banks, and private sector representatives by 2007.</p> <p>Specific actions taken to rectify distortionary regulations by project completion.</p> <p>Improved market governance system in place by project completion.</p> <p>Women participating in the consultation and workshops.</p> <p>Ministry of Agriculture and other line agency staff made familiar with characteristics of agribusiness activities and their potential role in stimulating and supporting agribusiness.</p>	<p>Project implementation monitoring through progress reports, semiannual and annual reports of the PIU</p> <p>ADB review missions</p> <p>Project progress reports and project completion report</p> <p>Training course completion reports</p>	<p><b>Assumption</b> Line agencies staff are committed to reorientation of their role, and appropriate trainees are selected for training.</p> <p><b>Risks</b> Government does not have sufficient incentive to make recommended changes to regulations and marketing structure.</p> <p>Parliament might not approve or pass critical proposed legislative changes.</p>
<p><b>Activities with Milestones</b></p> <p>1. Project management and start-up</p> <p>1.1 Project implementation unit set up and functioning by January 2006</p> <p>1.2 All consultants recruited by June 2006</p> <p>1.3 Agreements and operating arrangements with wholesale banks and NGOs finalized by June 2006</p> <p>2. Credit for small-scale agribusinesses</p> <p>2.1 First disbursement of the agribusiness credit line by March 2006</p> <p>2.2 NGO selection of subborrowers begins March 2006</p> <p>2.3 NGO lending with supporting services begins by June 2006</p> <p>3. Technical and marketing support for agribusinesses</p> <p>3.1 Training and support for small entrepreneurs</p> <p>First agribusiness subsector survey begins February 2006</p> <p>Training and support for small entrepreneurs begins March 2006</p> <p>3.2 Strengthening of agribusiness associations</p> <p>Agribusiness association strengthening proposals received by March 2006</p> <p>Proposals assessed by June 2006</p> <p>Implementation of proposals commenced by September 2006</p>			<p><b>Inputs</b></p> <p>ADB: \$42.5 million equivalent</p> <p>Government: \$2.0 million equivalent</p> <p>Subborrowers: \$15.3 million equivalent</p> <p>Contracted service providers: \$0.2 million equivalent</p>

Design Summary	Performance Targets/Indicators	Data Sources/ Reporting Mechanisms	Assumptions and Risks
<p>3.3 Agribusiness information and technology dissemination  Agribusiness promotion proposals received by March 2006  First contracts for agribusiness promotion given by June 2006  Agribusiness promotion activities commence September 2006</p> <p>4. Strengthening capacity of participating NGOs and wholesale banks in agribusiness lending</p> <p>4.1 Strengthening participating NGOs  Business plans of NGOs reviewed by June 2006  Initial training programs for NGOs formulated by September 2006  Training programs for participating NGOs begin by January 2007</p> <p>4.2 Strengthening wholesale banks  Training program for wholesale bank staff formulated by June 2006  Training programs for wholesale bank staff initiated by September 2006</p> <p>4.3 Monitoring and reporting system set up in participating NGOs and wholesale banks by June 2006</p> <p>5. Improving the enabling environment for agribusiness</p> <p>5.1 Agribusiness cell set up and functioning by January 2006</p> <p>5.2 Regulatory policies  Policy study begins by September 2006, and completed by March 2007  Consultations of recommendations completed by June 2007  Approval of recommended changes by December 2007</p> <p>5.3 Market management  Marketing study begins by September 2006  Consultations commence by March 2007  Approval of recommended changes by January 2008</p> <p>5.4 Agribusiness training for the government staff  Formulation of agribusiness training program commences by March 2006  and completed by September 2006  Training program commences by January 2007</p>			

ADB = Asian Development Bank, GDP = gross domestic product, NGO = nongovernment organization, PIU = project implementation unit.

## AGRICULTURE SECTOR ANALYSIS AND AGRIBUSINESS DEVELOPMENT

### A. Rural Poverty in Bangladesh

1. Despite positive macroeconomic growth during the 1980s and 1990s, and over the last few years, Bangladesh remains one of the poorest countries in the world. Per capita gross domestic product (GDP) is \$361, and poverty incidence based on calorie intake is 50%.<sup>1</sup> While the incidence of poverty nationwide is high, rural poverty is even higher at 53%. Moreover, while urban poverty declined throughout the 1990s at a reasonable rate of 2.2% per year, rural poverty has been much more intractable, declining at the significantly slower annual rate of 1.6%.<sup>2</sup> The major economic activity in rural areas is agriculture production and agriculture-related activities. The agriculture sector accounts for about 60% of employment nationwide and about 90% in rural areas.

2. Poverty in Bangladesh remains largely rural: 80% of the population and 85% of the poor live in the countryside. The source of rural poverty can be readily identified. Due to extremely high population density, most of the rural residents eke out a living from limited land and agriculture resources. Some 6 million households (or 33% of the population) have no farm holdings at all, effectively meaning they are landless. Another 3.4 million households (19% of the population) have only marginal holdings of 0.02 hectare to 0.20 hectare. Thus, most people in Bangladesh do not have the land to earn enough income or grow enough food to be anything but poor. On the other hand, few other significant sources of income are available other than agriculture production. The country has few mineral resources, almost no forest resources, limited power generation capacity, and severe infrastructure and location limitations on rapid industrialization. As such, agriculture still represents the major source of raw materials in the country. Productive agricultural land, along with the manpower to cultivate it, is still the country's main resources and assets. Thus, any reduction in poverty will have to come from an intensification and diversification of the agriculture sector, as well as an increase in value added from the sector.

3. Even so, with the majority of the population owning so little land, most households never will break out of poverty through traditional crop production on their own land. Instead, they will have to earn their living from (i) producing higher value commodities, such as high-value crops or livestock and fisheries products; (ii) increased employment on larger farms; or (iii) through employment in agro-based enterprises of one type or another. Thus, the reduction of rural poverty depends on a commercialization of the agriculture sector to generate a range of income-earning opportunities in (i) diversified and intensified production, (ii) input supply, (iii) provision of services, (iv) processing, (v) packaging, (vi) transport, and (vii) downstream marketing to urban centers or abroad. In other words, the reduction of rural poverty in Bangladesh will depend on the expansion of commercial activities in the agriculture sector—agribusiness.

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<sup>1</sup> Osmani, S. R., W. Mahmud, B. Sen, H. Dagdeviren, and A. Seth. 2003. *The Macroeconomics of Poverty Reduction: the Case Study of Bangladesh*. United Nations Development Programme.

<sup>2</sup> Economic Relations Division, Ministry of Finance, Government of the People's Republic of Bangladesh. 2003. *A National Strategy for Economic Growth, Poverty Reduction and Social Development*. Dhaka.

## **B. Characteristics of Agriculture and Agribusiness in Bangladesh**

### **1. Overall Importance**

4. Agriculture remains a fundamental sector of the economy, accounting for 22% of the GDP in 2002 (down from about 30% at the end of the 1980s) and absorbing more than 60% of the workforce. When forward and backward links are taken into account, the agriculture and agribusiness contribution to GDP is estimated at about 35% (as opposed to about 38% in 1990), while the contribution to employment exceeds 75%.<sup>3</sup> Agribusinesses comprise about 3 million enterprises, of which 90% have less than 10 workers or employees and 36% have only one worker. Nonetheless, they are estimated to account for half of household income for about 15 million people.<sup>4</sup>

### **2. Crop Production and Diversification**

5. Crop production in Bangladesh is being transformed from subsistence farming to commercial farming. Most agricultural production still is concentrated on a limited number of crops, with rice accounting for about 79% of total cultivated area. Other major crops include wheat (5.0%), jute (3.2%), pulses (3.4%), sugarcane (1.2%), and oilseeds (3.0%). With the exception of wheat, most of these are traditional crops with only a limited scope for major market expansion or value added during processing. Crops with a high potential for cash income generation and value added through further processing, urban market sales, or export include spices, fresh vegetables, fruits, and potatoes. Though such crops account for only about 5% of the total cropped area,<sup>5</sup> the scope to expand production of these crops is considerable as demand and markets for the produce are developed. Bangladesh has begun to enter the European market with exports of vegetables and other high-value crops. The demand encourages private sector investment in high-value crop production, seed production (especially hybrid seeds), chemical and blended fertilizers, agroprocessing enterprises, etc.

### **3. Livestock**

6. Livestock production accounts for about 3% of GDP and 10% of agricultural GDP. Livestock production is an important component of the household income of poorer households, and employs about 20% of the rural labor force. Livestock production also has important backward links through the requirement for feed and (in the case of poultry) chicks, as well as forward links through processing.

### **4. Fisheries**

7. Fisheries are another important component of the sector. While Bangladesh's access to marine fish resources is limited, its inland fisheries resources are among the richest in the world. Fisheries provides livelihood to more than 1 million full-time and 10 million part-time fisher folks, and fish make up 80% of the animal protein intake of the population. Fisheries account for about 6% of the country's GDP and 72% of agriculture exports. Most of these exports consist of frozen shrimp, which generate foreign exchange earnings of \$270 million annually and constitute the

<sup>3</sup> Agrico Limited. 2004. *Project Preparatory Technical Assistance Final Report on the Bangladesh Agribusiness Development Project*. New Zealand.

<sup>4</sup> Daniels, Lisa. 2003. *National Private Sector Survey of Enterprises in Bangladesh*. Department for International Development, et al.

<sup>5</sup> Rice is grown for subsistence and for cash income generation.

second largest source of export earnings. As with livestock, backward and forward links are significant.

## 5. Income Elasticity of Agriculture Products

8. The estimates of income elasticity (Table A2.1) indicate that elasticities are much higher for noncereal agricultural products than for cereals, particularly for fruits, vegetables, livestock, fish, and a range of nonfarm services. Rising incomes in rural and urban areas in Bangladesh have spurred demand for noncereal crops, livestock, fishery, and processed food products, a trend that will continue to increase.

**Table A2.1: Income Elasticity for Major Product Groups**

		Food	Cereals	Noncereal Crops	Fruits	Fish	Livestock	Services
Income	Rural	0.65	0.30	0.72	1.15	1.08	1.50	1.52
Elasticity	Urban	0.58	0.23	0.55	1.04	0.87	1.25	1.39

Source: Hossain, M. 2003. *Rural Non-Farm Economy in Bangladesh: A View From Household Surveys*. Dhaka.

## 6. Emergence of Agribusiness in Bangladesh

9. Until the early 1990s, state-owned enterprises in subsectors such as sugar, jute, and fertilizers carried out most of the agribusiness. Private sector involvement in agribusiness was relatively modest and limited to subsectors such as tea, rice and wheat milling, and marketing of agricultural products. In the 1990s, private agribusinesses, as well as trade and industry associations, began to grow. This accelerated in the second part of the decade, and continued in the early part of the 2000s. Most growth took place in subsectors such as poultry, shrimp, potato and cold storage, fruit processing, and supermarket chains.

10. Four interrelated factors were responsible for the emergence of private agribusiness during the 1990s. First, market reforms initiated during the 1980s and continued in the 1990s provided a policy framework for the involvement of the private sector in several activities previously controlled by the public sector, such as the distribution of agricultural inputs and agricultural exports. Second, sustained growth of the economy has increased purchasing power, particularly in urban areas, with the consequent increase in demand for nonstaple foods and more processed items. Rice self-sufficiency achieved during this period increased food security and expanded opportunities for agricultural and nonfarm diversification. Third, infrastructure developments (the most notable example being the Jamuna bridge) improved opportunities for enterprise development. Improvements in road and telephone (e.g., the mobile revolution and internet) communication, electrification, and energy infrastructure (e.g., gas pipelines), while far from being adequate, have stimulated greater trade volumes and investment outside the two major urban centers of Dhaka and Chittagong. Fourth, some projects have facilitated the emergence of new agribusiness ventures and strengthened existing ones. The most important example of these projects was the Agro-based Technology Development Project I, which the United States Agency for International Development funded during 1996–2001.

## 7. Distribution of Agribusinesses in Bangladesh

11. Bangladesh has many household level, cottage or micro-industries concerned with processing agricultural and related raw materials, including nonfood items, involving jute, cotton, bamboo, or timber. Nonfarm households (i.e., the landless) manage about half of these, while

mostly small farmers (owning less than 1.0 hectare) manage the rest. These activities can be very important to the livelihood of the poorer segments of rural communities, which are unable to survive on crop production alone. Often, nongovernment organization (NGO) microfinance funds them. Investments in this category are typically below \$1,000 per household. These enterprises usually serve a localized market around the village or subdistrict headquarters.

12. The next layer of agribusiness is made up of rural-based enterprises. Bangladesh has about 3 million such enterprises, which make up the bulk of the country's agribusinesses. These typically include small poultry, dairy, and fisheries enterprises, as well as rural produce and input traders and transporters. This segment of rural business is fairly dynamic and market-driven. Investments are \$1,000–\$10,000 per enterprise.

13. Medium-sized, generally urban-based, agroprocessing enterprises constitute another layer. These include commercial juice, jelly, jam, pickles, and snack food preparation; potato cold stores; fish freezing plants; and farmers' service cooperatives. Most of them have investments well below \$100,000. At the upper level of the agroprocessing sector are large high-technology, capital-intensive enterprises, such as integrated shrimp processors, which have been operating in Bangladesh for some time and producing for export markets. Many of these have investments exceeding \$100,000. However, overcapacity has affected the shrimp industry due to disease problems in shrimp ponds, as well as difficulties with meeting the hygienic standards of the European Union. Exporters are resolving some of these problems by adhering to strict hygiene standards. A few large, urban-based processors also are engaged in the juice, poultry, and dairy industries that serve the national market.

14. These different strata of agribusiness tend to serve different markets. Table A2.2 shows an analysis of cottage, small, medium, and large enterprises in the country, the majority of which are agriculture-based.

**Table A2.2: Relationship Between Size of Company and Target Market**

<b>Scale (Capital Investment)</b>	<b>Local Village Market</b>	<b>Nearest Town</b>	<b>National Market</b>	<b>Regional Exports</b>	<b>EU and US Markets</b>
Cottage (less than \$1,000)	High	Low			
Small (\$1,000–\$10,000)	Low	High	Low		
Medium (\$10,000–\$100,000)	Low	Moderate	High	Low	
Large (more than \$100,000)	Low	Moderate	High	Moderate	Low

EU = European Union, US = United States.

Source: Montgomery, R. D., M. Khondkar, M. Hassanullah, and A. Sergeant. *Agribusiness Scoping Study*. Department for International Development and World Bank. 2002.

## **8. Sector Performance**

15. Over the past decade, the agriculture sector has increased productivity, including achieving self-sufficiency in rice. The sector also started modest diversification into value-added products, such as fruits, vegetables, poultry, dairy, and fish. This improvement was achieved despite a large population (close to 140 million) and high population density, scarce cultivable land (an average of 0.6 hectare per household), and regular occurrence of natural calamities. Nonetheless, the overall annual growth rate of agricultural GDP during the 1990s averaged about 2.4%, versus overall GDP growth of 5%. Over the past 4 years, general agricultural growth has improved, reaching an annual average growth rate of 3.7%.

16. While Bangladesh has the potential to intensify and diversify production further, and develop backward and forward links (through processing, packaging, storage, and export industries), little progress has been made. Most processing is small in scale and aimed at local markets. The poultry, dairy, and shrimp subsectors appear to be exhibiting the most rapid growth. In terms of post-harvest handling, packaging, storage and transport, the country is also seriously underdeveloped. For the local markets, virtually no packaging is used. Perishable fruits and vegetables are handled and transported in bulk or semi-bulk baskets, trucks, or boats without any protection or packaging. Motorized transport is available everywhere in Bangladesh. However, moving commodities from farm to consumer can take up to 10 days due to the many market intermediaries, and the need to pack and repack at every stage of the marketing chain. Warehouse and cold storage facilities for agricultural commodities are lacking. Except for potatoes, virtually no cold storage facilities are available for vegetables. Therefore, much remains to be done to realize the potential for the generation of additional employment through higher value agriculture and agribusiness, and to reduce poverty significantly.

### **C. Constraints**

17. A plethora of constraints impede the development of commercially based agriculture production, processing, and marketing in Bangladesh. Many are associated with the severely limited infrastructure, such as (i) poor road, rail, and water transport connections; (ii) inadequate and poorly maintained markets; (iii) lack of electricity connections (most rural households do not have electricity connections and the power supply is unpredictable); (iv) poor port and airport facilities, limiting access to export markets; and (v) general lack of storage facilities.

18. The regulatory environment in the country also constrains commercial activities in, or related to, the agriculture sector. Produce markets are poorly run and maintained. Nationally enforced quality and health standards for agricultural produce are missing. In addition, the general public and potential private sector investors, as well as the staffs of public sector line agencies, financing agencies, and development institutions, generally do not understand the potential for agribusiness development. Knowledge of potential markets for different types of agriculture products also is lacking. Moreover, potential investors are deficient in technical know-how.

19. However, the most serious constraint is the inability of potential investors to mobilize finance for agribusiness ventures. The two sources of formal credit available in rural Bangladesh are commercial banks and NGOs. Few rural enterprises borrow from commercial banks. Banks are not interested in the small loans that many agro-based enterprises require, and potential small-scale investors usually lack the collateral required by commercial banks to secure a loan. The *National Private Sector Survey of Enterprises in Bangladesh* (footnote 4) indicated that less than 15% of enterprises had received formal credit from commercial banks. Borrowing from NGOs also was limited. The survey found that 17% of enterprises had received credit from NGOs, although finance was identified as the most important start-up problem enterprises had faced. NGO lending for agribusiness has not been extensive. Except for a few of the more experienced NGOs, which are pioneering lending to enterprises, most traditionally have focused on poverty-targeted microfinance.

### **D. Implications for Project Design**

20. Given the many landless and marginal farmers, increases in the production of traditional staple crops alone will not be sufficient to reduce rural poverty in Bangladesh. Nonetheless,

economic growth and poverty reduction still will depend on increases in agriculture production and value added to that production. No other comparable resource base is available. This growth, however, will have to be based on employment generated and value added by switching to higher value commodities, and developing economic activities based on commercially oriented upstream and downstream links within the sector. The potential for growth in these types of activities is limited by the narrow range of commodities produced in the country. Still, the scope is large enough to generate considerable growth and employment through upstream input and service industries, as well as downstream handling, storage, and processing industries. Given the difficulties of accessing international markets on a large scale, these will be focused primarily on local and national markets.

21. Some constraints continue to prevent the rapid commercialization of the agriculture sector and agribusiness development. As many of these constraints are infrastructure-based, they will not be resolved until the country has better roads, rail links, water transport facilities, and international connections, as well as a more extensive and dependable electricity supply. Many constraints, however, can be tackled now. These include constraints imposed by (i) the regulatory environment; (ii) a lack of knowledge of investment potentials and the technologies involved in improved handling, storage, and processing; and (iii) lack of access to finance. The Project has been designed to begin addressing these latter constraints. The aim is to promote realistic agribusiness development within the medium term, while awaiting the longer-term infrastructure improvements (i.e., more and better roads, more dependable electricity supply, and better and more efficient port facilities). The longer-term improvements will be needed to stimulate growth in the sector and the development of export markets.

22. NGOs are the primary strategic points of entry to address the constraints to the sector. Under the Project, NGOs will provide agribusinesses with the finance they need to grow and expand. Several reputable NGOs now target enterprises with loans of up to \$5,000, whereas earlier lending seldom exceeded \$500 per subloan. However, they are having increasing difficulty mobilizing the finance they require for these programs. For BRAC alone, the funding requirement in 2005 exceeds \$100 million—and 20% growth in lending is projected each year. Agribusiness in Bangladesh comprises numerous small borrowers spread throughout the rural areas, which has limited the ability of NGOs to provide sound financial services with training and support. As such, an efficient means of supporting agribusiness in Bangladesh is to support the NGOs' new strategic thrust into the sector.

**EXTERNAL ASSISTANCE WITH RELEVANCE TO AGRIBUSINESS**

<b>Project Title</b>	<b>Duration</b>	<b>Executing Agency</b>	<b>Donors</b>	<b>Funding</b>
Small and Medium Enterprise Sector Development Program	2005–2008	Finance Division of Ministry of Finance, Bangladesh Bank	ADB	\$50.0 million
Northwest Crop Diversification Project	2001–2008	DAE, Bangladesh Bank	ADB	\$46.3 million
Rural Livelihood Project	1999–2006	Bangladesh Rural Development Board	ADB	\$42.6 million
Second Participatory Livestock Development Project	2004–2010	PKSF, Department of Livestock Services	ADB, Danida	\$20.5 million
Participatory Livestock Development Project	1997–2003	Department of Livestock Services	ADB, Danida	\$30.0 million
Rural Infrastructure Improvement Project	2003–2008	LGED	ADB, GTZ, KfW	\$76.9 million
Third Rural Infrastructure Development Project	1998–2005	LGED	ADB, IFAD, SIDA, JBIC	\$139.6 million
Farm to Market Enterprise Development Project	1998–2002	DAE	CIDA	\$14.0 million
Agriculture Sector Programme Support	2000–2011	MOA, MOFL	Danida	\$60.0 million
Agricultural Market Information Improvement Project	2002–2003	Department of Agricultural Marketing	FAO	\$256,500
Integrated Horticulture and Nutrition Development Project	2000–2005	DAE	FAO	\$5.7 million
Business Development Service Program	2003–2008	Ministry of Commerce	GTZ	€13.0 million
Bangladesh Seed Development Program	1997–2004	Bangladesh Agricultural Development Corporation	GTZ	\$7.5 million
Agricultural Diversification and Intensification Project	1997–2004	DAE, LGED	IFAD	\$18.9 million
Aquaculture Development Project	1998–2004	MOFL	IFAD	\$23.8 million
Agro-based Technology Development Project I	1996–2001	MOA	USAID	\$10.0 million
Agro-based Technology Development Project II	2001–2005	MOA	USAID	\$37.0 million
Agricultural Services, Innovation and Reform Project	1999–2003	DAE, Horticulture Export Development Foundation	World Bank, DFID, FAO	\$12.4 million
Export Diversification Project	1999–2003	Ministry of Commerce, Tariff Commission	World Bank	Tk169.8 million
<p>ADB = Asian Development Bank, CIDA = Canadian International Development Agency, DAE = Department of Agricultural Extension, Danida = Danish International Development Assistance, DFID = Department for International Development, FAO = Food and Agriculture Organization, GTZ = Gesellschaft für Technische Zusammenarbeit, IFAD = International Fund for Agriculture Development, JBIC = Japan Bank for International Cooperation, KfW = Kreditanstalt für Wiederaufbau, LGED = local government engineering department, MOA = Ministry of Agriculture, MOFL = Ministry of Fisheries and Livestock, PKSF = Palli Karma-Sahayak Foundation, SDC = Swiss Agency for Development and Cooperation, SIDA = Swedish International Cooperation Development Agency, USAID = United States Agency for International Development.</p> <p>Source: Asian Development Bank estimates.</p>				

## **ELIGIBILITY CRITERIA FOR PARTICIPATING NONGOVERNMENT ORGANIZATIONS AND WHOLESALE BANKS**

1. The Project will work with nongovernment organizations (NGO) that have developed sound microcredit loan portfolios, and are seeking to expand their portfolio of small-scale individual lending to agribusiness. Wholesale banks, which will be expected to conform to selected performance criteria, will finance the NGOs through lending.
  
2. To be selected and participate in the Project, wholesale banks must have:
  - (i) at least 3 years experience in project-relevant financing, including a steadily increasing portfolio of NGO or nonbank financial institution lending;
  - (ii) classified loans<sup>1</sup> accounting for less than 10% of total loans outstanding;
  - (iii) at least 3 years of satisfactory financial performance, as shown by financial statements audited to international accounting standards, as well as satisfactory financial forecasts for the current year and each subsequent year of the project participation that indicate profitability and the maintenance of prudent financial ratios;
  - (iv) a capital adequacy ratio<sup>2</sup> of at least 9%, plus satisfactory compliance with Bangladesh Bank regulatory and inspection requirements;
  - (v) a maximum loan deposit ratio<sup>3</sup> of 1.0; and
  - (vi) a proven ability to monitor and regularly report financial and physical indicators needed to measure project status and impact.
  
3. The maximum loan deposit ratio for the wholesale bank will be calculated excluding the portion of loan portfolio financed by project borrowing. Before a wholesale bank joins the Project, and for each year of participation, the bank should perform in accordance with the standards set in para. 2 for which Bangladesh Bank has supervisory responsibility.
  
4. To be selected and participate in the Project, NGOs must have:
  - (i) a level of governance and internal controls that clearly demonstrate an ability to manage and account for financial intermediation operations separate from, and independently of, other activities carried out by the NGO;
  - (ii) satisfactory compliance with standards and instructions issued by Bangladesh Bank for NGOs involved in microfinance;
  - (iii) a strategy statement within their corporate plan that shows a commitment to the development of agribusiness financial services;
  - (iv) satisfactory work plans for the next 3 years, showing project-related activities to be undertaken and their relationship with all other activities of the NGO;
  - (v) financing services to at least 100,000 borrowers before project participation;
  - (vi) at least 5 years of satisfactory financial performance and at least 3 years of satisfactory experience with microenterprises, as shown by financial statements and satisfactory external audit reports;
  - (vii) sound and transparent subborrower selection procedures, including, in the financing of production-related services, a detailed and time-bound plan that will result in the commercial packaging of these services and their ownership by private sector entrepreneurs;

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<sup>1</sup> Loans that are classified as substandard, doubtful, or loss.

<sup>2</sup> Capital adequacy ratio is a measure of a financial institution's financial strength, particularly its ability to cushion operational and abnormal losses. It is derived by comparing the ratio of an entity's equity with its asset-at-risk.

<sup>3</sup> The amount of a bank's loans divided by the amount of its deposits at any given time.

- (viii) satisfactory financial statements for the current year, and forecasts for each subsequent year of project participation, which indicate profitability and the maintenance of prudent financial ratios (profitability will be measured by a return on equity averaged over 2 years of not less than 6 percentage points above the rate of inflation and an expenses-to-revenue ratio of not more than 90%);
- (ix) a net worth of at least Tk120 million, and capital adequacy of not less than 12%; and
- (x) classified loans accounting for less than 10% of total loans outstanding.

5. The Asian Development Bank has conducted a due diligence review to compile a short list of NGO candidates for participation in the Project. The shortlist follows eligibility guidelines established for the Project. Wholesale banks will review the loan application of each NGO. If an application is considered bankable, the banks will determine how much to loan the NGO in accordance with own loan management procedures, which will have been modified with project assistance. The wholesale banks will bear the credit risk of NGO lending, and will financially monitor these NGOs and provide summarized reports to project implementation unit (PIU). NGOs will be required to provide summarized reports on social and financial aspects of their project activities to PIU. With consultant assistance, PIU will determine the content and frequency of these summarized reports. In addition, PIU will randomly inspect NGO head office and field office activities to ensure sound and transparent subborrower selection procedures are being followed.

6. PIU will work closely with the wholesale banks in the first 3 months to (i) develop guidelines and procedures to be followed in evaluating and accepting NGO proposals; (ii) establish priorities in the selection of proposals; (iii) establish performance and project benefit indicators, as well as a process of monitoring these regularly through NGOs; and (iv) formulate steps to be followed if an NGO ceases to perform satisfactorily. PIU and the wholesale banks will work out a procedure to follow that will enable a sample check of subborrowers to ensure that agribusiness is being financed, and that funds are not being diverted elsewhere.

## DETAILED COST ESTIMATE BY EXPENDITURE CATEGORY

**Table A5.1: Expenditure Accounts Project Cost Summary**

	(Tk Million)			(\$ Million)			% Foreign Exchange	% Total Base Costs
	Local	Foreign	Total	Local	Foreign	Total		
<b>A. Investment Costs</b>								
1. Agribusiness Credit	2,064.5	229.4	2,293.9	32.4	3.6	36.0	10	61
2. Subborrower Investment Contribution	974.9	—	974.9	15.3	—	15.3	—	26
3. Consulting Services								
a. International Consultants	—	129.7	129.7	—	2.0	2.0	100	3
b. Domestic Consultants	88.2	—	88.2	1.4	—	1.4	—	2
<b>Subtotal (A3)</b>	<b>88.2</b>	<b>129.7</b>	<b>217.9</b>	<b>1.4</b>	<b>2.0</b>	<b>3.4</b>	<b>60</b>	<b>5</b>
4. Contracted Services <sup>a</sup>	37.0	—	37.0	0.6	—	0.6	—	1
5. Training and Technical Supports	41.4	—	41.4	0.7	—	0.7	—	1
6. Vehicles and Equipment								
a. Vehicles and Motorcycles	10.0	9.9	19.9	0.2	0.2	0.4	50	1
b. Office Equipment and Furniture	22.0	7.3	29.3	0.3	0.1	0.4	25	1
<b>Subtotal (A6)</b>	<b>32.0</b>	<b>17.2</b>	<b>49.2</b>	<b>0.5</b>	<b>0.3</b>	<b>0.8</b>	<b>35</b>	<b>2</b>
7. Surveys and Studies	9.2	—	9.2	0.1	—	0.1	—	—
8. Project Staff	27.5	—	27.5	0.4	—	0.4	—	1
9. Overheads and Operational Costs <sup>b</sup>	82.3	—	82.3	1.3	—	1.3	—	2
<b>Total (A)</b>	<b>3,357.0</b>	<b>376.3</b>	<b>3,733.3</b>	<b>52.7</b>	<b>5.9</b>	<b>58.6</b>	<b>10</b>	<b>100</b>
<b>B. Recurrent Costs</b>								
<b>Total Baseline Costs</b>	<b>3,357.0</b>	<b>376.3</b>	<b>3,733.3</b>	<b>52.7</b>	<b>5.9</b>	<b>58.6</b>	<b>10</b>	<b>100</b>
Physical Contingencies	10.1	0.9	11.0	0.2	0.0	0.2	8	—
Price Contingencies	38.2	12.1	50.3	0.3	0.1	0.4	25	1
<b>Total Project Costs</b>	<b>3,405.3</b>	<b>389.2</b>	<b>3,794.5</b>	<b>53.1</b>	<b>6.0</b>	<b>59.1</b>	<b>10</b>	<b>101</b>
Interest During Implementation	—	57.6	57.6	—	0.9	0.9	100	2
<b>Total Costs To Be Financed</b>	<b>3,405.3</b>	<b>446.8</b>	<b>3,852.1</b>	<b>53.1</b>	<b>6.9</b>	<b>60.0</b>	<b>12</b>	<b>102</b>

<sup>a</sup> On strengthening agribusiness associations, and agribusiness promotion and information dissemination.

The contracted associations and service providers will provide one third of the proposed activity cost.

<sup>b</sup> Including vehicle and office rental expenses.

— = not available

Source: Asian Development Bank estimates.

**Table A5.2: Expenditure Accounts by Financiers  
(\$ million)**

	Asian Development Bank		Government of Bangladesh		Subborrowers		Contracted Service Providers		Total		Foreign (excluding Exchange Taxes)		Duties and Taxes
	Amount	%	Amount	%	Amount	%	Amount	%	Amount	%			
<b>A. Investment Costs</b>													
1. Agribusiness Credit	36.0	100.0	—	—	—	—	—	—	36.0	60.0	3.6	32.4	—
2. Subborrower Investment Contribution	—	—	—	—	15.3	100.0	—	—	15.3	25.5	—	15.3	—
3. Consulting Services													
a. International Consultants	2.1	100.0	—	—	—	—	—	—	2.1	3.5	2.1	—	—
b. Domestic Consultants	1.5	100.0	—	—	—	—	—	—	1.5	2.4	—	1.5	—
Subtotal Consulting Services	3.6	100.0	—	—	—	—	—	—	3.6	5.9	2.1	1.5	—
4. Contracted Services <sup>a</sup>	0.4	66.7	0.0	—	—	—	0.2	33.3	0.6	1.1	—	0.6	—
5. Training and Technical Supports	0.7	100.0	—	—	—	—	—	—	0.7	1.2	—	0.7	—
6. Vehicles and Equipment													
a. Vehicles and Motorcycles	0.3	75.9	0.1	24.1	—	—	—	—	0.3	0.6	0.2	0.1	0.1
b. Office Equipment and Furniture	0.4	87.5	0.1	12.5	—	—	—	—	0.5	0.8	0.1	0.3	0.1
Subtotal (A6)	0.7	82.8	0.1	17.2	—	—	—	—	0.8	1.4	0.3	0.4	0.2
7. Surveys and Studies	0.2	100.0	—	—	—	—	—	—	0.2	0.3	—	0.2	—
8. Project Staff	—	—	0.5	100.0	—	—	—	—	0.5	0.8	—	0.5	—
9. Overhead and Operational Costs <sup>b</sup>	—	—	1.4	100.0	—	—	—	—	1.4	2.4	—	1.3	0.1
Total Investment Costs	41.6	70.3	2.0	3.4	15.3	25.9	0.2	0.4	59.1	98.5	6.0	52.8	0.3
<b>B. Recurrent Costs</b>													
<b>Total Project Costs</b>	<b>41.6</b>	<b>70.3</b>	<b>2.0</b>	<b>3.4</b>	<b>15.3</b>	<b>25.9</b>	<b>0.2</b>	<b>0.4</b>	<b>59.1</b>	<b>98.5</b>	<b>6.0</b>	<b>52.8</b>	<b>0.3</b>
Interest During Implementation	0.9	100.0	—	—	—	—	—	—	0.9	1.5	—	—	—
<b>Total Disbursement</b>	<b>42.5</b>	<b>70.8</b>	<b>2.0</b>	<b>3.4</b>	<b>15.3</b>	<b>25.5</b>	<b>0.2</b>	<b>0.4</b>	<b>60.0</b>	<b>100.0</b>	<b>6.0</b>	<b>52.8</b>	<b>0.3</b>

<sup>a</sup> On strengthening agribusiness associations, and agribusiness promotion and information dissemination.

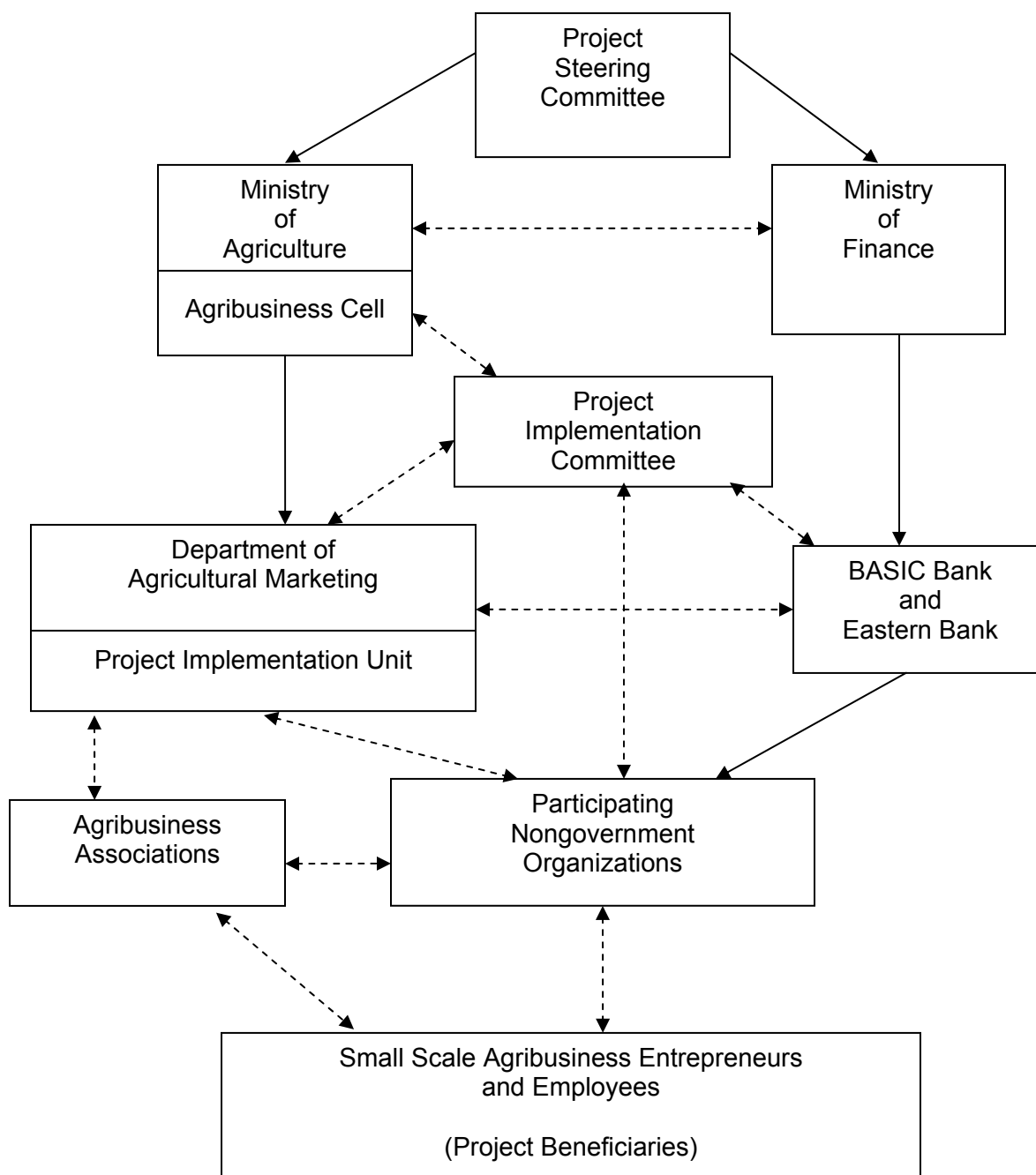
The contracted associations and service providers will provide one third of the proposed activity cost.

<sup>b</sup> Including vehicle and office rental expenses.

— = not available

Source: Asian Development Bank estimates.

## PROJECT MANAGEMENT STRUCTURE



Legend: Supervision 

Cooperation and Coordination 

Source: Asian Development Bank estimates.

## PROJECT IMPLEMENTATION ARRANGEMENTS

### A. Implementation Arrangements for Credit for Small-Scale Agribusinesses (Component 1)

1. **General.** The implementation of Credit for Small-Scale Agribusinesses (component 1) will depend on the participation of nongovernment organizations (NGO). NGOs interested in promoting agribusiness will be able to borrow from a credit line established in Bangladesh Small Industries and Commerce (BASIC) Bank and Eastern Bank. BASIC Bank and Eastern Bank, which will bear the credit risk for the NGO credit line, will select the participating NGOs. To assist BASIC Bank and Eastern Bank in the selection process, the Asian Development Bank (ADB) identified and conducted due diligence on three of the most qualified and experienced NGOs—each of which would be likely to participate in the Project. NGOs on this shortlist will be considered for the initial drawdown from the credit line. Additional NGOs may be considered for participation following the midterm review, provided they meet selection criteria (Appendix 4).

2. BASIC Bank and Eastern Bank will review the loan applications of each NGO to determine the amount of funds to be lent. If an application is considered bankable, the banks will determine the amount of the loan, following their own loan management procedures. These procedures will be modified with project assistance to meet the needs of the Project, while keeping in mind the financial soundness of the lending institutions. BASIC Bank and Eastern Bank will financially monitor the NGOs and provide summarized reports to the project implementation unit (PIU). The wholesale banks will inform PIU of the amounts lent, while the NGOs will inform PIU what their intended agribusiness development and lending targets are. NGOs will be required to provide to PIU summarized reports on the social and financial aspects of their project activities. With the assistance of the project monitoring consultants, PIU will determine the content and frequency of these summarized reports. PIU will report this information to the Ministry of Agriculture (MOA), which will pass it along to ADB. As part of the monitoring process, PIU will randomly inspect NGO field activities to ensure that the target group of the project is being reached.

3. **Lending Terms and Conditions for the Credit Line.** The Government will relend \$36 million equivalent in local currency to BASIC Bank and Eastern Bank at an annual service charge of 3.5% on the outstanding balance of disbursements from the Government. Loan terms and conditions will be set out in a subsidiary loan agreement between the Government and BASIC Bank and Eastern Bank. The wholesale banks and NGOs will borrow and repay their loans in local currency, free of foreign exchange calculations. BASIC Bank and Eastern Bank will lend to participating NGOs at the cost of funds from the Government, calculated on a simple interest basis plus the 3.5% spread. The rate charged to the NGOs will be 7%, the same as the Palli Karma-Sahayak Foundation charges larger NGOs. BASIC Bank and Eastern Bank will have a margin to cover the higher administrative and monitoring expenses associated with NGO and subproject lending, as well as provisions for bad and doubtful debt, and an adequate profit margin. As loan security, BASIC Bank and Eastern Bank stated that personal and corporate guarantees, supplemented where available by security over property and receivables, are accepted for lending to NGOs. Their primary focus will be on NGO cash flows available for loan repayment. Participating NGOs will borrow from BASIC Bank or Eastern Bank, and lend to their subborrowers to finance agribusiness activities. The service charge for this lending by NGOs will be at the prevailing market rate, which takes into account social mobilization, technical support, and financial service costs to ensure continuing operational viability. After 1 year, the Government and ADB will review the performance of the NGOs, and the impact of the service charge they imposed upon the subborrowers, for taking further action, if necessary.

4. The lending terms for participating NGOs will be based on the business plans submitted to BASIC Bank and Eastern Bank. Drawdowns for seasonal and short-term finance may be rolled over, subject to satisfactory performance by participating NGOs. At project completion, all outstanding lending to participating NGOs, which is unclassified according to Bangladesh Bank's standards, will be placed in revolving funds in BASIC Bank and Eastern Bank. These would continue to be available to NGOs for agribusiness activities. Repayment of funds by BASIC Bank and Eastern Bank would repay funds to the Ministry of Finance out of the revolving fund, which would close with a zero balance when ADB decides to dissolve the revolving fund.

#### **B. Implementation Arrangements for Technical and Marketing support for Agribusiness (Component 2)**

5. The agribusiness promotion consultants—working with NGOs, entrepreneur associations, and larger entrepreneurs that can be linked to small entrepreneurs in the value chain—will provide and develop the technical and marketing supports under Training and Support for Small Entrepreneurs (component 2a) through PIU. NGOs also will be encouraged to submit their own proposals for project support to improve their services for agribusiness borrowers and/or direct services for their borrowers. Proposals developed by the consultants and by NGOs, with the assistance of consultants for component 2a, will be submitted to a panel for review and approval. The panel will comprise the project manager, the project management training advisor (or his/her nominee), and the NGO associated with the proposal. The project management training advisor, in consultation with participating NGOs, will establish the guidelines for approving proposals and monitoring procedures.

6. Strengthening of agribusiness associations and agribusiness information and technology dissemination (components 2b and 2c) will be implemented based on proposals submitted to PIU. The proposals will specify what the training, capacity strengthening, or governance improvement needs are, and the types of promotional services the associations or service providers will provide. Funding will be shared. Approvals for component 2b will be based on the provision of some reciprocal service, such as participation in the training program for MOA staff or participation in one of the other activities under component 2 (e.g., the provision of technical advice). A committee comprising the project manager, the agribusiness promotion consultants, and the project management training advisor will vet the proposals for components 2b and 2c.

#### **C. Implementation Arrangements for Strengthening Capacity of Participating NGOs and Wholesale Banks in Agribusiness Lending (Component 3)**

7. NGO training courses will be designed and financed based on requests from, and appraisal of, individual NGOs. The agribusiness finance specialist, agribusiness promotion consultants, training specialist, gender advisor, women's entrepreneur promotion specialist, environmental and social advisor and specialists will deliver the courses. Training will be provided to the wholesale banks after the agribusiness finance specialist assesses the training needs.

#### **D. Implementation Arrangements for Improving the Enabling Environment for Agribusiness (Component 4)**

8. The agribusiness cell in MOA will implement identifying and correcting major policy constraints (component 4a) for the regulatory studies, while the Department of Agricultural Marketing (DAM) will implement the marketing studies. Consultants will be selected for the

necessary background studies, and to assist the agribusiness cell in drafting any revised regulations or legislation. The consultants also will assist in organizing consultations seminars, workshops, or publicity drives needed to get the revised legislation adopted. For regulations or legislation that are the responsibility of other ministries (for example the Ministries of Finance, Commerce, or Industry), a joint committee will be set up through the project steering committee to consider and redraft necessary recommended amendments.

9. Strengthening public sector agencies in agribusiness governance, support, and promotion (component 4b) will be implemented through PIU. A domestic training specialist, assisted by an international training advisor, will prepare curricula and formulate links with the private sector and NGOs for courses. These will be designed to illustrate agribusiness potential, and how this potential relates to the work of various line agencies, especially MOA and the Ministry of Fisheries and Livestock. The domestic training specialist then will ensure that training courses are provided at regular intervals (approximately 20 sessions per year for 4 years). The agribusiness cell will ensure that relevant staff of MOA and its line agencies are exposed to training when it is provided.

#### **E. Project Implementation Support (Component 5)**

10. Table A7.1 shows the incremental staff that will be needed for the project implementation support.

**Table A7.1: Incremental Staff Requirements**

<b>Position</b>	<b>Number of Staff Needed</b>
<b>A. Agribusiness Cell in MOA</b>	
1. Policy Officers	3
<b>Total</b>	<b>3</b>
<b>B. Project Implementation Unit</b>	
1. Project Director	1
2. Deputy Project Director	1
3. Senior Accountant Officer	1
4. Monitoring Officers	5
5. NGO Liaison Officer	1
6. Training Officer	1
7. Marketing Officers	4
<b>Total</b>	<b>14</b>

MOA = Ministry of Agriculture, NGO = nongovernment organization.

Source: Asian Development Bank estimates.

## PROJECT IMPLEMENTATION SCHEDULE

Activity	Year 1	Year 2	Year 3	Year 4	Year 5
<b>A. Project Start-Up</b>					
1. Appoint Project Staff	■				
2. Recruit Grant-Financed Consultants	■				
3. Set Up Project Implementation Unit	■				
4. Recruit Loan-Financed Consultants	■				
5. Establish Initial Working Arrangements with Participating NGOs and Wholesale Banks	■				
6. Establish Initial Ties with Agribusiness Organizations	■				
<b>B. Credit for Small-Scale Agribusinesses</b>					
1. Establish Imprest Accounts for Credit Lines	■				
2. Identify Small-Scale Borrowers by NGOs		■	■	■	■
3. Implement Small-Scale Lending Program		■	■	■	■
<b>C. Technical and Marketing Support for Agribusinesses</b>					
1. Training and Support for Small Entrepreneurs					
a. Training Program Formulation	■				
b. Training Program Implementation		■	■	■	■
2. Strengthening of Agribusiness Associations					
a. Receipt and Assessment of Proposals		■	■	■	■
b. Implementation of Proposals		■	■	■	■
3. Agribusiness Information and Technology Dissemination					
a. Contracts with Agribusiness Promotion Firms		■	■	■	■
b. Promotional Activities		■	■	■	■
<b>D. Strengthening Capacity of Participating NGOs and Wholesale Banks in Agribusiness Lending</b>					
1. Training in Agribusiness for NGOs					
a. Review and Revision of Business Plans	■				
b. Identification of Training Needs and Resources	■				
c. Implementation of Training Programs		■	■	■	■
2. Support to Wholesale Banks		■	■	■	■
<b>E. Improving the Enabling Environment for Agribusiness</b>					
1. Revision of Regulations					
a. Regulatory Study		■	■	■	■
b. Revising Regulations and/or Legislation		■	■	■	■
c. Consultations		■	■	■	■
d. Revised Regulations and/or Legislation Enacted			■	■	■
2. Revision of Marketing Legislation					
a. Marketing Study		■	■	■	■
b. Revision of Legislation		■	■	■	■
c. Consultations			■	■	■
d. Revised Legislation Enacted			■	■	■
3. Public Sector Agencies Training Program					
a. Formulation of Training Program	■				
b. Implementation of Training Program		■	■	■	■

NGO = nongovernment organization.

Source: Asian Development Bank estimates.

## INDICATIVE PROCUREMENT PACKAGES

Procurement Accounts	Number of Contracts	Mode of Procurement	Total Amount (\$ million)	ADB Financing (\$ million)
<b>A. Small-Scale Rural Credit</b>	Multiple	FI	36.0	36.0
<b>B. Consulting Services</b>	3	QCBS	3.6	3.6
<b>C. Contracted Services</b>	Multiple	DC	0.6	0.4
<b>D. Training and Technical Supports</b>	Multiple	DC	0.7	0.7
<b>E. Vehicles and Equipment<sup>a</sup></b>				
1. Vehicles and Motorcycles	4	DP	0.3	0.3
2. Office Equipment and Furniture	5	DP	0.5	0.4
<b>F. Surveys and Studies</b>	Multiple	DC	0.2	0.2
<b>Total</b>			<b>41.9</b>	<b>41.6</b>

ADB = Asian Development Bank, DC = direct contracting, DP = direct purchase, FI = financial intermediaries, QCBS = quality and cost-based selection.

<sup>a</sup> Including vehicle and office rental expenses.

Source: Asian Development Bank estimates.

## CONSULTING SERVICE SCHEDULE

	Person-Months					
	2006	2007	2008	2009	2010	Total
<b>A. International Consultants</b>						
1 Package 1. Agribusiness Lending and Technical and Marketing Support						
a. Agribusiness Promotion Advisor (team leader)	6.0	6.0	6.0	6.0	4.0	28.0
b. Agribusiness Finance Specialist	6.0	3.0	—	—	—	9.0
c. Environmental and Social Advisor	2.0	—	1.0	1.0	—	4.0
d. Gender Advisor	2.0	0.5	0.5	—	—	3.0
2 Package 2. Improving the Enabling Environment for Agribusiness						
a. Agribusiness Policy Advisor	3.0	6.0	3.0	—	—	12.0
b. Marketing Management Advisor	6.0	6.0	3.0	3.0	—	18.0
c. Training Advisor	4.0	3.0	3.0	—	—	10.0
3 Package 3. Project Implementation Support						
a. Project Management Information Advisor	6.0	2.0	1.0	—	—	9.0
<b>Subtotal (A)</b>	<b>35.0</b>	<b>26.5</b>	<b>17.5</b>	<b>10.0</b>	<b>4.0</b>	<b>93.0</b>
<b>B. Domestic Consultants</b>						
1 Package 1. Agribusiness Lending and Technical and Marketing Support						
a. Agribusiness Promotion Specialists (2 persons)	22.0	22.0	22.0	22.0	—	88.0
b. Women Entrepreneur Promotion Specialist	6.0	12.0	12.0	12.0	6.0	48.0
c. Training Specialist	9.0	12.0	12.0	12.0	3.0	48.0
d. Environmental Specialist	6.0	12.0	12.0	12.0	6.0	48.0
e. Social Impact Specialist	6.0	12.0	12.0	12.0	6.0	48.0
2 Package 2. Improving the Enabling Environment for Agribusiness						
a. Agribusiness Policy Specialist	6.0	12.0	6.0	—	—	24.0
b. Legal Specialist	-	6.0	12.0	6.0	—	24.0
c. Marketing Management Specialist	12.0	12.0	12.0	12.0	—	48.0
d. Training Specialist	9.0	9.0	9.0	9.0	—	36.0
3 Package 3. Project Implementation Support						
a. Project Manager (deputy team leader)	12.0	12.0	12.0	12.0	12.0	60.0
b. Project Management Information Specialist	12.0	12.0	—	3.0	—	27.0
c. Project Accounting Specialist	12.0	12.0	12.0	12.0	12.0	60.0
<b>Subtotal (B)</b>	<b>112.0</b>	<b>145.0</b>	<b>133.0</b>	<b>124.0</b>	<b>45.0</b>	<b>559.0</b>
<b>Total</b>	<b>147.0</b>	<b>171.5</b>	<b>150.5</b>	<b>134.0</b>	<b>49.0</b>	<b>652.0</b>

— = not available

Source: Asian Development Bank estimates.

**GOOD GOVERNANCE AND ANTICORRUPTION MEASURES**

<b>Potential Sources of Governance Failure</b>	<b>Prevention Measures Designed into Project</b>
<b>1. Project Start-Up</b>	<ul style="list-style-type: none"> <li>a. Identification of qualified participating nongovernment organizations (NGO) during appraisal</li> <li>b. Identification of potential participating wholesale banks during appraisal</li> <li>c. Project director to be appointed and project implementation unit (PIU) set up as condition of loan effectiveness</li> <li>d. Provision of advisory technical assistance (TA) on project management and implementation</li> </ul>
<b>2. Selection of Consultants</b>	<ul style="list-style-type: none"> <li>a. Department of Agricultural Marketing (DAM) to provide training in consultant selection procedures, according to the Asian Development Bank (ADB) guidelines provided by advisory TA consultants</li> <li>b. Selection process to be monitored by advisory TA consultants</li> <li>c. Short-listing and selection documents and procedures to be reviewed by ADB staff</li> </ul>
<b>3. Provision of Loans to NGOs by Wholesale Banks</b>	<ul style="list-style-type: none"> <li>a. Establishment of a project implementation committee, including all implementing stakeholders, so that governance and control issues can be raised and resolved transparently</li> <li>b. PIU monitoring of onlending under guidance of advisory TA consultants</li> <li>c. NGO liaison officer of PIU review of specific NGO complaints</li> <li>d. Bangladesh Bank monitoring of wholesale banks on behalf of the Ministry of Finance</li> <li>e. ADB staff monitoring of disbursement progress</li> </ul>
<b>4. Provision of Subloans to Entrepreneurs by NGOs</b>	<ul style="list-style-type: none"> <li>a. Wholesale banks review of NGO subborrower selection procedures before onlending</li> <li>b. Loans recorded and classified to Bangladesh Bank standard</li> <li>c. Requirement for annual external audit of project funds disbursed to NGOs through wholesale banks</li> <li>d. PIU staff monitoring of NGO field activities</li> <li>e. NGO liaison officer review of specific complaints from potential subborrowers</li> </ul>
<b>5. Procurement of Service Contracts by PIU</b>	<ul style="list-style-type: none"> <li>a. Training of PIU staff in procurement, according to ADB guidelines provided by advisory TA consultants</li> <li>b. Advisory TA consultants monitoring of service contracting</li> <li>c. Requirement to publicly announce service contract program and results of bidding</li> <li>d. Requirement to include names of contractees, amounts of contract, and terms of reference in semiannual and annual reports</li> <li>e. ADB staff monitoring of procurement</li> </ul>
<b>6. Procurement of Office Space, Vehicles, Equipment, and Materials by PIU</b>	<ul style="list-style-type: none"> <li>a. Training of PIU staff in procurement, according to ADB guidelines provided by advisory TA consultants</li> <li>b. Advisory TA consultants monitoring of procurement</li> <li>c. ADB staff monitoring of procurement</li> </ul>

Source: Asian Development Bank estimates.

## TECHNICAL ASSISTANCE FOR STRENGTHENING PROJECT MANAGEMENT

### A. Consulting Services

1. An international project management training advisor and a domestic project management training specialist will be recruited. The project management training advisor will be a highly qualified professional with experience in the management of internationally financed projects and agriculture or agribusiness development. A knowledge of, or experience in, providing credit to agricultural enterprises, as well as banking and finance, will be valuable. Experience in the agriculture, agribusiness, or small- and medium-sized enterprise sector in Bangladesh also will be viewed positively. The project management training specialist will be a highly qualified Bangladeshi professional with experience in managing internationally financed projects and possessing extensive contacts within the private sector, the nongovernment organization (NGO) sector, and the Government. The specialist will be familiar with the agriculture sector and its importance in Bangladesh, and will have a broad understanding of the role of NGOs and the private sector in developing the rural economy. Familiarity with credit programs and the banking and finance sector will be valuable attributes.

2. The project management training advisor will work intermittently for 12 person-months in the first 3 years of the Project, while the project management training specialist will work full time for the first 4 years. The consultants' primary responsibilities will be to help the project implementation unit (PIU), through on-the-job training, ensure a smooth project start-up and to build up PIU's capacity to manage the Project on its own. The duties will be to:

- (i) Prepare terms of reference for the agribusiness cell.
- (ii) Guide the Ministry of Agriculture (MOA) in setting up an agribusiness cell and the Department of Agricultural Marketing (DAM) in setting up PIU, paying particular attention to the recruitment of suitable staff.
- (iii) Guide MOA and DAM in the shortlisting, selection, and recruitment of the loan-financed project consultants, ensuring that the Asian Development Bank (ADB) guidelines are properly followed.
- (iv) Assist in the physical establishment of PIU office and the procurement of vehicles and equipment, ensuring that ADB's *Procurement Guidelines* are followed.
- (v) Work with the project manager to establish initial ties between PIU, NGOs, and wholesale banks; and establish initial ties between PIU and agribusiness associations.
- (vi) Ensure the full integration of NGOs, agribusiness organizations, and wholesale banks into the project structure on an operational basis.
- (vii) Ensure that the project imprest accounts are set up promptly, and that channels are established for the expeditious flow of funds to PIU and wholesale banks.
- (viii) Advise on the establishment of the project performance monitoring system to be designed and tested by loan-financed consultants.
- (ix) Ensure that the regulatory study and marketing study in Improving the Enabling Environment for Agribusiness (component 4) are initiated as scheduled, and guide MOA in the review of the studies and in determining the steps to implement the consultants' recommendations.
- (x) Assist the project manager and the loan-financed consultants in establishing reporting systems, formats, and procedures; and assist with the initial reports to MOA and ADB.
- (xi) Work closely with the project manager and the staff of the PIU to expedite the start of implementation. This will include ensuring that (a) the training program for

- NGOs is established, functioning, and funded; (b) agribusiness associations are informed of the Project, and submit proposals for strengthening; (c) contracts are let to promote the Project in particular and agribusiness in general; and (d) consulting services are fielded for strengthening NGOs and wholesale banks.
- (xii) Chair meetings of the committee adjudicating applications for technical assistance provisions and contract services under Technical and Marketing Support for Agribusiness (component 2).
  - (xiii) After the start-up period, provide back-stopping advice to the project manager, MOA, NGOs, and wholesale banks on project operations; and ensure that ADB is apprised of any serious issues or potential issues as soon as possible to achieve smooth and unimpeded project implementation.

## B. Cost Estimates

3. The total cost is estimated at \$800,000 equivalent. The Government has asked ADB to finance \$600,000 equivalent, covering the entire foreign exchange costs (\$300,000 equivalent) and part of the local costs (\$300,000 equivalent). ADB will fund these with a grant basis from the technical assistance funding program. The proposed government contribution of \$200,000 equivalent will cover workshops and training, office accommodation, additional vehicle rental and transport, and remuneration of counterpart staff. The estimated cost breakdown is in Table A12.1.

**Table A12.1: Technical Assistance Cost Estimates and Financing Plan**  
(\$'000)

Item	Foreign Exchange	Local Currency	Total Cost
<b>A. Asian Development Bank Financing<sup>a</sup></b>			
1. Consultants			
a. Remuneration and Per Diem			
i. International Consultant	210.0	0.0	210.0
ii. Domestic Consultant	0.0	230.0	230.0
b. International and Local Travel	10.0	5.0	15.0
c. Reports and Communications	5.0	5.0	10.0
2. Equipment <sup>b</sup>	10.0	10.0	20.0
3. Vehicle and Operating Costs	30.0	5.0	35.0
4. Miscellaneous Administration and Support Costs <sup>c</sup>	0.0	20.0	20.0
5. Contingencies	35.0	25.0	60.0
<b>Subtotal (A)</b>	<b>300.0</b>	<b>300.0</b>	<b>600.0</b>
<b>B. Government Financing</b>			
1. Office Accommodation and Transport	0.0	50.0	50.0
2. Remuneration and Per Diem of Counterpart Staff	0.0	35.0	35.0
3. Counterpart Staff Travel	0.0	25.0	25.0
4. Workshops and Training	0.0	90.0	90.0
<b>Subtotal (B)</b>	<b>0.0</b>	<b>200.0</b>	<b>200.0</b>
<b>Total</b>	<b>300.0</b>	<b>500.0</b>	<b>800.0</b>

<sup>a</sup> Asian Development Bank's technical assistance funding program to provide financing on a grant basis.

<sup>b</sup> Including a photocopier, an air conditioner, computers, printers, scanners, and other required office equipment.

<sup>c</sup> Including office utilities and supplies, and secretarial expenses.

Source: Asian Development Bank estimates.

## PROJECT JUSTIFICATION AND FINANCIAL ANALYSIS

### A. Introduction

1. The growth of the rural economy is essential to poverty reduction in Bangladesh, as well as the expansion of the national economy. Most of the poor in Bangladesh live in rural areas, deriving their livelihood from agriculture. Accelerating agricultural growth will be impossible if strategies continue to focus mainly on production. The agriculture sector has to be reoriented towards agribusiness, including commercial production, processing, and marketing, to grow and generate large benefits to the rural economy and the poor.

2. Agribusiness growth will increase employment and income in rural areas; stimulate farm and nonfarm activities, such as agroprocessing, marketing, and business services; establish value chain links among farmers, traders, and agroprocessors; and add value to products. The project benefits will include (i) expanded employment and income in rural areas; (ii) increased private investment in the sector; (iii) improved status of the poor and women; (iv) improved policy and regulatory framework for agribusiness development; (v) strengthened agribusiness associations; and (vi) improved provision of agribusiness services in rural areas.

### B. Unmet Demand from Bankable Agribusiness Subprojects

3. Opportunities for agribusiness growth exist in Bangladesh, because of a comparative advantage in the production of a range of agricultural commodities and because of a growing demand for a variety of quality, convenient, and high-value products. *The National Private Sector Survey of Enterprises in Bangladesh*<sup>1</sup> found that Bangladesh's agribusiness sector is dominated by small-scale units in production, processing, and distribution. An estimated 2.6 million small-scale agribusinesses are scattered throughout Bangladesh—39% of which (or about 1 million enterprises) would like to get credit support and are confident about paying it back. Most of the credit demand from the small-scale enterprises is estimated to be for loans of \$500–\$5,000. If a small-scale agribusiness needs on average \$2,500 equivalent for investment and operations, the total unmet credit demand is far more than any single project can offer.

### C. Financial Projection and Absorptive Capacity of Participating NGOs and Wholesale Banks

4. The size of the Project's agribusiness credit line (\$36 million) is based on the financial projection and absorptive capacity analysis of the participating NGOs. The three NGOs have different sets of factors affecting their absorptive capacity for lending, as envisaged under the Project. Information is derived from the due diligence performed on each institution (Supplementary Appendixes C–G). Each NGO has stated an intention to become a licensed, deposit-taking microfinance institution (MFI) once enabling legislation is passed at the end of 2005. Each has at least 3 years experience in making agribusiness loans to individuals, with average loan sizes of \$1,000–\$1,500. The loan recovery rate of 99% is similar to their more traditional group-based lending. Agribusiness lending has been developed cautiously. The forecasted growth rate in lending has been scaled back to 85–90% of the rate over the last 3 years. For each NGO, proposed project financing will be less than 6% of its liabilities. The Project has at least as much to do with building institutional capacity in agribusiness lending as

<sup>1</sup> Daniels, Lisa. 2003. *National Private Sector Survey of Enterprises in Bangladesh*. Department for International Development, et al.

it does with financing. Table A13.1 summarizes the key financial indicators (current versus projected) of the financial institutions.

**Table A13.1: Financial Indicators of the Participating Financial Institutions**

Indicator	BASIC Bank	Eastern Bank	BRAC	ASA	TMSS
(31 December 2004)					
Capital adequacy ratio (%)	12.1	16.0	33.5	63.2	35.5
Loan deposit ratio	0.8	1.0	1.8	2.7	2.0
Expense/revenues (%)	70.0	62.0	86.0	38.0	62.0
Net worth (Tk million)	1,491.0	2,631.0	5,161.0	7,844.0	358.0
Net income (Tk million)	527.0	851.0	533.0	2,102.0	97.0
<b>Total assets (TK million)</b>	<b>19,437.0</b>	<b>23,048.0</b>	<b>17,118.0</b>	<b>15,902.0</b>	<b>1,312.0</b>
(Projected for 31 December 2010)					
Capital adequacy ratio (%)	12.3	14.2	34.9	65.6	39.0
Loan deposit ratio	0.8	0.9	2.39.0	3.4	2.3
Expense/revenues (%)	70.0	67.0	81.0	49.0	72.0
Net worth (Tk million)	4,085.0	9,039.0	12,175.0	20,985.0	1,035.0
Net income (Tk million)	1,460.0	2,697.0	1,625.0	3,677.0	156.0
<b>Total assets (TK million)</b>	<b>50,045.0</b>	<b>80,243.0</b>	<b>38,759.0</b>	<b>35,750.0</b>	<b>3,010.0</b>

ASA = Association for Social Advancement, BASIC = Bangladesh Small Industries and Commerce, Tk = taka, TMSS = Thengamara Mohila Sabuj Sangha.

Source: Asian Development Bank estimates.

5. **Association for Social Advancement (ASA).** In real terms, ASA's loan portfolio has grown 22% annually in the last 3 years, with much of this expansion being funded out of retained earnings. The projected rate of growth during project implementation has been scaled back to 17.5%. Individual and agribusiness lending is projected to grow at the same rate as other lending, remaining at 10% of the total loan portfolio. The projection indicates that, even with a reduction in the loan interest rate, much of ASA's future growth will continue to be funded out of retained earnings. Agribusiness lending is estimated to increase by Tk1,465 million by 2011, and half of this (Tk733 million) would be eligible for project financing. Project financing would represent 5.3% of ASA's liabilities. Agribusiness lending would be 4% of the loan portfolio. If agribusiness lending were to increase to 5%, project borrowing could increase to Tk880 million. In 2011, borrowing from all sources is estimated to be 11% of ASA's loan portfolio, compared with 27% in 2004. Debt financing is not seen as being a problem. Management and loan administration skills are highly capable, and governance is sound. ASA continues to be financially viable under a range of alternative scenarios. The capital adequacy ratio (CAR) is never less than 38%, and the return on equity is generally above 15%, even with a reduction in interest rate charged on lending.

6. **BRAC.** As envisaged, BRAC's loan portfolio will grow 15% annually during project implementation, which is not high by NGO standards. Agribusiness lending will increase from 12% of all lending to 15% by 2012. An estimated 20% of individual lending (Tk1,260 million–Tk1,340 million) will be project-relevant. This amount of financing would be less than 4.5% of total liabilities. In 2004, Tk6,240 million was disbursed in the *unnoti* ("economy") and *progoti* ("progress") programs, and loan recovery is highly satisfactory. Financial projections under a range of scenarios remain strong. CARs are always in excess of 30%, and the return on equity is more than a minimal 12%. The net profit of Tk533 million is expected to reach Tk1,866 million by 2011. Financial systems and their management and governance are sound. The major

concern is the ability of BRAC to find sources of borrowing needed to finance asset growth. Security is adequate: loan receivables are never less than 2.5 times borrowing. If Palli Karma-Sahayak Foundation (PKSF) does not increase its lending, BRAC will need to scale back its annual growth in group lending, reducing overall lending growth to about 12%. This would mean borrowing Tk1,260 million–Tk6,060 million from the Project through commercial banks. If BRAC became a deposit-taking MFI, its deposits would bridge much of the gap in financing, enabling annual 15% growth in lending to be financed.

7. **Thengamara Mohila Sabuj Sangha (TMSS).** The annual growth rate in TMSS lending is forecasted at 20% during project implementation. In 2004, agribusiness lending was 7% of its loan portfolio, and this is expected to grow to 21% by project completion. In 2012, half of the expected Tk660 million in agribusiness would be eligible for project financing, which would amount to 6.5% of total liabilities. In 2012, borrowing would total Tk1,394 million (an increase of Tk915 million from 2004), which is estimated at 42% of its loan portfolio, compared with 54% at present. TMSS is not part of the group of large NGOs, and it has reduced its interest rates. Thus, PKSF is expected to finance much of the increased group-based borrowing. Although the CAR remains above 35%, return on equity will decline from 29% to 15.7% in 2012. This is largely due to a graduated decrease in interest charged on lending. Overall financial performance remains sound. Net profit of Tk91 million will increase steadily to Tk207 million in 2012. Governance and internal controls, which are sound but cumbersome, will be tested as TMSS disentangles its microfinance operations from many social interventions. This is complicated by a need to improve information technology to reduce the reporting time, and to improve management access to information.

8. **BASIC Bank.** BASIC Bank was chosen as a wholesaler because it has (i) low administrative expenses on its lending; (ii) efficient and profitable financial intermediation; (iii) experience in working with aid agency-funded projects; and (iv) the confidence of, and lends to, NGOs. Financial projections show that BASIC Bank's strong financial indicators will continue. Anticipated project financing will represent 3% of its liabilities and the project NGO portfolio will be 3.4% of its lending. With six corporate borrowers with average loan sizes of more than \$5 million, BASIC Bank has experience in making large individual loans. All these loans are unclassified. However, the anticipated net worth of BASIC Bank to 2011 will limit loan exposure to a single NGO to around \$8 million–\$9 million, which is less than the amount BRAC is likely to request in a year.

9. **Eastern Bank.** Eastern Bank is a private commercial bank whose management team gained extensive experience from working with highly reputable foreign banks. The Board of Directors fully supports the team. Since 2001, Eastern Bank steadily has improved the quality of its loan portfolio and streamlined its operations. Administration expenses on earning assets are 1.7–2.1%, while the CAR is more than 16%. Anticipated project financing will represent 1.3% of total liabilities, 1.3% of Eastern Bank's total loan portfolio, and 1% of total assets. The net worth of Eastern Bank allows it to make loans to individual borrowers of up to \$6.3 million. By 2010, with the anticipated increase in net worth, this limit will cover individual NGO loans up to \$16 million.

## D. Project Impacts

### 1. Representative Enterprises Analysis

10. The Project is designed to stimulate commercial activities in the agriculture sector ranging from preproduction support through commercial production to postproduction handling,

processing, transport, storage, and marketing. Demand will drive the investments, which will be identified during implementation. As a result, the likely mix of the scale and types of interventions, and the project benefits, cannot be ascertained accurately. Thus, a full-scale cost-benefit analysis would be impractical. Instead, financial analyses were conducted on representative agribusinesses that the private sector could implement under the Project. NGO staff will be trained to appraise each subproject to ensure its viability and compliance with environmental and social safeguards of ADB and the Government.

11. As detailed in Supplementary Appendix K, the representative enterprise analysis is based on the enterprise budget model with breakdown on revenue and cost by the enterprise outputs and inputs, as well as projected cash inflows and outflows over 10 years priced at constant 2005 prices. The enterprise capacity is assumed to be realized by scaling up, with full capacity reached in the third year. The cost structure of an enterprise usually consists of fixed investment (machinery, building, and land where applicable) and operating costs (raw materials, labor, electricity, repair and maintenance, depreciation, loan repayment, transport, and miscellaneous expenses). Sensitivity analysis has been done to identify some of the major business factors, and to evaluate the impact changes in these factors would have on each enterprise. The analysis finds that agribusiness investment is profitable, sustainable, and generates substantial and permanent employment for the rural poor.

## **2. Economic Development Impacts**

12. The cumulative impact of the Project on the economy will be significant through direct increases in production, increases in value added, and employment generation. In addition to increases in gross domestic product, economic benefits will include an increase of around 70,000 new jobs (para. 13). Additional indirect economic benefits will accrue from (i) increased production generated by the availability of better support services; (ii) increased demand for agricultural produce for processing and urban sales, resulting in higher producer prices and greater quantities of produce marketed; and (iii) multiplier effect generated through greater demands for on-farm labor, transport, storage, and handling. Disadvantaged segments of the community will benefit from the increased labor demand and increased demand for farm produce. They also will benefit directly through the promotion of intensive agribusiness activities (e.g., dairy, poultry raising, and fish farming) that do not require significant land.

## **3. Employment Generation and Poverty Reduction Impacts**

13. The Project will assist the start-up or expansion of at least 28,000 small agribusinesses. This assumes that each credit package to the individual enterprise will be, on average, about Tk160,000, and that the credit will revolve at least once during the 5-year life of the Project. In addition to maintaining existing employees, each subloan will generate on average 2.5 new jobs. Thus, 70,000 new jobs (or 350,000 person-years) are expected to be generated from the Project. If credit is disbursed and recycled expeditiously, the employment generation could be much higher. The generated jobs will be primarily in rural areas where 53% of the population lives in poverty.

14. The entrepreneurs will review their costs and hire very poor people to lower their operating costs. More than 60% of labor requirements of the financed enterprises will be for manual and low-skilled workers who will be poor, according to estimates. Manual labor is needed for tasks such as carrying inputs and outputs, weeding, irrigating, and operating feed and oil mills. Necessary labor skills, apart from the skills of the entrepreneurs, will be learned on-the-job. These include working with dairy cows, producing milk by-products, working in

nurseries, and working in broiler houses. Though the wage rates paid for this type of labor are attractive only to the poor, the average wage paid is Tk115–Tk130 per working day, which is well above the average of Tk65 per day for casual labor.

15. Additional indirect poverty-reduction impacts will come from employment and higher incomes generated by demand for produce and services, such as transport, handling, and storage needed for the operation of the new enterprises. Since the demand will be mostly for semiskilled and unskilled labor, a high proportion of those employed certainly will be poor. The demand for raw materials also will generate some indirect impacts. This will stimulate production, thus generating additional employment and income-earning opportunities.

16. Beyond the provision of a daily wage, poverty-reduction impacts also will be generated. Full-time employment will provide the possibility of sustained economic and social betterment. Previously unskilled laborers will have the opportunity to learn skills and develop a craft, while semiskilled workers will be able to perfect the skills they already have. With regular incomes, both groups of workers will be in a better position to provide skills and an education to their children, helping their families out of poverty.

#### **4. Policy and Institutional Impacts**

17. The Project will have a significant impact on the policy environment by identifying and rectifying specific regulatory constraints that impede agribusiness. These will include (i) import and export regulations, (ii) market management, (iii) access to technology, (iv) information dissemination, and (v) other constraints identified by the agribusiness stakeholders.

18. The Project will have a strong positive effect on the institutional environment through measures including (i) institutional strengthening of NGOs in providing agribusiness credit; (ii) enhanced NGO technical training; and (iii) training for staff of the wholesale banks in agribusiness lending to NGOs. The Project will train the line agency staff in the importance of agribusiness, as well as their potential role in (i) encouraging commercial activities in the agriculture sector, (ii) strengthening agribusiness organizations, and (iii) enhancing the capacity of NGO staff and trainers in promoting agribusiness investments among small borrowers. The establishment of an agribusiness cell in the Ministry of Agriculture and the establishment of the project implementation unit in the Department of Agricultural Marketing (DAM) also will strengthen the institutional environment for agribusiness development by providing an institutional focal point for further investment and aid agency involvement in agribusiness expansion.

#### **5. Impacts on NGOs Scaling Up to Efficient MFIs and Rural Financing**

19. By providing credit and technical support to the project subborrowers, the participating NGOs will diversify and strengthen their loan portfolios based on a long-term and stable debt liability structure. The project targets are in line with the corporate goal of the participating NGOs—scaling up to become efficient MFIs.

20. The participating NGOs will be strengthened financially. Although they already have sound financial performance indicators, they have depended on aid agency and grant funding. Consequently, they have not developed the commercial links with the banking sector that are necessary for any viable enterprise or institution. Such links will expose them to rigorous financial and managerial reviews by bank lenders. Their dependence on aid agency funding, furthermore, makes them vulnerable to pressures to finance microenterprises at cheap and

unsustainable interest rates and/or to restrict their activities to segments of society or geographical areas targeted by government planners. Their participation in the Project will help these NGOs to improve their financial management, asset and liability structures, and profitability to ensure access to a broader and continuing range of sources of financing. This also will enable them to service debt, while maintaining sound debt-equity ratios. The provision of long-term debt will assist greatly these NGOs in their long-range planning and development of individual borrower loan products needed in the market. The strengthening of these NGOs will encourage the Government to proceed with its legislative program to support the emergence of sound and sustainable MFIs.

21. The Project is a pioneering effort to use the banking system to channel funds through reputable and experienced NGOs to small-scale agribusiness entrepreneurs, who traditionally have been unable to access finance for their ventures. The successful growth of agribusiness lending through experienced NGOs will demonstrate to policymakers that the key to expanding rural financial services is engaging capable institutions with the financial and managerial strengths to respond to the growing demands of the market. The Project will facilitate a new avenue for a vibrant, crucial, and important section of the country's private sector to access finance.

## **E. Project Sustainability**

22. **Institutional Sustainability.** Through its training components and strengthening of DAM, the Project will contribute to developing capacity within the public sector, the nonprofit private sector (through its support to NGOs), and the profit-based private sector (through agribusiness associations and wholesale banks) to serve and support agribusiness development. By the end of the Project, these public and private entities will be in a position to continue providing services to the commercial enterprises in the agriculture sector.

23. **Financial Sustainability.** The financial projections indicate that, throughout the Project, the NGOs and wholesale banks will be in compliance with prudential financial indicators established by Bangladesh Bank. The projected financial statements, with the financial management assessments, indicate that the financial institutions have sufficient financial and managerial capacity. The Project is considered financially viable and sustainable.

24. **Investment Sustainability.** Regarding the sustainability of credit-financed investments, the enterprises sponsored by the Project, as private sector ventures, will continue to operate on a self-sustaining and financing basis as long as they are profitable. Undoubtedly, some attrition will occur, but their success will not depend on support or inputs from the public sector. No special subsidies or preferential treatment will be involved. Thus, on the whole, the project investments will be sustainable as long as the enterprises are properly run in a favorable financial and regulatory environment.

## SUMMARY POVERTY REDUCTION AND SOCIAL STRATEGY

### A. Links to the Country Poverty Analysis

Is the sector identified as a national priority in country poverty analysis? Yes	Is the sector identified as a national priority in country poverty partnership agreement? Yes
<p><b>Contribution of the sector or subsector to poverty reduction in Bangladesh:</b></p> <p>Despite Bangladesh's considerable success in reducing poverty during the 1990s, around half of the population still lives in poverty. Poverty is mostly rural, with 85% of the poor population living in the countryside. In rural areas, 53% of people live in poverty, compared with 36% in urban areas. Further, poverty in rural areas is twice as severe as in urban areas. A majority of the rural population depend on agriculture, but the low base of agribusiness development remains a hurdle for growing the agriculture sector, as well as the national economy.</p> <p>Agriculture remains a fundamental sector of the economy, accounting for 22% of the gross domestic product (GDP) in 2002 and more than 50% of the national workforce. When forward and backward links are taken into account, the contribution of agriculture and agribusiness to GDP is estimated at about 35%, while the contribution to employment exceeds 75%. Of the estimated 3 million agribusinesses in the country, 90% have less than 10 workers and 36% have only one worker. Nonetheless, they are estimated to account for half of household income for about 15 million people.</p> <p>The draft poverty reduction strategy paper (PRSP) recognizes that the Government's priorities for rapid poverty reduction are to (i) develop the private sector; (ii) facilitate the development of women entrepreneurship; and (iii) promote employment of, and benefits to, the poor. The PRSP emphasizes the enhancement of agriculture and the rural nonfarm sector with backward and forward links for accelerating rural nonfarm growth. An integrated approach with expansion of the technology base, agroprocessing, marketing, infrastructure, information, human development, etc. has been considered. The PRSP points out the importance of (i) correcting policy distortions that hurt rural nonfarm activities, (ii) creating an enabling environment, (iii) opening up opportunities, (iv) reducing risks, and (v) expanding credit flow to rural entrepreneurs. Essentially, these are key elements for agribusiness development. Agribusiness development can contribute substantially to reducing rural and urban poverty by facilitating the creation of employment and income-generating opportunities within the agribusiness value chain, thereby contributing to the economic growth.</p> <p>The Agribusiness Development Project (the Project) is to expand rural and peri-urban employment opportunities for adults, increase the value added of nontraditional crops and commodities, raise rural incomes, reduce the incidences of child labor and worst form of child labor in existing economic activities, and reduce poverty by expanding the activities of rural enterprises engaged in commercial agriculture (and its backwards and forwards links). The Project aims to (i) promote small-scale agribusiness activities by channeling credit and providing technical supports to small-scale agribusinesses in rural areas of the country through reputable, experienced nongovernment organizations (NGOs); (ii) strengthen agribusiness associations for policy dialogue on the enabling environment, agribusiness promotion, and information dissemination; and (iii) improve the enabling environment for private sector entrepreneurs through legislative and regulatory changes, and reorientation training for the staff of public sector agencies.</p> <p>The Project focuses on grassroots, rural-based entrepreneurs in the private sector. This is a key group with substantial economic growth potential, which multilaterally financed projects in Bangladesh have neglected. Agribusiness investments undertaken by these small-scale agribusinesses are expected to generate directly substantial employment opportunities, while increasing the demand for agricultural products. In turn, this will translate into demand for a broader range of produce, higher prices, additional employment, and increased rural incomes. Agribusiness development in general also will support income generation of poor farmers engaged in agribusiness through improved organization of market links, supply contract, adoption of appropriate pre- and post-harvest agricultural technology, and availability of financing and services of facilitating agencies.</p>	

### B. Poverty Analysis

### Targeting Classification: General intervention

#### What type of poverty analysis is needed?

In rural Bangladesh, household poverty is associated mainly with small farms (or landlessness) and unstable (or casual) employment. Scarce access to productive assets, especially land, and loss due to natural calamities are key determinants of household poverty. Poor households typically own less land than the non-poor, and are highly represented among the functionally landless. The incidence of poverty among landless and households with less than 0.05 acres is 67%. This rate decreases as land size increases. The scope for redistributing land to the poor, or bringing more land under cultivation, is limited. Thus, measures aimed at improving land productivity and at promoting nonfarm activities are considered the most feasible options for development.

High incidence of casual wage labor, instead of permanent labor, is a severe burden for rural households. In rural areas, the incidence of poverty in households where the head is a casual laborer is 75% (compared with an average in rural areas of 53%). About half of the poor in rural areas lives in households where the main occupation of the head is casual wage employment. The heads of one quarter of the poor rural households are self-employed in agriculture. However, poverty is relatively less among salaried employees—approximately 6% of the rural poor, with an incidence in the category of 35%. Women are effectively the head of about 25% of the households, and among the poorest. Many poor migrate to urban areas in search of employment due to unemployment and loss of productive assets. Still, the agriculture sector provides employment for the majority of rural people, mainly due to the low employment opportunities in, and low absorptive capacities of, the other sectors.

While a significant number of participants in different subsectors of agriculture are women, their participation in the labor force is low as they are mainly involved in household-based or subsistence activities. Therefore, their income is low and contribution to GDP is not recognized. A considerable gap with men remains in literacy, access to health care, and nutrition. A preliminary analysis during the project preparatory technical assistance found that women's participation in agribusiness is low and wage discrimination exists. The Project will be a remarkable opportunity to reduce the burden of poverty on women in Bangladesh. The potential for women laborers and entrepreneurs to contribute to, and benefit from, more commercial-oriented agribusiness activities is huge.

The Project will address poverty by (i) focusing on rural areas and small-scale agribusinesses; (ii) prioritizing employment creation in farm and nonfarm sectors; (iii) promoting market links, which will increase profitability for smallholder farmers; (iv) emphasizing partnership and supply contracts among NGOs and private sectors, which have positive impacts on women and poor participation; and (vi) involving marginal areas during the dissemination campaign of project activities.

Following on these considerations, special emphasis has been given to include direct and indirect beneficiaries in the analysis of project impact on poverty reduction. While the poor might benefit directly from the Project when involved in project activities, they also can benefit indirectly as employees of beneficiary enterprises, as clients in the value chain, or as suppliers of agricultural goods and services. Besides, they can benefit from employment opportunities generated in supportive manufacturing and servicing enterprise growth. For an ongoing analysis of the poverty reduction impact, the Project will utilize (i) baseline household and community surveys; (ii) records of NGOs and financial intermediaries; and (iii) participatory techniques with a special focus on poor farmers, enterprise employees, women, children, and ethnic groups, to gather data and information on needs, assets, entrepreneurship potential, and vulnerability.

### C. Participation Process

Is there a stakeholder analysis? ☒ Yes ☐ No

Is there a participation strategy? ☒ Yes ☐ No

A participatory process was adopted during project design for understanding the needs and the constraints of the poor population, women, and ethnic minorities regarding agribusiness development. This consisted of an extensive participatory rural appraisal (PRA), which was conducted in 17 districts of the country. The PRA involved farmers, factory workers, and daily laborers. The PRA was complemented by informant interviews, which included managers of factories, entrepreneurs, NGO officials, and representatives of chambers and associations.

The project implementation also will adopt a participatory approach. In particular, NGOs are expected to play a crucial role in managing the credit component for the entrepreneurs, and providing and/or facilitating other services. Agribusiness promotional activities and capacity-building activities will be supported upon submission of proposals from associations, NGOs, and facilitating agencies. In particular, to increase the exposure of the poor and vulnerable groups (such as women, tribal communities, and remote area farmers) to the benefits of the Project, special care will be given to enhance their participation through intense dissemination activities and focused awareness campaign. For this purpose, the Project will develop the capacity of associations, and assist in establishing links within private sector.

The awareness building campaigns will involve, among others, issues of child labor and worst form of child labor (impacts and extent). The capacity initiatives will involve establishment of child-friendly environment in the private sector. Measures will be undertaken to withdraw children from the worst form of child labor, and provide alternatives to them (in education, training, and skills development) and their parents (in employment, access to credit, market, and services) for enhanced income to support their family.

### D. Gender

#### Strategy to maximize impacts on women:

Women are likely to benefit from the Project through increases in (i) new employment possibilities at the household level in agroprocessing and post-harvest tasks; (ii) profitability through scaling up of enterprises; (iii) access to financial

resources; (iv) income at household and/or enterprise level; (v) improved human capital and skills through training and capacity building activities; and (vi) availability and quality of agricultural goods.

The combination of these effects could increase significantly the overall status of women in the household and in society. However, various constraints might prevent or reduce benefits to women. By considering women's potential involvement in employment opportunities, attention needs to be given to (i) social and cultural constraints that limit women's participation in the labor force and/or business, (ii) economic constraints that make women work inside the household for children care and housekeeping, and (iii) facility constraints, which prevent women from accessing appropriate facilities in work or the market place. The project design encompasses several general strategies: (i) development of backward and forward commercial links that are positively associated with the participation of women; (ii) collaboration with women entrepreneurs and women's associations; (iii) implementation of an awareness campaign for promoting project activities among women borrowers and entrepreneurs; and (iv) capacity building for institutions, NGOs, associations, groups, financial institutions, and women to facilitate women's access and participation in agribusiness and agroprocessing. Special emphasis will be given to girls to ensure that they are exempted from child labor and worst form of child labor, and have greater access to education, health, and other social services.

**Has an output been prepared?**

A gender action plan has been prepared in Appendix 15.

**E. Social Safeguards and Other Social Risks**

Item	Significant/ Not Significant/ None	Strategy to Address Issues	Plan Required
<b>Resettlement</b>	None	Not applicable.	No
<b>Affordability</b>	Not Significant	The Project will strengthen backward and forward links with producers, NGOs, and private sector service providers and/or entrepreneurs. This will increase the availability of goods and services. The improvement in the quality of the final product might be reflected in an increase in its price. This effect does not raise affordability concerns since (i) the improvement in the quality is accompanied by an increase in the supply of the goods, and (ii) the higher-quality goods are oriented towards non-poor consumers. It also facilitates increased income of the poor through the support for scaling up their enterprises.	No
<b>Labor</b>	Not Significant	The Project will increase employment opportunities in agribusiness for men and women. No negative impact on labor market is foreseen. At the same time, the prospects of economic growth and profitability might push farmers to involve child labor in the activities. The Project will ensure close monitoring of the conditions and activities of children in beneficiaries' households, and mobilize the necessary resources to prevent child labor and worst form of child labor. Also, the diffusion of "fair trade" principles and permanent jobs created for parents will decrease the incentives to utilize child labor.	No
<b>Indigenous Peoples</b>	None	The Project will not have any negative impact on indigenous people. The adoption of a demand-driven approach for funding of interventions should allow participation of indigenous people.	No
<b>Other Risks and/or Vulnerabilities</b>	Not Significant	Risks include political instability, weak commitment to understanding agribusiness development, and inadequate institutional coordination. The capacity to improve agribusiness development also is influenced by exposure to natural disasters, such as flooding and droughts. The project focus on NGO-operated credit should decrease the risk of difficulties in repayment capacity. Also, the Project will strengthen the coordination among stakeholders. This might be a useful strategy for coping with difficulties associated with the negative effects of natural disasters, such as floods and droughts.	No

## GENDER ACTION PLAN

1. Women's effective participation in the Agribusiness Development Project (the Project) is expected to contribute to poverty reduction and social development. This Gender Action Plan (GAP) factors gender concerns into all project components to promote women's participation equally as agents and beneficiaries in the Project's development process.

2. A significant share of the participants in different subsectors of agriculture is women, though women's contributions often go unrecognized. The GAP aims to (i) reduce poverty among women, (ii) increase women's participation as stakeholders in agribusiness development, (iii) increase women's economic and social benefits from the Project, (iv) develop women as contributors to the country's economic growth, and (v) support women's empowerment in decision-making and public life.

3. The Project will (i) support women's access to newer employment opportunities in upstream and downstream agribusiness enterprises and services; (ii) increase profitability prospects for agro-entrepreneurs; (iii) increase household income; (iv) improve human capital; (v) improve links with service institutions; and (vi) increase access to market, finance, and other resources. A summary of the planned activities is in Table A15.1.

**Table A15.1: Activities for Women's Participation**

Component	Activity and Target
<b>1. Credit for Small-Scale Agribusinesses</b>	<ul style="list-style-type: none"> <li>• Effective mechanism will be developed to ensure women's increased access to the agribusiness credit, so that 30% of the subborrowers are women by 2010.</li> <li>• A minimum of 10% of the revolving fund will be earmarked for lending to women entrepreneurs. If such earmarked funds are not utilized within 2.5 years from the start of project implementation, they will revert to the general pool of funds.</li> <li>• NGOs will support a substantial number of women former microcredit borrowers under the credit program for agribusiness. Agribusiness development ventures that will create employment opportunities (at least two) for the poor and women will be supported.</li> <li>• NGOs will support the preparation and revision of the business plan of former microfinance borrowers to scale up their activities as subborrowers of the targeted credit program.</li> </ul>
<b>2. Technical and Marketing Support for Agribusinesses</b>	<ul style="list-style-type: none"> <li>• Raise awareness among potential entrepreneurs through periodic information campaigns to inform them of the business services and credit line opportunities, as well as agribusiness technologies.</li> <li>• Ensure that all the campaign messages are gender friendly, and a gender friendly dissemination methodology is used to reach women and men.</li> <li>• Organize periodic campaigns and information dissemination activities with appropriate messages to reach the associations and NGOs about the scope in agribusiness promotional activities.</li> <li>• NGOs will provide training and guidance to subborrowers on business planning, preparation of project proposal, financial control and reporting, business and credit management, etc., for all women borrowers, as they require.</li> <li>• NGOs will provide technical training to all women subborrowers on livestock, fisheries, agronomy, storage, processing etc., as they require. The training also will include orientation on formalities, opportunities, taxes and tariffs, etc.</li> <li>• NGOs will provide services to integrate the enterprises owned by women with downstream agribusiness activities provided by NGOs and the private sector.</li> </ul>

Component	Activity and Target
	<ul style="list-style-type: none"> <li>• The project implementation unit (PIU) will identify agribusiness opportunities through a subsector study.</li> <li>• Support women entrepreneurs to establish links with market and financial institutions.</li> <li>• NGOs will assist with forming producer groups and associations, including those for women entrepreneurs, to ensure efficiency and support through training, study tours, etc.</li> <li>• Identify the capacity building needs of private sector and potential associations to link with women entrepreneurs.</li> <li>• Help in developing the capacity of the private sector chambers and associations on a demand basis to support agribusiness development, particularly to promote women's participation in agribusiness. The support will include training, workshops, domestic study tours, etc., on a cost-sharing basis.</li> <li>• A special support package will be designed for women private sector associations and/or chambers to improve their capacity to identify and invest in agribusinesses and link with agribusiness entrepreneurs.</li> <li>• Support women entrepreneurs and associations for publicity drives to disseminate information for agribusiness promotion on a cost-sharing basis.</li> <li>• Support organizing publicity drive including seminars, trade fairs on the opportunities of agribusiness development, which will focus on the opportunities for women. Women entrepreneurs, chambers, and/or associations will be targeted for information dissemination and participation in those activities through campaigns.</li> <li>• Women's access in publicity drives, trade fairs seminars, and other awareness raising and technical assistance activities will be supported through information dissemination and special provisions.</li> <li>• Larger or medium-size entities that are willing to enter into supply contracts with the women agribusiness entrepreneurs will be identified and linked.</li> </ul>
<b>3. Strengthening Capacity of NGOs and Wholesale Banks in Agribusiness Lending</b>	<ul style="list-style-type: none"> <li>• Support wholesale banks promoting agribusiness lending and participating NGOs promoting women entrepreneurs.</li> <li>• Train wholesale bank and NGO staff in agribusiness promotion with emphasis on tapping women's potential and addressing gender-based needs.</li> <li>• Train the staff of the financial intermediaries to develop the capacity to provide financial services and other support, and to monitor in a gender sensitive manner.</li> <li>• NGOs with expertise in women entrepreneurship and/or agribusiness development will be considered when selecting new implementing partners.</li> <li>• Participating NGOs and wholesale banks will be oriented to install a monitoring and reporting system with gender-based indicators, outputs, and results.</li> </ul>
<b>4. Improving the Enabling Environment for Agribusiness</b>	<ul style="list-style-type: none"> <li>• Provide technical expertise to identify regulatory impediments to private sector operations in agribusiness with analysis of impediments of women's participation.</li> <li>• Redraft key regulations and documents with provisions to facilitate women's participation in the sector in a participatory and transparent manner.</li> <li>• Assess current situation of public market management and impediments to women's access to market, and suggest mitigation measures.</li> <li>• Ensure participation of women, farmer groups, associations, chambers, and existing and potential entrepreneurs in relevant seminars and consultations.</li> <li>• Strengthen the capacity of DAM, MOA, and MOFL in agribusiness governance, adjusting their roles as facilitators in linking primary producers with the market.</li> <li>• Train the staff of these agencies to deal with NGOs and private sector, as well as addressing gender issues in agribusiness development.</li> </ul>

<b>5. Project Implementation Support</b>	<ul style="list-style-type: none"> <li>• Ensure that at least 30% of the project staff and consultants are women.</li> <li>• Ensure recruitment of women as extension agents of the NGOs.</li> <li>• Engage a gender advisor and a women's entrepreneur promotion specialist.</li> <li>• Orient all stakeholders, including the agribusiness cell, PIU, DAM, wholesale banks, and NGO staff on the GAP.</li> <li>• Ensure a congenial work environment for men and women.</li> <li>• Build training capacity under the Project by developing a group of trainers within DAM and participating NGOs.</li> <li>• Train DAM staff to deliver services for agribusiness development and implement the GAP.</li> <li>• Ensure GAP orientation for relevant MOA and MOFL staff.</li> <li>• Orient NGO staff on the GAP, related gender issues in agribusiness, and their roles in promoting gender equality. These institutions will be oriented to develop mechanisms within business plans to support women entrepreneurs in agribusiness by addressing their credit needs.</li> <li>• Orient relevant chamber members and/or staff on GAP issues and on their roles in promoting gender equality.</li> <li>• Ensure that all training is gender sensitive.</li> <li>• Orient project staff and consultants about the GAP and their own roles, as envisaged in the GAP.</li> <li>• Involve women in motivational activities for agribusiness development.</li> <li>• Develop the capacity of the executing and implementing agencies on gender-based monitoring.</li> <li>• Ensure collection of gender-desegregated data, as well as gender-based monitoring, evaluation, and reporting within the Project's monitoring systems.</li> </ul>
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DAM = Department of Agricultural Marketing, GAP = gender action plan, MOA = Ministry of Agriculture, MOFL = Ministry of Fisheries and Livestock, NGO = nongovernment organization, PIU = project implementation unit.

Source: Asian Development Bank estimates.

## INTEREST RATE STRUCTURES AND PRICING

### A. Nongovernment Organization Interest Rates on Subborrowers

1. **Introduction.** The Project's lending and onlending rates have been discussed in Appendix 7. Nongovernment organizations (NGOs) will charge interest rates that allow full cost recovery on loans to the subborrowers, which are small-scale agribusiness entrepreneurs. The practice is consistent with the Asian Development Bank (ADB) *Microfinance Development Strategy*,<sup>1</sup> and takes into consideration key lessons learned from ADB and other aid agency projects on micro and rural finance in Bangladesh and other countries:

- (i) The credit line should provide flexibility to participating banks and NGOs in setting their interest rates to reflect credit risks of the respective clients.<sup>2</sup>
- (ii) Interest rate and financial viability go hand to hand. Capping interest rates would constrain the growth in microfinance aimed at poverty reduction. Market competition should determine the interest rate, not the Government.<sup>3</sup>

2. **Sustainability of NGO Enterprise Lending.** Sustainability is the key factor that ADB and the Government should consider in recommending what interest rates NGOs should charge. For the Project, NGOs are recommended to continue determining their loan pricing according to market conditions and services being provided for cost recovery. This is to reduce the risk of political intrusion and to avoid market distortions. With a market focus, financial services and institutional relationships can be expected to sustain and expand after the Project. The financial projections for the participating NGOs show that, with the proposed full cost-recovery rates, they are able to maintain their financial integrity while increasing market outreach.

3. **NGO Cost Structure.** NGO lending usually carries a higher rate than bank lending, because of NGOs' higher delivery costs involved in smaller transactions delivered virtually to the subborrowers location. Interest rates need to cover three basic types of costs: (i) cost of funds for onlending; (ii) cost of risk (loan loss); and (iii) administrative costs (identifying and screening clients, processing loan applications, disbursing loans, collecting repayments, and following up on non-repayment). Administration costs are inversely related to loan size, and usually exceed 10% of the amount of loan for small loans. Furthermore, service pricing for different NGOs needs to consider NGO product differentiation. Distinction needs to be made between NGOs that charge weekly or monthly, those that provide grace periods for principal, and those that provide interest rebates to proven borrowers. Several other factors also affect the pricing of NGO credit in Bangladesh: (i) natural disasters, (ii) uncertainty over the future sources of finance for asset expansion, (iii) higher cost of equity financing, (iv) widespread practice of cross-subsidization between loan products, (v) inclusion of social and technical support costs, and (vi) effect of taxation liabilities on NGOs becoming microfinance institutions.

4. **Repayment Capabilities of Subborrowers.** The direct subborrowers of the Project will be the small entrepreneurs, while ultra-poor people will benefit from the jobs created. By moving into the market for small-scale enterprises, the NGOs have seen significant potential in the market if service can be provided efficiently at reasonable prices. The many borrowers (more than 160,000) of NGOs' small enterprise program, annual lending growth of more than 20%, and the high repayment rate of at least 99% clearly show the demand for these loans and ability of the small entrepreneurs for loan repayment out of enterprise profits.

<sup>1</sup> ADB. 2000. *Finance for the Poor—Microfinance Development Strategy*. Manila.

<sup>2</sup> ADB. 2003. *Project Performance Audit Report on Second Aquaculture Development Project in Bangladesh*. Manila.

<sup>3</sup> Local Consultative Group (LCG). 2005. *LCG comments on the Draft Poverty Reduction Strategy Paper*. Dhaka.

5. **Problems with Interest Rate Ceilings.** A review of microfinance in different countries, including Bangladesh, shows that the poor generally consider ongoing access to credit more important than the cost of the credit. An interest rate ceiling often hurts, rather than protects, the most vulnerable by shrinking poor people's access to financial services. An interest rate cap introduces market distortions, damages the sustainability of NGO lending, ignores fundamental pricing calculations, and ignores NGO product differences. As a demonstration, the capping of interest rates on agricultural lending through development finance institutions (such as Bangladesh Krishi Bank and Rajshahi Krishi Unnayan Bank) and nationalized commercial banks has weakened these financial institutions to the point of insolvency. It also has diminished severely their impact on, and capacity for, rural financial intermediation.

6. **Competition as the Mechanism for Lowering Interest Rates.** Competition will be the most powerful mechanism for lowering credit cost and interest rates. Under the Project, the increased supply of individual loans will increase competition between participating NGOs and banks that downscale services. This will lead to more attractive pricing of small loans, as well as a broader range of products and terms, to the benefit of users. Competition among NGOs, and from banks that scale down their operations, will lower interest rates. In principle, price adjustments should not be enforced externally, especially since this market segment of NGO lending (of \$500–\$5,000 loans) for agribusiness is relatively new.

## **B. Wholesale Banks and Their Margins**

7. The use of sound commercial banks as wholesalers of project funds provides an alternative and sustainable source of funds for larger NGOs. Wholesale banks, such as Bangladesh Small Industries and Commerce (BASIC) Bank and Eastern Bank, are needed because NGOs in Bangladesh are not registered financial institutions and cannot source funds directly from the Ministry of Finance or Bangladesh Bank. Most NGO borrowing in Bangladesh has been from Palli Karma-Sahayak Foundation (PKSF).<sup>4</sup> Such dependency on a single source of finance leads to loss of autonomy in management, as well as in the design and pricing of services. This has occurred in many medium and small NGOs.

8. The proposed margin of 3.5% for BASIC Bank and Eastern Bank is to cover administration expenses, income tax liabilities, and credit risk. The average cost of administration on earning assets for these wholesale banks is 2.0%, which is lower than at private commercial banks (about 3%). The loan-loss provisioning of the wholesale banks is 1.5%. Furthermore, participating in such a long-term project increases the political risk threshold far more than with short-term lending. This must be taken into account, along with risk from natural disasters and NGO institutional risk. Thus, the proposed margin of 3.5% is considered the minimum acceptable figure for Bangladeshi conditions.

9. The proposed margin for the wholesale banks is consistent with other wholesaler rates. A review of margins charged by intermediaries wholesaling or retailing funds to NGOs shows a common margin of not less than 3.5%. In 2004, PKSF had an administration cost of 1.21% and a remaining margin of 2.29% to cover loan loss and profit margin for a total of 3.5%. Citigroup is charging BRAC a margin of 1.5% (above the treasury bill rate), plus 2.0% credit risk guarantee to be paid to Financierings-Maatschappij voor Ontwikkelingslanden, a Dutch development financing agency, for a total of 3.5%. In its lending to NGOs in Central Asia, European Bank for Reconstruction and Development is charging 6-month London interbank offered rate (now 3.65%) plus a margin of 5.25% and a first time fee of 1%. This is an effective margin of not less than 5.5%.

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<sup>4</sup> As discussed in para. 14 of the main text, limited funds are available in the market that NGOs can mobilize to support agribusiness.