

Supplementary Document 19: Lessons and Synergies

LESSONS AND SYNERGIES

1. The proposed additional financing project was designed, based on work completed under the ADB-financed Innovations for Agriculture Modernization Technical Assistance for the Republic of Uzbekistan (TA 8567-UZB) which was implemented during 2014 and 2015 and the preliminary implementation results of the ongoing Horticulture Value Chain Development Project (Loan 3471-UZB approved on 26 November 2016). The proposed project takes into account the information and recommendations of these previous activities, coupled with the lessons learnt from ADB's country and sector assistance program. The proposed project is also in full alignment with the Government of Uzbekistan's own development strategy which is found in the Welfare Improvement Strategy which focuses on greater rural productivity, increased employment in rural areas and more income generating activity, including key measures; i) further structural reforms to agriculture and the diversification of agricultural production; (ii) mechanization of the sector, infrastructure build-up, and agribusiness development; (iii) more productive use of land and water; and (iv) greater financial stability of farm entities and more market-oriented agricultural policies.

2. ADB's current Country Operations Business Plan identifies agricultural productivity as a main development outcome, and rural enterprise development as a key area of assistance. The ADB Country Partnership Strategy (CPS) supports Uzbekistan's transformation into a modern industrial and service economy through sustained and inclusive growth, a reduction in poverty, and expanded regional cooperation. Strategic assistance to be provided under the CPS will catalyze industrial development, accelerate economic diversification, promote private sector development, ensure climate-resilient investment, and create new jobs for women and men.

3. The proposed project has incorporated the findings and recommendations of the previous phase of the ADB-financed Innovations for Agriculture Modernization Technical Assistance (TA 8567-UZB) and other related projects/programs, as well as previous ADB knowledge and experience for both the agriculture and finance sectors in Uzbekistan, including previous sector assistance and any subsequent evaluations.¹ Key lessons learnt include: (i) the need for diversification away from continual cotton / wheat crop rotations; (ii) the need for investment into modern systems of production, (iii) importance of preparing designs based on an analysis of agricultural demand and socio-economic needs; (iii) the need to also address the whole value chain to ensure sufficiency of logistical capacity; (iv) the importance of appropriately designed credit programs that are relevant to size and scope of likely sub-borrower demand; (v) the importance of a demand driven approach to credit, including a timely decision making process; (vi) the need for support for the PFI's so that they are better able to technically assess loan applications; (vii) that small businesses are the critical drivers for inclusive growth and job creation, and (viii) an understanding that sub-borrowers need access to appropriate high quality equipment that is relevant to their situation, regardless of its source, rather than a one option must fit all approach.

4. The proposed project design has integrated critical lessons learned from past and ongoing initiatives in the agriculture and rural development sector, along with relevant finance and credit projects (especially the ADB Small Business Finance Project – SBFP UZB-42007) to ensure the best fit and approach for sectoral and cross-sectoral investment efficiency and synergies with the aim to boost developmental impact and sustainability.

¹ ADB Land Improvement Project (LIP) - TA 4820-UZB: Implementation and Monitoring of Policy Reforms in Agriculture Sector.

5. The proposed project is similar in concept to the World Bank Horticulture Development Project (P133703) which was approved in June 2014 and been effective since 5 October 2015, but only operates in certain areas of Uzbekistan and has limitations on the amount of credit that can be taken which could be a constraint in the development of an efficient modern agricultural processing or storage facility.

A. The World Bank-financed Horticulture Development Project (P133703)

6. Along with a number of other donors, including ADB, the World Bank has been attempting to open dialogue with the Government of Uzbekistan on a diversified program of support for a broader section of the agriculture production sector, outside of the main cotton and wheat production systems for a number of years and for wide ranging technical, environmental and social reasons, The Horticulture Development Project (HDP) is the first significant project that has actually made it past concept stage and into implementation. Since project concept in 2013, following a previous horticulture sector assessment, it has taken over two years to become actually effective.

7. The World Bank HDP was approved in June 2014 and was made effective only in October 2015. Planned closing date is June 2021. The project development objective is to enhance the productivity and profitability of the horticulture sector in the project area. The project has three components: (i) Agricultural Support Services (\$35.21 million), (ii) Access to Credit (\$139.81 million), and (iii) Project Management (\$8.11 million). The project executing agency is the Rural Restructuring Agency (RRA).

8. Primary project beneficiaries comprise of farmers, farmer groups, private enterprises, agro-firms, and agro-processing enterprises, involved in the country's horticultural sub-sector. The project will focus on small dehkan farms with up to 5 ha of household plots per farm, and private farms with land size not less than 5 ha per horticultural farm. Secondary beneficiaries anticipated to benefit include: PFIs through improved skills and acquisition of a more diverse menu of suitably adapted financial products; and the national network of private growers through training and technical assistance. In the public sector, the project will support institutional strengthening of the State Research Institutes and the plant protection services.

9. The credit component has a focus on: (i) provision through selected PFIs of Investment and Working Capital Sub-Loans and Lease Financings to Beneficiaries; and (ii) provision of technical assistance and Training to PFIs to increase their capacity in managing a range of innovatively structured finance products that support, inter alia, the development of value chains. In particular, this subcomponent aims to enhance access to financial services for farmers and agribusinesses operating in Uzbekistan's horticulture sector, to enable them to undertake the investments to strengthen their productivity and competitiveness. The maximum loan/lease size will be up to \$2.0 million.

10. Since loan effectiveness in October 2015 the project has been actively supporting PFI's and disbursing funds as agreed. Lessons learned from this initial phase of the Horticulture Development Project are provided below.

11. Demand for credit within the horticulture sector is large:

- (i) With Government support for agriculture always focussed on cotton and wheat production through the state order system, horticulture development has remained the domain of the small producer with no support from the government.

- (ii) The World Bank estimates that the investment needs in the horticulture sector is more than \$1 billion during 2018-2022. The financing need for planting of new orchards and vineyards and replacement of some old ones alone is estimated to be in the order of about \$600 million.
 - (iii) Current cold storage capacity is extremely limited—only around 3% of current production levels could be accommodated
 - (iv) Investment into modern intensive production systems—fruit trees or greenhouses in particular require high levels of investment and attention to detail which is in direct contrast to both standard cotton and wheat production.
12. Credit should be demand driven, rather than part of a directed government program:
- (i) Government, through the RRA will try and limit the availability of credit to only pre-approved loan applications that match the perceived needs of the sector. This is not only operating with a very narrow perspective it is usually not a true reflection of sector needs.
 - (ii) Will limit innovation and adoption of new ideas and novel approaches.
 - (iii) Stifles competition and does not develop a broad-based production sector.
 - (iv) In trying to pre-approve subprojects, there is a likelihood of proposals having unrealistic cost structures and business models increasing the risk of loan default and thereby risk for the PFI.
13. PFI's need increased technical capability and support (horticulture-focused):
- (i) Assessment of the current management capability and lending portfolios of all PFI's indicate limited knowledge and understanding of the agriculture sector which has very specific and unusual characteristics that have a big significance on any business model.
 - (ii) PFI's with agricultural credit officers are usually focussed on broad agriculture (cotton and wheat) or large-scale agriculture equipment – wheat or cotton harvesters, large tractors or cultivators, etc.
14. Loan approval process needs to be streamlined and maintained within a reasonable timeframe:
- (i) One significant issue identified by all of the PFI's evaluated as part of the project planning process was the time taken between the application being made by the proposed sub-borrower and eventual loan approval. The World Bank HDP appears to have a number of approval processes after the PFI has carried out the due diligence and approved the loan application. This can delay full approval for some time.
 - (ii) With seasonality of production and narrow windows for implementation of key activities in the horticulture sector, delays in decision making can be the difference between investment now for this season or having to wait for 11 months to get the timing correct.
 - (iii) Most of the delays are because of lack of depth in technical knowledge at the PFI and subsequent lack of confidence in the process by the implementing agency. This should be overcome by setting a proper timetable for approval and then developing the technical capacity at the PFI level (long term sustainability) rather than adding extra checks (and delays) at another later level.

- (iv) ADB preferred approach leaves decision making to PFIs with monitoring of compliance only for RRA.
15. Significant need for development of logistical capacity to facilitate production and export chain;
- (i) The World Bank HDP has significant development in the production level, with investment at farm level into improved intensive production to supply better quality products for potential export markets.
 - (ii) The bottleneck is now in the post-harvest part of the value chain where limitations in availability of cold storage, packing and grading facilities and processing are very obvious and limiting options for producers to gain from extended marketing seasons and for processors to be able to buy in and store raw materials when prices are lowest and supply plentiful so that the processing equipment has the longest operational period.
 - (iii) The proposed project will offer support through loans that are of a more appropriate size (up to \$5 million, which is more in line with realistic price expectations for an efficient modern processing line).
 - (iv) The process of exportation remains over complicated and in need of streamlining, including development of special export processing zones or centers where all necessary facilities for export can be located in one place. The government needs to facilitate this process and ADB and the World Bank (among others) to assist in development of capacity and through provision of training and development for key staff. This is intended to be addressed by ADB through follow on Technical Assistance activities which need to be deployed within a short time frame.
16. Business models show high returns, but risks are also high:
- (i) The economic models developed as part of the planning process for this project indicate that in the main, the horticulture sector is capable of developing investment projects that are capable of providing a high level of return and therefore a high likelihood of credit repayment.
 - (ii) Investment into projects such as intensive fruit trees needs careful planning and a credit facility that is flexible enough to withstand (a) the seasonality of production, (b) the inclement weather factor (late frosts can destroy the crop for a whole season) and, (c) the need for delayed repayment schedules so that young trees can mature and become fully fruiting before the need for loan repayments.
 - (iii) Numbers of loans to entrepreneurs for investment into intensive production have proven to be less than successful because of the general lack of technical skills and management knowledge among managers and technicians employed to implement the activities using the modern equipment, varieties or techniques. All models need to identify such risks in the planning process and address them as part of the loan application, either by setting aside specific funds for training of staff or for the hiring of advisers who can impart the knowledge on site through regular visits and management support, thereby developing local capacity.
17. There is a need for identification of alternate markets for export production:
- (i) Discussion with the government and most local producers focus on a very narrow window of opportunity for export development – which has occurred in Russia following the ban on imports from Europe and also more recently Turkey. While

this is an opportunity, it is also a risk in that during this project planning process the rapprochement between Russia and Turkey has already begun and a number of other countries are also eagerly preparing their production facilities to supply more fresh products to the Russian market – Egypt, Lebanon, Moldova, Cyprus, Morocco and Azerbaijan are all planning such interventions.

- (ii) Rapid introduction of quality systems – such as GlobalGap or HACCP systems by the World Bank HDP a part of the capacity development should assist in addressing some of the quality needs associated with getting products into more advanced markets such as the EU, Korea, or Japan.

18. The above-mentioned lessons learned have been incorporated into project design and planning for implementation.

B. ADB-Financed Projects

19. ADB has on-going projects in the water sector focusing on irrigation rehabilitation and upgrading, notably the Amu Bukhara Rehabilitation Project which is located in the Amu Darya irrigation network in the western area of Uzbekistan around Bukhara. Activities at this project and also taking into account the Land Improvement Project it is possible to provide the following recommendations and lessons learned: (i) the government remains unconvinced about the need for any technical support to assist in development or implementation of the project, insisting that there is enough local experience, but this is usually a very optimistic viewpoint that later results in delays and disagreements during implementation. In this case, Ministry of Agriculture (MOA)'s capacity is limited and does not have enough resources or technical capacity to deliver at the highest level on a consistent basis; (ii) ADB should do more through policy dialogue or advisory technical assistance to help MOA improve its own coordination efforts both internally with the MOA itself and also with international donors. ADB should consult with key development partners to see whether they would be interested in convening a relevant sector group. Helping MOA to develop agriculture sector strategy and to organize roundtables or workshops will be particularly effective in supporting the development of effective programs in coordination with development partners.

20. Relevant knowledge of the recently approved Small Business Finance Project (SBFP)² has also proven extremely useful in formulation of the working arrangements to maximize time and resource efficiency. The earlier financial intermediation loans also provided the following lessons, which have been considered in the project design: (i) providing PFIs with longer-term funds for on-lending to small businesses is very relevant in the horticulture sector when dealing with establishment of fruit orchards which may take several years to mature; (ii) strengthening PFIs' capacity for lending, rural outreach, and risk management; and (iii) extensively engaging with women's businesses to improve their entrepreneurial capacity.

21. Implementation results of the ongoing Horticulture Value Chain Development Project (Lona 3471-UZB) suggests that the success of projects of similar nature lies in PFIs proactively identifying a diverse potential clientele (or subborrowers) with financing demand for export-oriented horticulture value chain activities such as establishment of greenhouse, refrigerated storage, intensive orchards, processing lines for horticultural products. As of February 2018, seven qualified PFIs have done their potential clientele inventory, the preliminary demand estimates of which indicate that the proposed additional financing loan of \$198 million can be

² ADB. 2016. *Report and Recommendation of the President to the Board of Directors: Proposed Loan to the Republic of Uzbekistan for Horticulture Value Chain Development Project*. Manila.

fully utilized by December 2021 subject to the ADB's Board approval of the additional financing project.

C. Other Development Partners

22. The European Union (EU) is about to start activities in support of the World Bank HDP through provision of grant funding (€26 million) to implement the activities identified in component (i) Agriculture Support Services of the World Bank HDP. The International Fund for Agricultural Development is implementing a \$30 million Horticulture Development Project to assist in the productivity enhancement for high value orchards.

23. USAID has an ongoing project supporting Agriculture Value Chain Development in focus areas of Uzbekistan. As part of this activity it also has training and development activities relevant to the horticulture sector, looking in depth at agriculture markets and value chains for specific products.

24. In the area of agriculture development, GIZ is working with USAid and the European Union in introducing international standards in selected value chains (in particular horticulture – GlobalGap) and marketing strategies in selected focus areas with the medium-term objective to improve income and employment situation of disadvantaged sections of the population. In collaboration with national several research institutes, GIZ supported the establishment of a number of demonstration plots on fruit tree production on an area of 15 ha in Khorezm (Urgench State University), Surkhandarya (Uzbek Research Institute of Plant Industry) and Karakalpakstan (Shroedder Institute). New technologies (e.g., drip and sprinkler irrigation; efficient pumping technologies; sedimentation system of ponds to reduce salinity; IPM; tree pruning techniques; inter-cropping; conservation agriculture systems and technologies, together with land levelling in irrigated areas) were successfully tested and extension agents were trained to provide fee-based consultancy services to farmers.

25. The IFC Agribusiness Standards Advisory Program assists local companies in applying food safety, environmental, and social standards throughout the agribusiness value chain while strengthening the capacity of local consultants. Improved standards help agribusiness firms meet regional and export market requirements while building a foundation to mobilize investments and help the agribusiness industry realize its full potential.

26. The Japan International Cooperation Agency has the Enhancement of Farmers Income through applying Modern Apple Growing Technology (2015–2017)-Collaboration with Hirosaki University and Fujisaki City in Aomori, Japan to modernize apple varieties, improved technology of planting apple trees and improve marketing system to enhance farmer income.

27. The World Bank's country partnership framework includes 4 pipeline projects: (i) Ferghana Valley Water Resource Management Project, Phase II; (ii) Livestock Sector Development Project; (iii) Agriculture Modernization Project; and (iv) Horticulture Development Project (Additional Financing).³

28. Information and lessons from these initiatives have been taken for the additional financing project design, and coordination has been pursued to ensure that work is not planned in the same areas—or if so then complementary activities rather than overlapping activities are pursued.

³ The World Bank's Horticulture Development Project (Additional Financing) was approved in January 2018.