

PROJECT INFORMATION DOCUMENT (PID) CONCEPT STAGE

Report No.: PIDC27507

Project Name	Integrated Dairy Productivity Improvement Project (P155412)
Region	EUROPE AND CENTRAL ASIA
Country	Kyrgyz Republic
Sector(s)	Animal production (60%), General finance sector (20%), Agro-industry, marketing, and trade (20%)
Theme(s)	Rural services and infrastructure (25%), Rural policies and institutions (25%), Trade facilitation and market access (25%), Micro, S mall and Medium Enterprise support (15%), Climate change (10%)
Lending Instrument	Investment Project Financing
Project ID	P155412
Borrower(s)	Kyrgyz Republic
Implementing Agency	Ministry of Agriculture and Melioration, Agribusiness Competitiveness Center
Environmental Category	B-Partial Assessment
Date PID Prepared/ Updated	28-May-2015
Date PID Approved/ Disclosed	27-Jul-2015
Estimated Date of Appraisal Completion	16-Mar-2016
Estimated Date of Board Approval	02-Jun-2016
Concept Review Decision	Track II - The review did authorize the preparation to continue

I. Introduction and Context

Country Context

1. With GNI per capita of US\$1,200 (2013), the Kyrgyz Republic is one of the low income economies of the Europe and Central Asia Region. In 2013, about 37% of the population lived below the poverty line. The incidence of poverty in rural areas was higher than in urban areas (41% vs. 28%). The economic growth in the country is quite volatile. The GDP growth was 6% in 2011 but contracted by 0.9% in 2012, owing to a sharp drop in gold output. In 2013, the economy grew at a whopping 10.9%, but slowed back to moderate 3.6% in 2014. The narrow export base is dominated by gold with some share coming also from the agriculture sector. The Kyrgyz Republic is highly vulnerable to external shocks, including many households depend on remittances from the energy-based economies of Russia and Kazakhstan. It is partially dependent on wheat imports from

Kazakhstan and the past global food price shocks quickly transmitted to the country. The official, unemployment rate in the country has hovered below 10% for the past decade, however mostly on account of significant outmigration of labor force (predominantly men, majority from rural areas) to Russia and Kazakhstan. The recent economic difficulties of Russia and strong devaluation of the ruble has heavily affected the earnings of the migrants and their remittances to their families in Kyrgyzstan. Albeit not in a mass scale, return of a certain share of the close to a million labor migrants can be expected. It can create further pressure on the employment and job market in the country. Rural households have been most affected by recent crises.

Sectoral and Institutional Context

2. Agriculture is an important sector for the Kyrgyzstan economy and livestock farming is a major livelihood support system for the rural people. Agriculture contributes about 20% of the GDP, yet is still a major employer, providing more than a third of jobs in the economy. It is a key priority for government because of its contribution to poverty reduction and rural employment. Livestock production, which accounts for about 50% of the agricultural GDP is dominated by household and small farm production, and is important for rural household food security, nutrition, providing regular income and acting as a social safety net which can be sold in times of hardship and economic distress. The primary land use of the country is native pasture production (87% of the total land is under pastures), which provides an advantage for livestock-based livelihood and food security for the rural population.

3. With the accession of the Kyrgyz Republic to the Eurasian Economic Union (EEU), the country's agriculture sector is facing new challenges and but also new opportunities. Kyrgyz Republic became a full member of the EEU in May 2015. The EEU, among other countries, also includes Russia and Kazakhstan, which are Kyrgyzstan's main export markets. However, since 2012 a dairy export ban to Kazakhstan has been in force, limiting the number of dairy exporters to seven (more information in paragraph 6 below). The concern, therefore, persists that even though the membership to the EEU presents new market opportunities, the Kyrgyz dairy producers and processors may be unable to capitalize on them due to their inability to meet the animal health, food safety and quality standards of the EEU. It reduces their competitiveness in the EEU and puts them at risk of not being able to sell their dairy products. However, on the opportunity side the Kyrgyz dairy products are believed to be of better taste and quality due to the production model under which most or significant share of the cow feed comes from natural pastures. Any project intervention into the dairy sector would be very timely, as it would allow the Kyrgyz dairy sector to capitalize on the new market opportunities, as well as on the achievements and initiatives of the previous and ongoing projects in the agriculture sector .

4. The demand for Kyrgyz dairy products, in particular, in Kazakhstan, is significant. Even though the border is closed to most of the official dairy exports (only seven companies can export dairy products to Kazakhstan), the informal trade is booming. Based on unofficial data, while the official exports of milk/dairy products in 2012 were indicated as \$30 million (equivalent to 4% of the annual milk volume), the unofficial export revenues were closer to US\$ 100 million (14% of the milk volume). Russia is also considered a potentially large export market for dairy products (such as cheeses). Once the milk quality is upgraded, exporting to other countries (such as China), should be possible.

5. The Kyrgyzstan dairy sector is primarily dependant on small holder private dairy units with an average herd size of 3-5 cows. Around 60% of rural population own livestock, but the average herd

size tends to be small. Milk is an important part in the diet and around 90% of the population consume dairy products regularly. In value terms milk is one of the top 5 agricultural products of the country. The per capita availability of milk is around 193 kg and 25% of the milk produced is in surplus for processing and export. Dairy export is therefore a pressing need for Kyrgyzstan. It should be noted, however, that farmers who keep animals do not consider themselves dairy farmers, and the animal breeding practices are very poor, which accounts for very low dairy sector productivity.

6. Livestock productivity is very low if compared to international standards. Furthermore, the productivity is falling year-by-year: 2,041 kg (2009), 2,036 kg (2010), 2,023 kg (2012) and 2,013 kg (2013). Many factors cause this low productivity at the farm level: animal diseases, inadequate animal health control, weak laboratories, fragmented vaccinations, low breed stock quality and absence of breeding policies and practices except for limited cases; inadequate feeding, proper shed maintenance, and hygiene issues; overall weak knowledge of animal husbandry techniques; low level of investments into production and marketing infrastructure. Addressing these issues can significantly increase both the productivity and total output of milk, which can help solve the problem faced by the dairy processors. Namely, the processors experience shortage of clean and high quality milk, and as a result underutilize their processing capacities and forego additional incomes that could come from exporting to other countries, and primarily, to the neighboring Kazakhstan. The export volume of dairy products is about US\$ 26.0 million annually. However, it has been prone to import ban risks from Kazakhstan, such as in October 2012 when it banned the import of dairy products from Kyrgyzstan due to the epizootic situation in the country. The ban was lifted at end of 2014 for seven out of 11 exporting dairy processors of Kyrgyzstan. The ban affected not only the processors but also the milk selling farmers and households as well other players in the chain.

7. To help the country capitalize on market opportunities presented by the Eurasian Economic Union, the Kyrgyz Dairy Sector Development Program (KDSDP) was initiated by IFC in 2014, to help ensure steady milk exports to Kazakhstan through a dedicated dairy value chain approach. The KDSDP implementation was started through some DFID and SECO funding (about US\$ 1million), mostly supporting the processors. However, issues related to animal health concerns and low productivity also have to be resolved, so the initiative grew into a comprehensive program – now called Kyrgyz Dairy Sector Development Program. The KDSDP is expected to cover all aspects of the dairy value chain: cattle breed improvement, animal feed improvement, improvements of animal productivity and milk quality, animal health and hygiene, milk collection upgrades, laboratory and testing capacity (animal disease control, food safety and milk quality) upgrades processing capacity upgrades, food safety standard upgrades, enabling regulatory framework, and export promotion. The activities are grouped in four broad areas, with the following geographic coverage in Issyk-kul area:

I. Veterinary sanitary protocols, animal identification, data management system and border check posts. This will be implemented by the state veterinary department and the private veterinary service system. An FAO project on animal identification and data management would be integrated into this component. The entire Rayons (5 Rayons) of the Issyk-kul Oblast will be taken up for this activity.

II. Dairy value chain intervention for farmers and agro-processors. This component would be implemented through the processing companies and their clients i.e. farmers and milk collection agents. The set of activities that will be implemented through this component include organizing

farmers groups, demonstration farms, pasture and feed management, farm hygiene improvements, clean milk production, credit systems for herd expansion and acquiring farm machineries, advisory and extension services, strengthening milk collection infrastructures, hygienic and transparent milk collection and transportation, milk processing through HACCP standards, etc. These interventions will be implemented predominantly in three rayons (Tup, Ak-Suu, Jeti-Oguz) of the Issyk-kul Oblasts where dairy farming is most intensive.

III. Strengthening of State infrastructures responsible for disease diagnosis, disease control, disease monitoring, research and development, vaccine and drug quality control, food quality and safety, farmers' training organization, breeding institutions, OIE accreditation and linkage with International livestock and veterinary Institutions for capacity development.

IV. Policies, regulations, legislations and creating an investment climate and business enabling environment. Simultaneous efforts to be taken to work on issues related to meeting the legal requirements such as EU and EEU regulations, export logistics and exploring new potential markets such as China and Middle East.

8. The KDSDDP, in addition to the start-up funding from DFID and SECO mentioned in paragraph 7 above, is expected to be funded by a number of financiers, including WBG, DFID, Government of Austria, other donors, private sector and government of the Kyrgyz Republic. The total cost of the program is around US\$30-35 million (depending on the scope). Each donor/participant in the program will focus on a specific area, in order to ensure efficient use of the funding and avoid financing the same activity twice. Through T&C/IFC and F&M/IFC, the DFID and Austrian Government are providing co-financing for development of the dairy sector value chain, focusing on the agro-processing, export promotion and regulatory framework. However, to make the value chain development successful, it is imperative that on-farm improvements are supported to ensure high quality milk, as well as necessary public sector investments. The Program will also leverage private sector investments, in particular from the agro-processing companies and farmers, and a credit line from IFC.

9. Selection of the project area. Issyk-kul Oblast has been selected as the project area based on the results of the F&M/IFC-financed feasibility study carried out in February 2015. Issyk-kul Oblast was recommended as the suitable site for this dairy value chain intervention, considering the natural barriers for restricting the animal movement, abundance of pasture, farmers' willingness to adopt, existence of direct milk collection system from farmers, less competitiveness between buyers, better milk production growth rates and closeness to Kazakhstan. The Oblasts covers about 330,000 population and 200,000 heads of livestock.

Relationship to CAS

10. The strategic objective of the 2014-2017 Country Partnership Strategy is to help reduce extreme poverty and promote shared prosperity through support for improved governance, with emphasis on three broad areas: public administration and public service delivery; business environment and investment climate; and natural resources and physical infrastructure. The overall dairy sector development program, and this proposed project, are fully in line with the CPS strategic objective. The program will help reduce poverty by supporting the smallholder dairy producers, and promote jobs and prosperity through building and strengthening the dairy value chain linkages and adding value along the chain, also contributing to the Bank's twin goals. Improved public service delivery aspects will be addressed through joint work with the Veterinary Services Department, while the

business environment and investment climate issues, specific for the dairy value chain, will be tackled through business advisory and legal and regulatory advice and technical assistance under the complementary IFC projects financed by DFID and the Government of Austria. Training in proper fodder management and animal feeding will encompass efficient land resource management including pastures and fodder production.

11. The project activities are also fully in line with the priorities of the agriculture sector described in the CPS (para 34) such as expanding the agricultural extension services, animal health and veterinary services, food safety, encouraging greater private sector participation, developing small and medium-sized agricultural enterprises, designing appropriate financial instruments and investing into storage and distribution. The CPS also highlights livestock as the sub-sector of agriculture with good prospects, although further strengthening is required to be internationally competitive.

12. In addition, the project will support a number of cross-cutting areas such as gender, job-creation, climate change, and conflict prevention. Gender and jobs are expected to be positively affected as dairy farming is a labor intensive business and requires family or hired labor, and in many cases women tend to the animals, while youth are involved in grazing, grass cutting and fodder preparation, shed cleaning etc. Climate change and environment would benefit from: (i) proper manure management practices as manure is one of the major sources of greenhouse gas (GHG); (ii) land resource and pasture management, in particular to help the overgrazing issue around villages; and (iii) strategies on balanced feeding practices will have positive impact on methane and other GHG emission reduction. Finally, trust building activities along the dairy value chain and working towards the same goal can prevent or mitigate potential conflicts among the value chain participants.

13. The project also supports the National Strategy of Sustainable Development 2013-2017. In Agriculture is the first sector listed in the section on development of strategic sectors of the economy, followed by energy, mining, etc. Among other things, the National Strategy calls explicitly for development of agriculture clusters, improvement of breed stock, improvement of veterinary services, provision of training to farmers, support to production of feed, milk and dairy processing. The comprehensive value-chain approach used by the project will address all or most of these issues.

II. Proposed Development Objective(s)

Proposed Development Objective(s) (From PCN)

The development objective of the project is to contribute to achievement of the Dairy Sector Development Program objectives by improving animal feeding, breeding and management practices in the project area, as well as animal health care and veterinary services, through investments and training support.

The overall development objective of the Dairy Sector Development Project in the Kyrgyz Republic is to improve export potential of Kyrgyz dairy products to neighboring countries (Russia and Kazakhstan), increase incomes of dairy farmers, and create new jobs along the dairy supply chain.

Key Results (From PCN)

14. The expected project-level outcomes:

- 1) At least 60% of farmers are using improved animal feeding, health, breeding and management practices;

- 2) 100% cattle population covered under animal identification system and preventive vaccination program in the project area;
- 3) At least 40% of the milk procured in the project area is of highest quality standard.

III. Preliminary Description

Concept Description

15. Approach.

(i) Creating jobs and incomes along the value chain. The dairy sector is rather labour-intensive, and the value addition along the value chain and created linkages between farmers, processors and further to the markets yielding higher returns are expected to increase incomes of farmers and create jobs along the value chain. This will involve partnership building activities along the value chain (dairy producers, processors and traders), association of farmers into groups, as necessary, and providing access to training, knowledge and investments for the value chain participants.

(ii) Gender and youth dimension of the project is very strong. Gender and jobs agenda are expected to be positively affected as dairy farming is a labor intensive business and requires family or hired labor. In addition, the milk collection, animal feed preparation and other activities are expected to generate additional employment and, possibly small business development. Women are in particular focus under this project, as in many cases women tend to the animals (it is quite commonly observed in smallholder dairy systems that two thirds of the husbandry activities are handled by women). The employment generation and small business activities may encourage young people to stay in the villages and take up farming and generate (additional) income through provision of services (such as grass cutting and fodder preparation, shed cleaning, milk collection and testing, etc.).

(iii) Citizen engagement and feedback. The engagement of the beneficiaries in the project implementation is expected to be very close by the nature of project. Therefore, transparency, consultations and feedback mechanisms will be central part of the project. The project support building a value chain, which requires development of mutual trust between the various links of the value chain (such as among the milk producers, as well between producers, processors and traders). To ensure that the project beneficiaries trust each other and work towards the same objective will require continuous consultations and information and knowledge exchange. Facilitation of beneficiary engagement and feedback will be a key task of the project staff located in the field. In addition, a feedback mechanism operating at both national and regional levels will allow project beneficiaries to provide feedback on project activities. Feedback/grievances responded and/or resolved within the stipulated service standards for response times will be monitored. Finally, specific third party monitoring of project activities will be supported annually to ensure transparency and feedback on project progress.

(iv) World Bank Group synergies. Project design and implementation involves active collaboration with IFC which views agribusiness as a priority sector. The IFC advisory staff will, using the expected funding from DFID and the Government of Austria, focus on working with agro-processors, building upward linkages to markets, and partnerships with farmers and farmer associations. These activities will focus on: (a) identify suitable aggregators (dairy companies) and strengthening their capacity to expand, invest and provide services to farmers; (b) assist the Government of the KR in improvement of the food safety control by reforming relevant legislation

and trainings of public officials; (c) improvement of the doing business conditions and investment attractiveness of the dairy sector by improvement of the current regulatory environment and introduction new regulations. The possibility of IFC Investment to contribute financing to the credit line for on-farm investments is also being discussed.

Project Components

16. The IDA-financed project will contribute to the implementation of overall program, by supporting the necessary public investments (such as veterinary posts and animal health laboratory upgrades), support the AI services and breeding infrastructure, farmer training, and provide a small credit line to support on-farm investments. The project components that have been described below are for the interventions of imminent urgency, without which it would be difficult to start the program even though other donor funding becomes available. The other donor funding is expected to predominantly finance agro-processing, marketing and export promotion activities, (including the regulatory framework), and IDA financing is key to support on-farm activities and public sector involvement. The total financing gap for the Program is in the order of US\$15 million. The full financing would allow full implementation of the activities related to the public investments and on-farm activities in the project area .

Component 1: Fodder and Feed Development Program (tentatively US\$1.5 million, all IDA)

17. The component will finance seeds, other inputs, equipment, and training and demonstrations to support farmers in feed and fodder development program. The component will support activities related to high quality fodder production, hay preparation, establishment of sites for silage preparation, feeding practices (balanced feeding), access to pre-formulated concentrate feed and mineral supplements. A number of demonstration farms/household will be selected for practical training and dissemination of results of improved practices where the project will support, on matching grant basis, demonstrations of sound practices. Demonstration farm/households will share the results achieved with farmers and other interested parties, to disseminate good practices.

Component 2: Veterinary Services and Animal Health (tentatively US\$1.9 million, all IDA)

18. The component will focus on the following activities (i) animal identification and registration; (ii) ensuring vaccinations of 100% of animals in the project area; (iii) upgrading the regional veterinary laboratory and capacity building in disease control; (iv) establishment and maintenance of the veterinary posts; and (v) training of farmers in animal health care management, sound manure management and animal husbandry practices.

19. This component will contribute to the PDO by improving the traceability and health of the animals as well as by supporting the improvements in the breed stock of the dairy cows.

20. Animal identification and registration activities will build on the ongoing FAO Animal Identification Pilot Project that aims to develop the software and registration procedures, which will then be tested out in the Issyk-Kul region. The IDA project will support the scaling up of the animal identification for cattle, such as support the training of registrars and equipment for registration .

21. Support to vaccinations will target also the cattle population for major diseases like FMD, anthrax and brucellosis, and regular heard testing for tuberculosis. This will include procurement of

vaccines, training of private veterinarians, and provision of basic veterinary equipment for eligible private veterinarians with contracts to serve the targeted farmers.

22. The regional veterinary laboratory in Karakol, which is in very poor shape, will be supported with upgrading of its facilities, equipment and staff qualifications to an acceptable level.

23. The component will help to set up the veterinary zoning with establishment of veterinary checkpoints in the exit/entry sites to the region. There are 3 main entry/exist posts in the Oblasts, and veterinary posts will be equipped and supported by the project.

24. The component will also train farmers in a minimum range of subjects, including farm hygiene, animal health care, sound manure management, animal husbandry, on-farm quality standards for high quality milk production, supported by demonstrations.

Component 3: On-farm Investments (tentatively US\$3.6 million, including US\$1.0 million IDA, US\$2.0 million IFC, and US\$0.6 million beneficiaries)

25. Farmers need access to finance to invest in productivity improvements, herd expansion, farm mechanization, system for quality measures, etc. A credit line through participating financial institutions will support the farmer needs for investment and working capital financing. The project is expected to work with one or two selected financial institutions which have undergone due diligence and interested in supporting value chain development in the agricultural sector. As appropriate, new tailored financing schemes will be introduced (e.g. lending to group of farmers, or lending through processing companies, etc.), which will be supported by PFI training in the new financial instruments.

Component 4: Project Management (tentatively US\$0.6 million, all IDA)

26. The component will cover the costs associated with the project management, monitoring and evaluation and impact assessment. It is expected that Agribusiness Competitiveness Center (ABCC) and the Credit Line Management Unit (CLMU) at the Ministry of Finance will implement the technical assistance and credit line activities, respectively. In addition, as under the previous projects, ABCC will be responsible for procurement activities under the project, and CLMU for financial management of the project. ABCC will also open a regional office in Issyk-kul. The PMU will closely liaise with the other projects under the program, to ensure that all necessary activities are implemented, and no duplications/over-laps occur.

IV. Safeguard Policies that might apply

Safeguard Policies Triggered by the Project	Yes	No	TBD
Environmental Assessment OP/BP 4.01	x		
Natural Habitats OP/BP 4.04			x
Forests OP/BP 4.36		x	
Pest Management OP 4.09			x
Physical Cultural Resources OP/BP 4.11		x	
Indigenous Peoples OP/BP 4.10		x	

Involuntary Resettlement OP/BP 4.12		x	
Safety of Dams OP/BP 4.37		x	
Projects on International Waterways OP/BP 7.50		x	
Projects in Disputed Areas OP/BP 7.60		x	

V. Financing (in USD Million)

Total Project Cost:	5.00	Total Bank Financing:	5.00
Financing Gap:	0.00		
Financing Source			Amount
BORROWER/RECIPIENT			0.00
International Development Association (IDA)			5.00
Total			5.00

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