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NICARAGUA

INNOVATIVE MODELS FOR PROVIDING LONG-TERM FINANCING TO COFFEE PRODUCERS IN NICARAGUA

(NI-M1038)

DONORS MEMORANDUM

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ABBREVIATIONS

C2F	Canadian Climate Fund for the Private Sector in the Americas
CRF	Coffee Renovation Facility
FUNIDES	Fundación Nicaragüense para el Desarrollo Económico y Social [Nicaraguan Foundation for Economic and Social Development]
GAFSP	Global Agriculture and Food Security Program
IDA	International Development Association (World Bank Group)
IDB	Inter-American Development Bank
IFC	International Finance Corporation (World Bank Group)
PSR	Project Status Report
SCF	Structured and Corporate Financing Department
SME	Small and medium-sized enterprise
SMPs	Small and medium-sized producers
SMS	Sustainable Management System

PROJECT SUMMARY

INNOVATIVE MODELS FOR PROVIDING LONG-TERM FINANCING TO COFFEE PRODUCERS IN NICARAGUA

(NI-M1038)

The most recent outbreak of coffee leaf rust[1] has had a severe impact on coffee growers in Central America. Losses during the 2012-2013 crop year were estimated at US$499.4 million in the region,[2] where some 50% of the total land area planted in coffee was affected by this fungus. The incidence rate varies by country, but in Nicaragua and Honduras alone it is estimated at between 20% and 40%.[3]

Coffee leaf rust is causing a decline in the incomes of coffee growers and of all the families that depend on the crop for their source of employment, as the fungus reduces production yields. While there are already some public-private efforts under way at the regional level to address the technical aspects of coffee leaf rust in the field, it is clear that if the sector is to emerge from the crisis it will also be necessary to mount a broad program of financing for renovating coffee plantations or establishing new ones. In this respect, the responses have not been as strong. Given the risks inherent in the sector, the fragile nature of small-scale family farming, and the instability of coffee prices, neither the banks nor the governments themselves have come up with a plan for coffee financing in a strategic manner. With annual renovation costs estimated at US$5,000 per hectare during the first three years and an average of US$1,200 per hectare in maintenance costs,[4] and an interval of three to four years before the new coffee plants begin to produce cherries, there is an urgent need to provide a complete solution that incorporates long-term financing, something that the financial sector is not doing at this time.

Coffee experts and leading firms such as Starbucks and Mondelez agree that to address the current situation in Central America will require more than just a technical or agronomic fix. As indicated in a recent study,[5] 89% of producers surveyed in Nicaragua were relying on short-term credit to pay their workers and to purchase inputs during the season prior to harvest and during the harvest. Nevertheless, only 11% had access to medium-term credit for coffee growers, and only one producer had access to long-term credit for renovation.

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1 *Roya*, or coffee leaf rust, is an orange-colored fungus that grows on coffee trees, limiting the source of nutrition for the coffee cherries, causing the leaves to fall, and reducing the quantity and quality of the coffee harvest.

2 Based on the 13 May 2014 report of the International Coffee Organization (ICO) http://dev.ico.org/documents/cy2012-13/ed-2157e-report-clr.pdf.

3 Ibid.

4 IFC/IDB estimates, depending on the size of the farm and the incidence of the fungus. Producer standards in Nicaragua (small-scale producer, less than 12 hectares; medium-sized producer, 12 to 50 hectares; large-scale producer, more than 50 hectares).

5 Performed by IFC as part of the due diligence mission, jointly with the IDB's SCF.

This project takes an innovative approach that will offer flexible financing alternatives for small and medium-sized producers (SMPs) of coffee, through a specialized private export agent, ECOM, a solid operator that has been in the coffee business for decades, negotiates directly with producers, and provides short-term loans on flexible terms designed to fit with the seasonal nature of the business. In contrast with the majority of private firms, ECOM has established a technical and financial structure through which it maintains close relations with coffee growers. Both the World Bank's International Financial Corporation and the IDB's Structured and Corporate Financing Department (SCF) are in the process of guaranteeing a loan operation of up to US$12 million each, as part of a US$30 million line of credit for developing a long-term financing framework for coffee producers in the ECOM supply chain through its subsidiary in Nicaragua, Exportadora Atlantic. This line of credit will offer producers the long-term financing they need to replace their coffee plants with leaf-rust-resistant coffee plants.

The objective of this MIF project is to provide strategic technical assistance so that long-term financing for producers can be sustainable over time and profitable, while incorporating best practices in a branch of agriculture that is sensitive to climate change. Specifically, the MIF funds are expected to improve the credit processing capacities of Exportadora Atlantic[6] and to strengthen information technology tools, technical tools for crop monitoring, and risk control within the firm. Atlantic's financing is expected to comprise long-term loans of up to eight years, with a grace period of three years. These conditions are necessary to allow producers to phase in the partial replacement of their coffee plantations over time. MIF support will complement the IFC/SCF loans in four areas: creating capacity for long-term loans; evaluating climate risk and monitoring its impact; empowering women coffee growers; and generating and disseminating knowledge. With this project, the MIF will be joining with other actors committed to providing a comprehensive solution to the coffee leaf rust infestation by testing an innovative financing model that could be replicated in other value chains in order to increase access to financing for SMPs throughout the region. This is a pilot project for ECOM in Nicaragua, which has plans to replicate it in other countries where it operates, including Costa Rica, Honduras, Guatemala, and Mexico, by transferring the newly developed capacities to other countries of the region. The IDB loan is planned as a line of credit that is based on the outcomes in Nicaragua, and that can extend financing with similar conditions for other countries.

[6] The loan and the technical assistance will be channeled through Exportadora Atlantic Ltda., ECOM's subsidiary in Nicaragua. A detailed description can be found in the section on the executing agency

INNOVATIVE MODELS FOR PROVIDING LONG-TERM FINANCING TO COFFEE PRODUCERS IN NICARAGUA (NI-M1038)

EXECUTIVE SUMMARY

Country and geographic location:	Nicaragua (areas: Nueva Segovia, Jinotega, and Matagalpa) Honduras[7] (areas: Comayagua, Cópan, Lempira, La Paz, Santa Barbara, El Paraíso, Ocotepeque)
Executing agency:	Exportadora Atlantic
Access area	Access to Finance; Access to markets and capabilities
Agenda:	SME financing; Linking small producers to high-value markets
Coordination with other donors/ Bank operations:	This project has been designed and will be implemented jointly with the IDB's SCF and the World Bank's IFC.
Direct beneficiaries:	The project is expected to have 560 direct beneficiaries who will obtain longer-term loans for renovating their plantations.
Indirect beneficiaries:	The project is expected to have 4,000 indirect beneficiaries in Honduras and Nicaragua, who are part of ECOM's coffee supply chain.

Financing:

Technical cooperation:	US$ 326,705	60%
Investment:	US$ 0	
IDB loan (SCF):	US$12,000,000	
Total MIF Contribution:	US$ 326,705	
Counterpart:	US$ 219,600	40%
Cofinancing (if any):	US$ 0	
Total Project Budget:	**US$ 546,305**	100%

Execution and disbursement periods:	36 months for execution and 42 months for disbursements
Special contractual conditions:	The following will be conditions precedent to the first disbursement: (i) a progress report on the portfolio of loans to producers using resources from the Bank's financing; and (ii) a development plan for the consulting services to be performed under this project, and their respective coordination with the IDB/SCF credit component.

[7] Honduras is the second country after Nicaragua in which loan operation RG-X1220 will grant financing. Although this is not a regional project, some of the activities will be carried out in Honduras, with the objective of increasing capacities prior to the start of lending operations in that country.

Environmental and Social Impact Review:	This operation has been pre-evaluated and classified according to the requirements of the Bank's Environment and Safeguards Compliance Policy (OP-703). As the impacts and risks are limited, the proposed category for the project is C.
Unit with disbursement responsibility:	Country Office in Nicaragua

I. BACKGROUND AND RATIONALE

A. The problem to be addressed by the project

1.1 The most recent outbreak of coffee leaf rust [8] has had a severe impact on coffee growers in Central America. Losses during the 2012-2013 crop year came to US$499.4 million in the region,[9] where some 50% of the total land area planted in coffee was affected by this fungus. The incidence rate varies by country, but in Nicaragua and Honduras alone it is estimated at between 20% and 40%.[10]

1.2 Coffee leaf rust is causing a decline in the incomes of coffee growers and of all the families that depend on the crop for their source of employment, as the fungus reduces production yields, which constitutes a real threat to the financial survival and stability of the producers. While there are already some public-private efforts[11] under way at the regional level to address the technical aspects of coffee leaf rust in the field, it is clear that if the sector is to emerge from the crisis it will also be necessary to mount a broad program of financing for renovating coffee plantations or establishing new ones.

1.3 The main problem to be addressed by this project is the **lack of viable alternatives for long-term financing supplemented by adequate risk mitigation**, which coffee SMPs need in order to renew their plantations in a sustainable manner. A study by the Nicaraguan Foundation for Economic and Social Development (FUNIDES)[12] confirms that, although coffee growers have access to short-term financing, the medium- and long-term financing options in the country are limited. According to data from the Superintendency of Banks, less than 11% of the private banking system's portfolio was geared toward the agriculture sector in 2014, compared with 13% in 2011.

1.4 The FUNIDES study recognizes that the absence of medium- and long-term financing can also be attributed to low productivity in the agriculture sector. While producer credits are available in the form of advances for coffee harvests and collection, investors and financial institutions offer no long-term products, because of the limited capacity of SMPs to boost their yields and future incomes. In this respect, productivity has become a key concern for coffee SMPs, given the speed

8 *Roya*, or coffee leaf rust, is an orange-colored fungus that grows on coffee trees, limiting the source of nutrition for the coffee cherries, causing the leaves to fall, and reducing the quantity and quality of the coffee harvest.

9 Based on the 13 May 2014 report of the International Coffee Organization (ICO) http://dev.ico.org/documents/cy2012-13/ed-2157e-report-clr.pdf.

10 Ibid.

11 The Inter-American Institute for Cooperation on Agriculture, the United States Agency for International Development, and other institutions are cooperating in their efforts to solve the problem through the introduction of new, more resistant coffee varieties.

12 Solorzano, Julio and Caceres, Félix. "Productive improvement for Small and Medium Coffee Growing Farmers." May 2012.

with which coffee leaf rust is spreading in Central America. It has now affected 30% of Nicaragua's coffee plantations, according to estimates of the International Coffee Organization. Only with a well-coordinated program that works closely with farmers to enhance their yields over the long run will it be possible to attract long-term financing, which is what this project with Exportadora Atlantic, a subsidiary of ECOM, is proposing.[13]

1.5 Working through Exportadora Atlantic, the MIF's technical assistance will address these two issues in a comprehensive manner. It will support the technical operations of Atlantic in its fieldwork with producers, strengthening instruments for intervention and monitoring of production over the long term, and it will work to strengthen the mechanisms for granting credit, which will accompany the technical assistance program in the field. Coffee growers (who are already part of the Atlantic supply chain) will benefit from more flexible and longer-term financing terms and conditions, with the option of repaying the Atlantic loan in coffee.

Causes of the problem

1.6 **Financial intermediaries do not offer adequate services to small-scale coffee producers at this time.** Currently, the regional and local financial system only participates in the coffee sector in a limited way. According to FUNIDES, the coffee growers' restructured debt is only now recovering from the financial crisis that Nicaragua experienced with the collapse of world coffee prices over the 2000-2005 period. Consequently, the available options do not match the needs and the timeframes for coffee plantation renovation programs. As a result, private exporters have become increasingly important in the financing of small and medium-scale producers.

1.7 **Rising perception of the risk associated with climate change**. The serious outbreak of coffee leaf rust in Central America has reduced harvests by between 10% and 20%. Around 30% of the coffee growing area in Nicaragua is severely affected by the fungus, and the average harvest is only 0.5 tons (10 quintals) per hectare.[14] With limited tools available in the field for assessing the climate change risk, smaller harvests will merely increase the risk profile of coffee growers and limit their access to financing even further.

1.8 **Lack of adequate, reliable, and usable historical information on coffee production and yields, as needed to reduce credit risk**. While there have been a number of studies of coffee production at the regional level,

[13] Atlantic is a coffee and cocoa buying, processing, and marketing firm. For more details, please refer to the section on the executing agency.

[14] Based on information obtained from Atlantic, field observations by the team, and a November 2013 study financed by IFC.

they are not available to producers and buyers as a basis for making quick decisions. Only a few commercial-scale farms have advanced and complex information systems integrated within a single operating platform. The great majority of growers have no access to these levels of information. In this respect, Atlantic has developed a "Sustainable Management System" (SMS) designed to compile data on all small-scale producers who are part of its chain. This system, which captures historical data on production, farm location, yields, pests and other matters, has great potential for improvement to make it more useful to farmers and their medium- and long-term renewal plans.

1.9 In conclusion, the commercial banks are not extending long-term loans to farmers because they lack the agricultural knowledge and information on the producers needed to perform due diligence, and they have no risk profile for doing so. Conversely, firms such as Atlantic do have this type of knowledge about coffee production and are well acquainted with the farmers, but they do not always know how to implement long-term financing on a sustainable basis.

B. Project beneficiaries

1.10 This project will be carried out in Nicaragua and the beneficiaries will be 560 current small-scale producers, 85% of whom have fewer than 50 hectares of coffee plantations under production. However, the main objective is to expand the project to the regional level (by developing a regional line of credit[15] once the pilot project is implemented). The goal is to reach some 3,000 small-scale coffee growers in the ECOM supply chain in Nicaragua, Honduras, Costa Rica, and Mexico. The indirect beneficiaries will be the laborers employed by farmers to gather the harvest (approximately five coffee pickers per hectare).

1.11 The project will also address the unequal access to finance faced by women producers, who represent around 15% of the suppliers preliminarily identified by ECOM[16] to participate in the leaf rust-related plantation renewal project. According to earlier studies performed by IFC, women are less likely than men to own land or livestock, to adopt new technologies, to use credit or other financial services, or to receive an education or benefit from extension services. In some cases, women are not even in control of their own use of time. Bridging the gender gap in farming would produce significant benefits for the agriculture sector and for society. If women had the same access to financing as men, they could boost the yields from their plantations by 20% to 30%.[17]

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15 The regional credit line mentioned is regional operation RG-X1220, developed by SCF and approved in July 2014.

16 According to the due diligence conducted by SCF.

17 "Men and Women in Agriculture: Closing the Gap." Food and Agriculture Organization: United Nations. http://www.fao.org/sofa/gender/key-facts/en/.

1.12 For participating farmers, the line of credit has the potential to boost their harvests significantly (by a factor of two or three) and to reduce their vulnerability to climate change. Moreover, women producers will benefit from the interaction with ECOM personnel, who will be better equipped to respond to their specific needs.

C. Contribution to the MIF mandate, market access, and IDB strategy

1.13 This project will contribute to the MIF's mission of serving as an experimentation laboratory for testing innovative models that will boost economic development and provide support to entrepreneurs and their businesses. With the technical assistance provided to Atlantic, the latter will be in a better position to offer long-term loans to its producers and guide them through the process of renovating their plantations, while contributing to the frameworks of access to financing and access to markets. The MIF will thus help to boost the productivity of those farmers and to test the effectiveness of an innovative financing model.

1.14 **Link to the agenda**. This initiative falls within the SME financing agenda, as well as the agenda for linking producers to higher value chains. Through this project, access to long-term financing and technical assistance will be provided to coffee producers so they can proceed with the renovation of their plantations. In addition to this operation, the MIF is also implementing operation RG-M1153 with executing agency Root Capital, to provide financing and technical assistance for renovating coffee plantations. It seeks to benefit 40 organizations of producers (around 32,000 families producing coffee) in Honduras, Guatemala, Nicaragua, Mexico, and El Salvador.

1.15 **Collaboration with the IDB group**. This project is aligned with the country strategy with **Nicaragua** (2012-2017), in that it implements an initiative in a sector of great interest, namely rural development and value chains. The project has been designed jointly with the IDB's SCF, which has approved a loan in the amount of US$12 million for Atlantic to extend long-term financing to its producers, under operation NI-L1088.

II. PROJECT DESCRIPTION

A. Objectives

2.1 In terms of impact, the objective is to provide long-term financing to small and medium-sized coffee growers affected by coffee leaf rust, primarily in Nicaragua and subsequently in Honduras.[18] In terms of outcomes, the project seeks to support an innovative lending model whereby the lender will be a coffee marketing firm that will disburse loans to producers working in its value chain.

B. Description of the model/solutions/intervention

2.2 The MIF technical assistance will be geared to creating the internal capacity of the lender, Atlantic, to administer long-term loans and to improve its operating capacity in the process of renovating the coffee plantations affected by coffee leaf rust. It will also strengthen Atlantic's production information systems to incorporate data via mobile tools, the input of climate information, and more effective monitoring of progress in the renovation programs with the producers, in terms of the agronomic piece.

2.3 What makes this project unique is that the lender will be a coffee processing and marketing firm with an in-depth knowledge of the business, and with interests that are aligned with those of small and medium-sized coffee growers. Atlantic has in the past been providing short-term credit to its producers.[19] Consequently it has the advantage of technical know-how, in comparison with the banks, since it works closely with farmers and can offer them flexible financing terms, such as partial repayment in coffee. These flexible financing terms will make it possible to finance multiple harvests and to renovate the plantations, since their tenors are longer than one year (up to eight years). By December 2014, Atlantic had a portfolio of loans to producers of close to US$16 million, most of which were short-term loans, and it had a delinquency ratio of less than 3%.

2.4 By enhancing the existing capacities of Atlantic to provide long-term loans, the project will take advantage of the firm's knowledge to adapt its loans to the harvest cycle, and will select borrowers in light of their track record with the firm. By providing the financing needed to replace the coffee plantations, Atlantic will guarantee the supply of coffee over the long run.

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[18] Honduras is the second country after Nicaragua in which loan operation RG-X1220 will grant financing. Although this is not a regional project, some of the activities will be carried out in Honduras, with the objective of increasing capacities prior to the start of lending operations in that country.

[19] For the 2014 crop year, the ECOM loans averaged between US$9,000 and US$90,000.

2.5 The MIF's technical cooperation operation will be complemented by the advisory services of IFC, which will provide technical support for renovation of the plants, while the MIF will focus on Atlantic's loan processing capacities. The MIF funds will also be supplemented with counterpart financing from ECOM (whose support includes the technical staff and loan officers needed to carry out project activities). ECOM is committed to a counterpart contribution amounting to US$219,600.

2.6 The MIF's technical cooperation is essential for making this long-term financing model operational and sustainable, in that it will: (i) help ECOM create the internal capacity to analyze and monitor risk related to the new long-term loans to be disbursed, including the risks associated with climate change; (ii) transfer operating capacity to ECOM's subsidiary in Honduras, by establishing the SMS; (iii) enable use of the ArcGIS climate change toolbox in the ECOM systems in Nicaragua; (iv) create and implement mobile applications for better capture and management of farm data; (v) support the financial inclusion of women entrepreneurs; and (vi) transfer the knowledge created with this pilot project in Nicaragua to other ECOM subsidiaries in Latin America, and foster replication of this model by other MIF partners in other business sectors.

The loan/financing model

2.7 The project involves financing of up to US$30 million in subloans to farmers in Nicaragua.[20] The subloans, the value of which will range between US$8,000 and US$200,000 on average, will be made by Atlantic, which will finance its portion of the subloans (see Table 1). Under this project, the IDB, IFC, and other industry actors, if available, will make loans to Atlantic to supplement the financing of the subloans.

2.8 The IDB and IFC loans will improve credit through a first-loss guarantee from the Global Agriculture and Food Security Program (GAFSP), designed to help implement the promises made by the G-20 in 2009, as shown in Figure 1.

2.9 Atlantic (a subsidiary firm of ECOM), as the borrower and lender of record, will provide 10% of the financing (US$3 million) from ECOM; IFC and the IDB (SCF) will each provide up to 40% (US$12 million each) in

[20] The outbreak of coffee leaf rust in Central America makes it urgent to renovate the older coffee plantations. The IDB (through the Structured and Corporate Financing Unit (SCF) and the MIF), IFC (through its Investment Services and Loan Advisory Units), the Canadian Climate Fund for the Private Sector in the Americas (C2F), the Global Agriculture and Food Security Program (GAFSP), and Starbucks have forged a partnership to create the Coffee Renovation Facility (CRF), operation RG-X1220, a US$30 million line of credit for long-term (11 years) lending. The first pilot project under the CRF will finance the renovation of more than 5,000 hectares of leaf rust-affected coffee plantations in Nicaragua. The CRF will be expanded to US$100 million in the next three years, in order to include Mexico, Costa Rica, Honduras, and Peru. The line of credit combines long-term loans and technical assistance, which will allow a series of ECOM's coffee supply chains in the region to renovate their plantations and adapt to the effects of climate change.

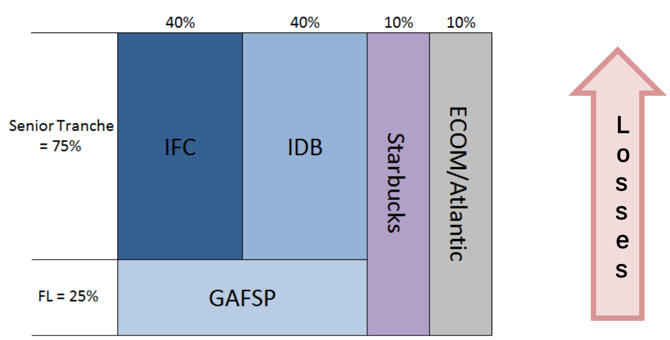
financing and will be lenders of record. Starbucks, as a co-lender, will provide 10% of the financing (US$3 million). In addition, GAFSP will cover up to 25% of the first loss on the IFC and IDB portion in Nicaragua (and later in Honduras), thereby considerably reducing the project's risk profile (see the structure below).

2.10 The loans to be provided by IFC and SCF will be approved in June 2015; the loan provided by the IDB (SCF) will be approved under the ATLANTIC operation (NI-L1088).

Table 1. ECOM Subproject 1 - Renovation of Coffee Plantations Exportadora Atlantic S.A.

Sources of financing	US$ (million)	%	Uses of financing	US$ (million)	%
Senior loans					
IDB	12.0	40%	Ground preparation, planting.	4.0	13%
IFC	12.0	40%	Inputs: seeds, fertilizers, fungicides	20.0	67%
Loans					
ECOM	3.0	10%	Transportation, technical cooperation	2.5	8%
Starbucks	3.0	10%	Contingencies	3.5	12%
Total	**30.0**	**100%**	**Total**	**30.0**	**100%**

Figure 1. Shared risk profile



2.11 IFC and the IDB (SCF) have approved their corresponding projects. Exportadora Atlantic, as lender of record, will identify borrowers from among its producers who meet the requirements and are in need of renovation; it will make and grant loans, provide periodic updates to borrowers, and offer technical assistance to farmers, in accordance with selection criteria agreed upon with the co-lenders. Given the risk inherent in long-term financing for farmers and in the local currency loan, the proposed financing structure divides the risk among various stakeholders.

a. **Operational details**. Atlantic will: (a) identify the borrowers who meet the requirements and evaluate their credit risk against the agreed selection criteria and the credit manual approved by the lenders; (b) produce project documentation and monitor disbursements, payments, and portfolio compliance; (c) restructure the subloans that are performing inadequately, execute the guarantees, and recover the unpaid loans; and (D) carry out the technical assistance activities in the field.

b. **Conditions on the subloans to producers**. The main selection criteria for the subloans to farmers include the following requirements: (a) that a farmer be an existing Atlantic supplier with a credit track record, approved in accordance with the ECOM credit manual; (b) a guarantee with a minimum asset coverage ratio (1.2x); (c) a financial analysis based on the entire plantation (renovated and non-renovated areas) indicating the capacity to repay the loans; and (d) participation in the parallel technical assistance program to mitigate the long-term payment risk.

2.12 The main parameters of the subloans will be: (i) a term of eight years, including a three-year grace period for payment of principal (from the first disbursement for each year of renovation under the project) of the investments in each crop year; (ii) the new subloans may be signed during the first three years of the project; (iii) at least 30% of subborrowers are farmers who own or operate coffee plantations of 12 hectares or less, and no less than 60% of the remaining aggregate balance of all subloans will be made to farmers who own or operate 50 hectares or more; (iv) the subloans will allow farmers to renovate only up to 30% of their coffee plantations, coinciding in general with the expected cash flow of farmers over the proposed term of eight years; and (v) farmers will not be obliged to sell their coffee to Atlantic.

C. Components of the MIF technical cooperation operation

Component I. Capacity building to provide long-term financing (MIF: US$20,000; Counterpart: US$20,000).

2.13 The objective of this component is to adapt Atlantic operations to the new (larger) scale, and to adjust the characteristics of its portfolio once the long-term loans are disbursed; while Atlantic already provides supplier credits to its producers under flexible terms, these are short-term working capital loans.

2.14 To improve Atlantic’s financial and credit capacities, the principal activities included in this component are: analysis and improvement of Atlantic’s credit risk assessment and monitoring capacities, in order to help it develop standard operating procedures and support the training of loan officers as well as technical advisors. Atlantic has developed an internal platform for producer finance (PROFIN), which will be adapted to include long-term financing considerations. In addition, MIF support will strengthen the platform in order to provide a portal for farmers that offers information on loans as well as market reports and general data.

2.15 To carry out the activities under this component, the project will engage the services of a consultant specialized in agricultural financing. The details of the consulting contract, the timing, and the estimated cost are included in the terms of reference that are part of the project files.

2.16 It is worth noting that the results of the activities under this component will be communicated to and taken into account by SCF to inform future disbursements under operation RG-X1220.

Component II. Technical assistance to enhance farmers' productivity.

2.17 The objective of this component is to enhance the technical capacity of the Atlantic team in the following areas:

(A) Strengthening of the Sustainable Management Services team (MIF: US$72,100; Counterpart: US$72,100)

2.18 This subcomponent seeks to replicate and strengthen Atlantic's SMS in Honduras, for the purpose of monitoring the conversion of coffee growers, planning and structuring visits by specialists, and verifying the traceability and certification of producers. The beneficiaries of these consulting services will be Honduran coffee growers to whom the SMS team provides services, i.e. approximately 1,500 producers. The potential beneficiary producers are located in such areas as Comayagua, Copan, Lempira, La Paz, Santa Bárbara, El Paraíso, and Ocotepeque,

2.19 The following SMS-related activities will be performed: (i) implement an SMS planning and target-setting model; (ii) develop a model for the retention, training, and conversion of coffee producers; (iii) redesign the structure and implement the SMS (visits by specialists); (iv) verify the traceability and certification of producers, and (v) design productivity indicators for producers.

(B) Update of the "farm module" web system and development of mobile applications in Android and iOS systems (MIF: US$40,000; Counterpart: US$40,000).

2.20 The objective of this portion of the project is to create and implement mobile applications for Atlantic technical personnel to use in gathering data from farmers. These data will help technical staff to monitor progress with plantation renovation and to centralize data in the Atlantic operating system.

2.21 The specific objective of the consulting contract is to ensure the "mobility" of the SMP information systems, so that this information is available in real time and relevant for immediate use. Specifically, the intention is that agricultural extension workers will have (prior) information from the producers in hand during their field visits, so that it can be used for making recommendations and implementing new farming practices. The analysis and viability of the information will in turn make for a much more profound and practical education process, allowing the farmer to incorporate and understand the advantages of the new practices.

2.22 The proposed activities are: (i) amend the modules on farm management, production costs, producer summary, and interactive graphs of the SMS Integrity web system; (ii) develop and implement the SMS sustainability standard in SMS Integrity; (iii) develop and implement the Android and iOS mobile applications of the SMS Integrity system; and (iv) train the SMS technical staff in the use of the mobile version of the SMS Integrity system.

(C) Georeferencing of the location of coffee producers (MIF: US$40,000; Counterpart: US$40,000)

2.23 This consulting assignment seeks in particular to achieve the georeferencing of the more than 4,000 small-scale producers who are part of the ECOM coffee supply chain in Nicaragua and Honduras. The georeferencing of farm locations will be adapted so that the data are available and integrated into the rest of ECOM's systems, for a more complete and efficient monitoring process. The information captured and processed for monitoring producers is the main element for reducing the risk in ECOM lending operations and ensuring that long-term loans to producers are sustainable over time.

2.24 The services of a consultant specialized in mobile information technologies will be contracted to carry out the activities under this component. The details of the consulting contract, timing, and estimated cost are included in the terms of reference that are part of the project files.

Component III. Monitoring and improvement of gender inclusion and climate change considerations (MIF: US$30,000; Counterpart: US$34,000).

2.25 This component has a dual objective: (i) to incorporate climate change assessment and technical assistance activities, and add project-related indicators to ECOM's existing administration tools through the geo-enabling of the ArcGIS geographic system with the SMS Integrity system; and (ii) to incorporate good practices with respect to gender, in particular by paying special attention to the needs of ECOM's women coffee-producing clients.

(A). The following activities are proposed for responding to climate change needs and in the quest for project sustainability: (i) develop a climate risk assessment tool to inform and monitor investment decisions in the coffee sector; (ii) link the ECOM systems with mapping and climate forecast applications in order to measure and monitor climate risks in the ArcGIS; and (iii) improve monitoring and evaluation capacities by defining and incorporating indicators of social, economic, and environmental performance to measure the project's impact.

2.26 This component will incorporate the results of the study by the International Center for Tropical Agriculture (CIAT), which provides forecasts for climate variables and how they will change over time: (a) mitigation of the investment risk level; and (b) decision-making by farmers.

(B) With respect to gender, this component will focus on empowering women coffee producers, so as to ensure that gender considerations are taken into account in all training provided by ECOM extension workers. This will enhance the effectiveness of the technical assistance with the resulting increase in productivity and fulfillment of ECOM's supply needs.

2.27 The gender-related activities under this component involve: (i) conducting an exhaustive gender analysis, which will focus on the following activities: (a) identify opportunities for women in the Atlantic value chain (for example, Atlantic indicated a preference for having women supervise the maintenance of seedlings in the nursery) and (b) provide support for women farmers in meeting the requirements for gaining access to loans from Atlantic. (ii) providing training on gender issues to ensure that Atlantic extension workers can adapt their methodology and their training and agricultural extension activities to the needs of men and women.

Component IV. Knowledge management and communication strategy (MIF: US$10,000; Counterpart: US$13,500).

2.28 This project will help reduce knowledge gaps in the program for financing and linking small-scale producers to high-value agricultural markets, by testing innovative financing models that combine credit with extension services provided by a private firm.

2.29 In particular, this project will test a new financing model whereby a specialized corporation (a coffee marketing firm) offers long-term credit to coffee growers, thereby satisfying a demand that is currently not being met by the standard financial sector (flexible long-term financing for agriculture). Through the technical cooperation operation, the institution will be strengthened to better serve the farmers as a technical agent and long-term credit agent.

2.30 The objective of this component is to systematize, document, and disseminate the experience and knowledge generated in this project, with a view to sharing the structure of the line of credit created for loans and enabling the lessons learned in this pilot project to be useful for pertinent audiences (see below).

2.31 The first user of this knowledge will be Atlantic, as a subsidiary of ECOM, since ECOM plans to extend the program to other countries (Honduras, Mexico, and Guatemala). The project's strategic audiences, in addition to the ECOM subsidiaries in Latin America, are: (i) private firms interested in developing their internal capacities for specialized long-term credit; (ii) financial institutions seeking to adapt or create new products and services geared to the agriculture industry; and (iii) nongovernmental organizations and multilateral organizations interested in replicating this experiment.

2.32 To meet the knowledge needs of these audiences, the project team proposes to create a case study that will spell out the steps to be followed to improve the capacity for making long-term loans in agriculture. This case will also introduce the audience to a climate assessment tool that is included as part of the risk mitigation strategy, as well as the steps for applying a gender perspective in technical training for participating farmers. In addition, this component will develop a strategy for replicating the initiative in other ECOM subsidiaries in Latin America.

2.33 Once a year, the executing agency will update the project technical file that contains basic information on the project, its challenges, the intervention strategy, and the outcomes.

2.34 Events and/or visits will be conducted to evaluate, capture, and disseminate the lessons learned upon completion of the technical assistance, assessing the impact on beneficiaries and Atlantic's progress and growth achieved through project implementation.

D. Project governance and execution mechanism

2.35 The project will be implemented by ECOM's subsidiary in Managua, known as Exportadora Atlantic Ltda. Exportadora Atlantic will designate a project coordinator who will be responsible to the Bank and the MIF for all project activities. Given the integration and coordination of ECOM/Exportadora Atlantic operations at the regional level, this person may be based in another country (i.e. Costa Rica), but will be responsible for coordinating communication with the technical, accounting, and financial departments of Exportadora Atlantic, as necessary. All the reports and terms of reference for the contracting of consulting services under this project will have to be agreed upon with the MIF official in Nicaragua. The consulting services may be conducted in Nicaragua, Honduras, or Costa Rica, as set out in the terms of reference.

E. Sustainability

2.36 One of the main goals of this project is to boost the sustainability of the coffee industry by encouraging producers, through loans and technical assistance, to renovate their leaf rust-afflicted plantations. Consequently, ECOM as the executing agency, the IDB group, and coffee producers will all have shared objectives for promoting project sustainability. The strengthening of Atlantic, as the executing agency, and of the producers themselves, through new monitoring systems and training, will guarantee the impact of the intervention and will help boost farmers' productivity and enhance their risk management.

2.37 One year prior to completion of the project a **sustainability workshop** will be conducted with all the entities involved in order to identify the measures needed to ensure continuity of project activities, once the funds are depleted.

F. Lessons learned from the MIF and other institutions reflected in the project design

2.38 The lines of credit, the conditions, and the technical assistance recommendations must be flexible. A credit package based on an oversimplified idea of the coffee plantation renovation process could be counterproductive, and could leave farmers highly indebted or could compromise their earning capacity over the short and medium terms. Nicaraguan producers who gained access to long-term credit declared that one of the reasons for the program's success was the effort that Atlantic put into adapting its loans to the individual needs of each producer.

2.39 Agricultural projects are most successful when a value chain approach is accompanied by practical training and documented supervision by the lender. In the project for rehabilitating and renovating cocoa plantations, carried out by the National Confederation of Dominican Cocoa Growers (CONACADO), practical supervision of technical training for farmers and a solid system of supervised conditional loans to monitor default rates were key factors for success, and they are relevant to the present operation. Market competitiveness can also be enhanced by adopting a value-chain approach that takes into account the entire value chain (including inputs, post-harvest processing, and logistics) instead of focusing solely on the production stage.

2.40 Fostering best practices through producer groups can increase the impact beyond the life of the project itself. Projects in which groups of producers participate have a stronger demonstration effect among other producers who may be more resistant to change. Producers who have received training can pass on their acquired knowledge and have other positive collateral effects, including the empowerment of producers and the development of social capital.

2.41 There is a demand for long-term credit, but the loan conditions must offer longer payment terms (exceeding five years) and they must be supplemented with technical assistance from the planning stage forward. A study conducted during the project revealed a glaring gap between credit supply and demand: while 85% of producers sought access to long-term credit, only 35% were successful in getting it. Because the loans will focus on renovation and it will take the newly planted coffee trees three or four years to start producing cherries, the organizations participating in the project recognize the importance of providing technical assistance at the planning stage (selecting appropriate coffee varieties, encouraging the adoption of best farming practices, etc.) in order to reduce the risk that farmers will default on their loans.

G. MIF additionality

2.42 **Nonfinancial additionality**. MIF experience with financial institutions can be transferred and will help the Atlantic team create the internal capacity to effectively administer long-term loans and expand its operational activities, resulting in a broader financial portfolio. The technical know-how developed through a series of agriculture and gender projects will also add depth to Atlantic's existing technical assistance program.

2.43 **Financial additionality**. The MIF financing will focus on addressing the executing agency's lack of experience in providing long-term financing. A failure in this respect would jeopardize the provision of financing that is so sorely needed by SMEs in Nicaragua (and that will be extended later to other countries of the region). Through participation in this initial pilot project, MIF financing will also be targeted at implementing innovative tools (such as the climate risk assessment tool) and adopting inclusive approaches (the gender perspective), which could become integral parts of the model and, if successful, could be replicated in other regions by other organizations.

H. Project outcomes

2.44 The expected outcome of the project is to expand the sustainable production of coffee in Nicaragua, through activities that will boost the capacities of Atlantic as a provider of long-term financing and technical assistance to its producers. The outcome indicators include the following:

- 560 coffee growers obtain financing through Atlantic for the renovation of their plantations, broken down by gender in Nicaragua (230500).
- 280 farmers adopt new practices when renewing a portion of their crops, broken down by gender in Nicaragua and Honduras (230100).
- Two products/services/tools developed and adapted for the benefit of firms and plantations (160100); (i) a long-term financing model for the coffee marketing corporation; (ii) development of a tool for climatic risk assessment and management.
- 5,000 hectares of land sustainably managed (240100).

- Increase in the yields per hectare of producers who gain access to credit (from 8 to 10 quintals per hectare to 20 to 30 quintals per hectare).

I. Project impact

2.45 The impact of the project will be to boost economic growth and employment for coffee growers so as to foster more sustainable and productive agriculture, as measured by the following impact indicators:

- 280 of 560 producers have boosted their yields through the renovation of coffee plants (330101).
- Average number of jobs created per year by firms and plantations (330300).
- A minimum of 15% of loan and technical assistance recipients are women producers (this is not a CRF indicator).

J. Systemic impact

2.46 The project will encourage systemic change by: (a) experimenting with a new financing model in which a private firm with a regional presence acts as lending agent, thereby expanding the project's scale and potential for replication; and (b) creating an investment partnership between five private actors and institutions (IDB, IFC, MIF, ECOM, and Starbucks), which will provide long-term loans through a model that can be expanded to other countries/crops/projects, diversifying and sharing risks as systemic agents of change and fostering innovation and economic development.

III. MONITORING AND EVALUATION STRATEGY

3.1 **Baseline**. The project baseline will be established once the ECOM long-term credit program is up and running in Nicaragua. This baseline is expected to include economic and social data on the beneficiaries, such as levels of income, sales and profits, health, nutrition, education, etc., since the executing agency requires this information in order to grant loans.

3.2 **Monitoring**. The executing agency will be responsible for collecting and reporting all the project indicators to the MIF within 30 days after the end of each six-month period, using the Project Status Report (PSR). The final PSR will give priority to the project results, project sustainability, and the findings from the final evaluation, including lessons learned, recommendations for future projects, and information from previous PSRs.

3.3 Extracts or evidence from the ECOM data system will be used to monitor farmers' progress, as well as the technical assistance consulting services intended to improve those systems.

3.4 **Evaluation**. The project budget includes funds for a final evaluation, to be performed when 95% of the MIF resources have been disbursed, or three months before the end of project execution, whichever comes first. The MIF will develop terms of reference for the external consulting services, as appropriate. The evaluation will consider: (i) the overall performance of the project and the degree to which project objectives have been achieved; (ii) the level of satisfaction among coffee growers who have received technical assistance and/or loans, in terms of the quality of the services provided by Atlantic; (iii) lessons learned and best practices to be considered in replicating the project in other entities seeking to implement similar projects; (iv) obstacles encountered by Atlantic and by the producers, and how they were overcome; and (v) barriers facing women in gaining access to finance, once Atlantic has implemented its new services and activities, and after the business training events.

3.5 The results of this evaluation and of the project in general will be presented in specialized meetings with organizations interested in the subject of sustainable coffee growing and long-term financing.

3.6 **Closing workshop**. In due course, the executing agency will organize a closing workshop, jointly with the other entities involved to evaluate the outcomes achieved, identify any additional steps needed to guarantee the sustainability of the actions initiated by the project, and to identify and disseminate lessons learned and best practices.

IV. COST AND FINANCING

4.1 The project has a total cost of US$546,305, of which US$326,705 (60%) will be provided by the MIF, and US$219,600 (40%) by the counterpart. The execution period will be 36 months, and the disbursement period, 42 months.

4.2 **Retroactive recognition of counterpart resources**. The Bank may recognize as a portion of the resources from the local contribution an amount equivalent to US$30,000 for expenses to adapt and improve the SMS, incurred prior to approval but after eligibility of the loan operation, provided the procedures established by the Bank were complied with.

Project Categories	MIF (US$)	Atlantic (US$)	Total (US$)	%
Component I	20,000	20,000	40,000	9.27%
Component II.A	72,100	72,100	144,200	33.40%
Component II.B	40,000	40,000	80,000	18.53%
Component II.C	40,000	40,000	80,000	18.53%
Component III	30,000	34,000	64,000	14.83%
Component IV	10,000	13,500	23,500	5.44%
SUBTOTAL before administrative expenses	**212,100**	**219,600**	**431,700**	**100.00%**
Administrative expenses	20,000		20,000	
Baseline and final evaluation	20,000	-	20,000	
Financial audit	20,000	-	20,000	
Contingencies	20,000		20,000	
SUBTOTAL	**292,100**	**219,600**	**511,700**	
Percentage	*57%*	*43%*		*100.0%*
Impact evaluation fund	14,605	-		
Agenda account + institutional strengthening	20,000	-		
Total	**326,705**	**219,600**	**546,305**	
Percentage	**60%**	**40%**		**100.00%**

V. EXECUTING AGENCY

5.1 Exportadora Atlantic, a subsidiary of the firm ECOM Agroindustrial Corporation (ECOM), will be the executing agency for this project and will sign the agreement with the MIF. The firm Exportadora Atlantic has been operating in the country for 18 years as a buyer, processor, and marketer of coffee and cocoa. As of December 2013, the firm had annual sales of close to US$88 million, assets of US$47 million, and a portfolio of loans to small coffee producers of US$16 million, most of which were short-term loans. ECOM, for its part, is a global commodities marketing firm with operations in 30 countries around the world. ECOM's portfolio of clients includes brand product manufacturers such as Nestlé, Starbucks, Hershey, Mars, Sara Lee, Kraft, and Folgers. In 2012 alone, the firm had sales of US$4.5 billion, 55% of which came from coffee.

5.2 ECOM supplies, processes, and sells commodities in sectors where smallholder producers predominate (for example, the coffee industry in Central America). In the specific case of coffee, ECOM has invested considerable resources throughout the value chain in many countries to boost the quality of coffee and to disseminate knowledge about best practices for profitable farming. Despite its efforts, the farmers in its supplier base have been affected by coffee leaf rust. Consequently, ECOM has been offering short-term loans in the form of seasonal credit to its coffee suppliers in Mexico, Guatemala, Honduras, and Costa Rica. In addition, ECOM has granted long-term loans, on a selective basis, for investments in infrastructure related to productivity or certification. ECOM’s lending operations are channeled through subsidiary firms. For purposes of this project in Nicaragua, Exportadora Atlantic Ltda. will act as lender to the farmers for renovation of their coffee plantations.

5.3 Exportadora Atlantic was a beneficiary and participant in MIF regional project RG-M1131, and specifically in operation ATN/ME-1101-RG for inclusive business development. That operation had a successful outcome, with a 31% increase in the yields of small coffee producers in the Atlantic chain. The 1,136 beneficiaries—smallholder coffee growers—were incorporated as suppliers into Atlantic’s coffee value chain, and received technical assistance, training, and, in some cases, loans. Atlantic introduced its Inclusive Business Program, which in the end reached 5,000 coffee and cocoa growers.

5.4 **Core business of the institution**. ECOM is primarily a commodities marketing and processing company, and not a primary producer, brand product seller, or financier. Every ECOM operation in each country is independent. ECOM's motivation is to expand its market share, boost coffee production, and serve the interests of its clients. In 2012, its business turnover exceeded US$4.5 billion.

5.5 In addition to ECOM, other important partners are participating in the project: the IDB, the GAFSP, IFC, and Starbucks. Starbucks has substantial knowledge of the coffee industry (varieties in demand, flavor parameters, etc.) and has demonstrated a strong interest in contributing its knowledge base to the program. The Canadian Climate Fund (through the IDB) has also expressed interest in participating in future replications and in providing a first-loss guarantee similar to that offered by GAFSP for countries that do not belong to the International Development Association (IDA) (approval of its first committee was obtained).

VI. PROJECT RISKS

6.1 The project risks identified are as follows:

6.2 **Inherent risks related to the coffee growing business.** The certified leaf rust-resistant seeds that will be used to renovate the plantations are in short supply, meaning that the availability of seeds for the project is uncertain. However, according to IFC calculations, the project can use half of the total amount of certified seeds in the country (Nicaragua) only as of the third year (out of the loan instrument's 11 years), and rust-resistant varieties can also be imported from Costa Rica.

6.3 **The project's credit risk**. The project’s credit risk is comprised of the following risks inherent in the coffee growing business: (i) price risk: models of breakeven prices under the loan criteria, including possible commitments with intermediaries, will have to be developed; (ii) demand risk: this will be mitigated by possible commitments with intermediaries and credit criteria; (iii) production risk: this includes climate change, disease, and producer practices that lead to low productivity. These will have to be mitigated through a parallel program of technical assistance administered by ECOM with financing from the MIF and other donors; (iv) portfolio loss rate assumption: portfolio losses of up to 25% will be absorbed by GAFSP, C2F, and, in part, ECOM, before they have any impact on the IDB and IFC. Only very limited data are available on the historic rate of loss for this type of loan. Consequently, first-loss protection for the IDB and IFC will have to be high in comparison with loss rates on short-term loans in the agriculture sector, which range between 1% and 4% of portfolios (to be confirmed during due diligence). The ongoing monitoring of the ECOM loans, which is also a way of ensuring against a portion of the project risk, will guarantee proper use of procedures and participation by the end beneficiaries in the technical assistance program.

VII. Environmental and Social Aspects

7.1 Given the nature of the subloans under the IDB/SCF-IFC line of credit, which includes the Atlantic subproject for plantation renovation loans, the direct impacts and risks of an environmental, social, health, and safety (ESHS) or occupational nature will be minimal to moderate. Beginning with the Atlantic subproject, the Bank, as part of the due diligence process, will analyze the ESHS aspects of the lending practices of each sponsor for the small-scale coffee plantations, as well as its system of environmental and social risk management, in order to assess management capacity to resolve environmental and social problems and provide advice to farmers. In the case of ECOM, the first subproject under this line of credit, an early indication suggests a solid management capacity for resolving environmental and social problems and providing advice to farmers.

VIII. Fulfillment of Milestones and Special Fiduciary Arrangements

8.1 **Disbursement by results and fiduciary arrangements**. The executing agency will undertake to respect the MIF’s standard arrangements relating to disbursement by results, procurement, and financial management. Detailed information on the executing agency’s procedures is available in Annex IV to the document.

IX. Access to Information and Intellectual Property

9.1 **Access to information**. As this project contains sensitive information on ECOM's business strategy, this document must be kept confidential.