PROJECT INFORMATION DOCUMENT (PID)
APPRAISAL STAGE

Report No.: PIDA26967

Project Name	MX: Expanding Rural Finance (P153338)
Region	LATIN AMERICA AND CARIBBEAN
Country	Mexico
Sector(s)	General agriculture, fishing and forestry sector (20%), SME Finance (40%), Other non-bank financial intermediaries (40%)
Theme(s)	Other Financial Sector Development (80%), Other rural development (20%)
Lending Instrument	Investment Project Financing
Project ID	P153338
Borrower(s)	Financiera Nacional de Desarrollo Agropecuario, Rural, Forestal y Pesquero
Implementing Agency	Financiera Nacional de Desarrollo Agropecuario, Rural, Forestal y Pesquero
Environmental Category	F-Financial Intermediary Assessment
Date PID Prepared/Updated	30-Jul-2015
Date PID Approved/Disclosed	30-Jul-2015
Estimated Date of Appraisal Completion	21-Aug-2015
Estimated Date of Board Approval	05-Nov-2015
Appraisal Review Decision (from Decision Note)	The July 15 Decision Review Meeting did authorize the team to appraise and negotiate.

I. Project Context

Country Context

Poverty rates are much higher in rural than urban areas of Mexico. States vary widely in wealth, and urban centers are dynamic while rural areas remain isolated. Poor rural infrastructure has inhibited significant advances in agricultural production. Extreme poverty in 2012 was more than double in rural areas than in urban areas (30.9 percent vs. 12.9 percent). Measurements of asset poverty (moderate poverty) according to national poverty lines also showed a stark divide-- 63.6 percent rural poor in 2012, well above the urban poverty headcount of 45.5 percent.

Agriculture employs an important share of the population, but is contributing less than other sectors to economic growth. Between 1999 and 2011 agriculture grew by an average of 1.6 percent while other sectors grew 3.7 percent. The agricultural sector plays an important social role given the importance of agriculture income in the total income of the rural poor. Agriculture's share of GDP was 3.5 percent in 2013, while its share of employment was 13 percent, a reflection of the relatively low productivity of the agricultural sector.

Sectoral and institutional Context

Despite a stable macroeconomic framework and a series of market-enhancing reforms, the financial market fails to provide adequate access to key segments in Mexico. A vibrant financial sector that identifies and funds viable business opportunities is an important micro-economic foundation for shared prosperity by supporting increased incomes while helping to manage risks.

Mexico's financial sector is small, and by international benchmarks rural credit is poorly developed. Credit to the private sector as a percent of GDP in Mexico was 23 percent in 2014, less than half the Latin America and the Caribbean (LAC) average of 47 percent and the upper middle income country average of 49 percent. According to the 2014 FINDEX data, 6 percent of adults in rural areas borrowed from a financial institution in the last year, the same level as in 2010. This is well below the 11 percent of adults borrowing in rural areas in Latin America and the Caribbean. Bank branches are present in 42.7 percent of rural municipalities, in comparison to 99.5 percent of urban municipalities. Rural lending models often require frequent repayment and are can be ill-suited for the harvest dependent agricultural cycle.

A small part of total credit goes to small enterprises few of which have loans or use bank finance for working capital. National data (by the National Banking and Securities Commission, CNBV) suggest that only 20–25 percent of all micro, small and medium-size enterprises (MSMEs) use bank credit. Commercial bank lending tends to be short term, costly and increasingly focused on the more profitable consumer credit.

The lack of rural enterprise credit depresses rural economic activity. A study by Love and Sanchez (World Bank, 2009) found that credit constraints were pervasive in the Mexican rural economy, limiting the investments and growth of rural enterprises. Preliminary findings from a 2014 QFPD/ World Bank survey of 1,000 farmers in Tlaxcala found that farmers are not using key inputs such as fertilizers that would improve their productivity with the primary reason cited for lack of use being lack of finance. Mexico's National Development Plan (2013-18) emphasizes a productive, profitable, and competitive primary sector.

The Government assigned a priority to address the lack of credit including through its DFIs as part of the 2014 financial reform. The reform promoted lending by private intermediaries as well as by DFIs. Mexico has six development banks, six government trusts and four development finance agencies to support key sectors, such as the rural economy. DFIs address access to finance gaps through the provision of financial services (both loans and deposits), finance, partial credit guarantees (PCGs), and technical assistance to NBFIs. The proposed borrower for this operation, FND, is one of these agencies.

FND supports access to finance for the rural economy both directly and by financing and strengthening small credit institutions. FND aims to support rural financial access through market-friendly instruments that encourage private sector activity including to agriculture, fisheries, forestry and rural commerce with the goal of improving productivity and improving the quality of life of the rural population. FND was known until 2014 as Financiera Rural. Its establishment was supported by the World Bank when Banrural was liquidated in 2002.

The Government of Mexico and FND have requested this project to support FND’s expansion of rural finance. FND is currently by law allowed to borrow only from domestic public institutions and IFIs. The IFI involvement will help expand activities based on good lending practices and leveraging global lessons. The successful implementation of FND’s strategy to expand its outreach requires an efficient operational interaction with PFIs, an effective approach to assessing and monitoring the financial performance and capacity of PFIs, and effective technical assistance to support PFIs.

II. Proposed Development Objectives

The project’s development objective is to expand the availability of finance to the rural economy.

III. Project Description

Component Name

Component 1: Expanding Credit for Rural MSMEs:

Comments (optional)

US$365 million are to be disbursed through PFIs (Component 1A). US$10 million can be applied to pilot new MSME financial solutions either through PFIs or through direct lending by FND (Component 1B).

Component Name

Component 2: Strengthening Institutional Capacity for Sustainable Rural Finance

Comments (optional)

This component will support the modernization of FND's core banking system to improve the delivery of rural financial services (Component 2A). Counterpart financing will be used to fund institutional strengthening activities for rural financial institutions (Component 2B).

IV. Financing *(in USD Million)*

Total Project Cost:	405.00	Total Bank Financing:	400.00
Financing Gap:	0.00		

For Loans/Credits/Others	Amount
Borrower	5.00
International Bank for Reconstruction and Development	400.00
Total	405.00

V. Implementation

FND is the borrower and the implementing agency for the proposed project. For implementation of the line of credit component (1A), the Borrower (FND) will enter into Subsidiary Financing Agreements with eligible PFIs to on-lend to rural MSMSEs through loan agreements.

VI. Safeguard Policies (including public consultation)

Safeguard Policies Triggered by the Project	Yes	No
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	✖	
Physical Cultural Resources OP/BP 4.11		✖
Indigenous Peoples OP/BP 4.10	✖	
Involuntary Resettlement OP/BP 4.12		✖
Safety of Dams OP/BP 4.37		✖
Projects on International Waterways OP/BP 7.50		✖
Projects in Disputed Areas OP/BP 7.60		✖

Comments (optional)

VII. Contact point

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