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Report No: 33165-BR

PROJECT APPRAISAL DOCUMENT

ON A

PROPOSED LOAN

IN THE AMOUNT OF US\$ 35.0 MILLION

TO THE

STATE OF MINAS GERAIS

WITH THE GUARANTEE OF

THE FEDERATIVE REPUBLIC OF BRAZIL

FOR A

RURAL POVERTY REDUCTION PROJECT

August 5, 2005

Brazil Country Management Unit
Environmentally and Socially Sustainable Development Sector Management Unit
Latin America and Caribbean Region

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CURRENCY EQUIVALENTS

(Exchange Rate Effective June 30, 2005)

Currency Unit = Real (R\$)
R\$1.00 = US\$0.4255
US\$1.00 = R\$2.3504

FISCAL YEAR

January 1 – December 31

ABBREVIATIONS AND ACRONYMS

BB	-	Bank of Brazil
BN	-	Bank of the Northeast
CA	-	Community Association
CAS	-	World Bank Country Assistance Strategy
CDD	-	Community-Driven Development
EMATER-MG	-	Minas Gerais State Company for Technical Assistance and Rural Extension
FUMAC	-	Municipal Community Scheme
GOB	-	Federal Government of Brazil
HDI	-	UN Human Development Index
IBGE	-	Brazilian Institute for Geography and Statistics
IDENE	-	<i>Instituto de Desenvolvimento do Norte e Nordeste de Minas Gerais/</i> Minas Gerais Northern and Northeastern Development Institute
IEF	-	<i>Instituto Estadual da Floresta</i> State Forestry Institute
MC	-	Municipal Council
MIS	-	Management Information System
NCB	-	National Competitive Bidding
NGO	-	Non-Governmental Organization
NRDP/PAPP	-	Northeast Rural Development Program
PAC	-	State Community Scheme
PPA	-	Multi-year Government Investment Plan
PRONAF	-	Brazilian Federal Program to Support Family Agriculture
R- NRDP	-	Reformulated Northeast Rural Development Program
RPAP	-	Rural Poverty Alleviation Project/Program
RPRP	-	Rural Poverty Reduction Project/Program
SEBRAE	-	Brazilian Agency for Micro and Small Enterprise Assistance
SEDVAN	-	<i>Secretaria de Estado Extraordinário para o Desenvolvimento dos Vales do</i> <i>Jequitinhonha e Mucuri e Norte de Minas Gerais/</i> Special State Secretariat for the Development of the <i>Jequitinhonha Mucuri</i> Valleys and Northern Minas Gerais
SEPLAG-MG	-	<i>Secretaria de Estado de Planejamento e Gestão/</i> Minas Gerais State Secretariat of Planning and Management
SOE	-	Statement of Expenditures
STU	-	State Technical Unit
TA	-	Technical Assistance

Vice President:	Pamela Cox
Acting Country Director:	Letitia A. Obeng
Sector Director:	John Redwood
Task Team Leader:	Luis O. Coirolo

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**BRAZIL
Rural Poverty Reduction Project - Minas Gerais**

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BRAZIL
Rural Poverty Reduction Project - Minas Gerais¹

Date: August 5, 2005 Acting Country Director: Letitia A. Obeng Sector Director: John Redwood	Team Leader: Luis O. Coirola Sectors: Other social services (85%); Sub-national government administration (10%); Central government administration (5%) Themes: Access to urban services and housing (P); Rural non-farm income generation (P); Rural markets (P); Participation and civic engagement (S)
Project ID: P052256 Lending Instrument: Specific Investment Loan	Environmental screening category: Category B

Project Financing Data

<input checked="" type="checkbox"/> Loan	<input type="checkbox"/> Credit	<input type="checkbox"/> Grant	<input type="checkbox"/> Guarantee	<input type="checkbox"/> Other:
For Loans: Total Bank financing (US\$m.): 35.00 Proposed terms: FSL				

Financing Plan (US\$m)

Source	Local	Foreign	Total
State Government	7.6	0.0	7.6
Community Associations	4.2	0.0	4.2
IBRD	0.0	35.0	35.0
Total:	11.8	35.0	46.8

Borrower: State of Minas Gerais/ Secretary of State Planning and Management (SEPLAG/MG) Rua Tomas Gonzaga, 686 5o. Andar - Lourdes Belo Horizonte Minas Gerais Brazil 30180.140 Fax: 55-31-3290-8259
Responsible Agency: Instituto de Desenvolvimento do Norte e Nordeste de Minas Gerais (IDENE) Rua Rio de Janeiro, 471 - Centro Belo Horizonte Minas Gerais Brazil 30.160-040 Fax: 55-31-2129-8114

Estimated disbursements (Bank FY/US\$m)

FY	2006	2007	2008	2009	2010
Annual	4.30	8.80	10.20	9.00	2.70
Cumulative	4.30	13.10	23.30	32.30	35.00

Expected effectiveness date: September 30, 2005	Expected closing date: July 31, 2010
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¹ Known in Brazil as *Projeto de Combate a Pobreza Rural da Região Mineira do Nordeste "PCPR- 1a Fase"*

Does the project depart from the CAS in content or other significant respects? <i>Ref. PAD A.3</i>	<input type="checkbox"/> Yes <input checked="" type="checkbox"/> No
Does the project require any exceptions from Bank policies? <i>Ref. PAD D.7</i>	<input type="checkbox"/> Yes <input checked="" type="checkbox"/> No
Have these been approved by Bank management?	<input type="checkbox"/> Yes <input type="checkbox"/> No
Is approval for any policy exception sought from the Board?	<input type="checkbox"/> Yes <input checked="" type="checkbox"/> No
Does the project include any critical risks rated "substantial" or "high"? <i>Ref. PAD C.5</i>	<input type="checkbox"/> Yes <input checked="" type="checkbox"/> No
Does the project meet the Regional criteria for readiness for implementation? <i>Ref. PAD D.7</i>	<input checked="" type="checkbox"/> Yes <input type="checkbox"/> No

Project development objective *Ref. PAD B.2*

The project aims to assist the State of Minas Gerais to reduce high levels of rural poverty by: (a) improving well-being and incomes of the rural poor through better access to basic socio-economic infrastructure and services and support for productive activities, using proven community-driven development techniques; (b) increasing the social capital of rural communities to organize collectively to meet own needs; (c) enhancing local governance by greater citizen participation and transparency in decision-making, through creation and strengthening of community associations and Municipal Councils; and (d) fostering closer integration of development policies, programs and projects at the local level, by assisting Municipal Councils to extend their role in seeking funding, priority-setting and decision-making over resource allocation, and by assisting the government to measure the efficiency and impact of its own programs to reduce rural poverty in rural space.

Project description *Ref. PAD B.3.a*

Component 1 (Community Subprojects) provides matching grants to rural community associations to finance approximately 1,860 socio-economic infrastructure and productive subprojects (up to US\$50,000 each) identified by these groups as priority investments that will improve community well-being and benefit around 93,000 families.

Component 2 (Institutional Development) will finance technical assistance and training to increase capacity of implementing entities including MCs, community associations and the STU.

Component 3 (Administration, Supervision, Monitoring and Evaluation) will finance incremental costs (excluding salaries) of project administration and coordination, including supervision, monitoring and impact evaluation.

Which safeguard policies are triggered, if any? *Ref. PAD D.6*

Environmental Assessment (OP/BP/GP 4.01)

Significant, non-standard conditions, **if any**, for:

Loan effectiveness:

Signing of a subsidiary agreement, satisfactory to the Bank, between the State of Minas Gerais and IDENE.

A. STRATEGIC CONTEXT AND RATIONALE

1. Country and sector issues

The northern half of the State of Minas Gerais shares many of the physical and social characteristics of the Brazilian Northeast region, among them the high incidence of rural poverty, which is concentrated in the regions known as *Norte de Minas*, *Vale do Jequitinhonha* and *Vale do Mucuri*. Statewide, some 631,000 rural households earn less than US\$2.50 per day – or less than US\$1 per person per day – and most of these households are located in the proposed project area. Among these poor rural households, approximately 50 percent lack piped water supply, about 35 percent are without sanitation services, and 25 percent have no access to electricity, compared, respectively, with 3, 1 and 1 percent for all urban households in Minas Gerais, and 44, 30 and 19 percent for rural Brazil as a whole. GDP per capita in the proposed project area is less than half that of Minas Gerais as a whole, infant mortality is 29 per cent above the average level for the State, and the percentage of population without formal education is 86 percent above the corresponding statewide figure.

Bank-financed, community-driven development (CDD) in Northeast Brazil began in 1985 under a component of the Northeast Rural Development Program (NRDP) which financed small-scale, demand-driven productive investments for poor rural communities. The component - *Apoio às Pequenas Comunidades Rurais* (APCR) - was the only NRDP activity to disburse effectively and achieve positive results on the ground. In late 1993, drawing on lessons from the APCR and similar schemes elsewhere in Latin America, the NRDP was reformulated into a full-scale, community-based development program (R-NRDP), which featured decentralized decision-making and community counterpart financing responsibilities. Subsequently, eight Northeast State Governments scaled-up the field-tested R-NRDP and ushered in the follow-on Rural Poverty Alleviation Projects (RPAPs), beginning in 1995/96, succeeded by a third generation of similar sub-national projects – the Rural Poverty Reduction Program (RPRP), now operational since 2001. The RPRP is consolidating gains made under the previous generations of CDD projects, while simultaneously integrating activities of the participatory project Municipal Councils with the local government and, through more focused investment linked to the Human Development Index (HDI) and integrated with other State- and Federal-level interventions, promoting asset accumulation of the poorest. Subsequent evaluation of these CDD projects confirms that not only has it been an effective model for rural poverty reduction, but also developed into a key tool of the Northeast States for promoting organized decentralization, local development and community participation.

The cumulative experience of the Northeast Program (i.e., R-NRDP, RPAP and RPRP) provides a springboard for the Government of Minas Gerais to advance to a new level of development impact in the rural space. Besides improving the well-being of a much larger number of rural communities through better access to essential infrastructure and services, the main contribution of the proposed Rural Poverty Reduction Project (RPRP) will be to test strategies to extend the reach of the Municipal Councils, by progressively involving them in proactively seeking funding from and participating in priority-setting and decision-making on resource allocation over a much wider range of Federal, State and local programs. Currently, a large share of the resources available under those programs either do not reach the rural poor, are directed to activities that are not among the highest priorities of the beneficiaries, or are not delivered in a cost-effective manner. Successful execution of the RPRP will help to realign and better integrate these programs, thereby leveraging the overall impact of public resources directed towards rural poverty reduction. A surprising 30% of the more than 1,500 project municipal councils established to date across the Northeast now participate in discussions about broader municipal investment needs, thus helping to shape a framework for development of the greater municipality. Notably, about 25% of all the community associations are now using community assets and social capital to leverage financing from sources beyond the Northeast Program.

The R-NRDP in Minas Gerais covered the municipalities of the northern part of Minas Gerais, belonging to the region known as *Norte de Minas*. Recently, the project area was further extended to include some municipalities in the similarly poor regions of *Vale do Jequitinhonha* and *Vale do Mucuri*, located in the northeastern part of the State. In Minas Gerais, the R-NRDP was not followed by a Rural Poverty Alleviation Project as other Northeast States. The results and the experience gained from the implementation of the RPAPs in the Northeast States are relevant, however, to Minas Gerais and were used in the design of the new RPRP for the State. Notwithstanding the absence of a Bank-supported project under the Northeast Program in Minas Gerais since the closing of the R-NRDP, the State has remained engaged in CDD through (i) its participation in the Bank-financed Land-Based Poverty Alleviation Project (*Crédito Fundiário*), (ii) continued involvement of the State team in Northeast Program events and (iii) the implementation of some State-financed poverty reduction activities following the CDD methodology. Furthermore, the Government of Minas Gerais kept together the same technical team that worked in the execution of the R-NRDP; this same team will be responsible for the implementation of the new RPRP.

As part of its efforts to reduce rural poverty, the Federal Government has agreed to support the RPRP in the Northeast region, including the State of Minas Gerais. Specifically, the Federal Government has agreed on aggregate borrowing amounts, which it will guarantee for each state, with half to be borrowed in an initial project and the balance for a second-stage operation after successful completion of the first. The proposed loan to Minas Gerais would support that state's initial RPRP project. Similar projects are now under implementation in the states of Bahia, Ceará, Paraíba, Pernambuco, Piauí, Rio Grande do Norte and Sergipe.

The project supports a CDD approach to rural poverty reduction, and fosters decentralization through the promotion of strong local participation in decision-making and resource allocation. The existing policy and institutional framework in Brazil is supportive of these objectives and is not expected to inhibit project viability. Rather, the need at this stage is to scale up implementation of successful approaches thus far tested under the Northeast Program, both expanding geographic coverage and extending the reach and potential impact of Municipal Councils on rural poverty reduction.

2. Rationale for Bank involvement

As the principal international partner engaged in a sustained, long-term partnership with the Brazilian Government to address rural poverty issues in the Northeast, the Bank is particularly well-placed to support expansion of community-based rural development efforts in the region. The Bank contributes its experience under the successful R-NRDP, RPAP and RPRP projects in the Northeast – which have served as a template in the design of this new operation. Bank participation will ensure that international experience with past and ongoing community-driven programs is incorporated into project design and that sound international quality standards of monitoring, evaluation and impact assessment are applied.

An especially important feature of Bank value-added in Minas Gerais will be its ability to facilitate closer local integration of a wide spectrum of programs aimed at rural poverty reduction. The Bank is well-positioned to help forge these links, not only because of its direct role in financing the Northeast Program and developing the participatory Municipal Council mechanism, but also because of its involvement in other important sectoral programs relevant to rural poverty reduction (irrigation, agricultural research, land reform, education, municipal development) and the many opportunities for policy dialogue and consensus building in the context of its fairly active program of collaborative research and analytical work on poverty and rural development issues in Brazil.

As the program has evolved and processes become increasingly refined, the Bank's role has also progressed. Under the RPAPs, the Bank assumed the critical role of catalyst, serving as an independent monitor and evaluator of program performance, helping to ensure that processes were complied with, that

undue interference was minimized, and that lessons learnt during implementation were captured and applied. Under the new program, where processes have already been well-developed, it is envisaged that the role of the Bank will shift once again to focus increasingly on strengthening the linkages between community organizations, their representative councils, local government, other public programs, financial institutions and markets. By serving as facilitator, the Bank can play a critical role in formalizing municipal councils as key partners in the local development process, be catalytic in helping to consolidate the participatory and transparent resource allocation at the local level (including the use of information technologies), and ensure that these processes continue beyond the life and scope of the project when external support will be gradually phased out or redirected to other aspects of poverty reduction.

Several strategic choices have been made in designing the project, such as:

- *Stimulating improvements in both social welfare and local economic activity.* A key constraint to rural development in Minas Gerais has been the lack of opportunity to intensify smallholder agriculture, and stimulate growth of commercial agriculture, downstream processing and other non-farm activities. This project will diversify income and employment opportunities in a range of farm and non-farm endeavors through support for productive activities, technical assistance and investment in social and economic infrastructure/services, identified by communities as most relevant for their well-being.
- *Community-based approach:* The community-based approach, when compared to similar investments executed by traditional public sector entities, has proven to be cost-effective, more responsive to local priorities and to offer better prospects for sustainability.
- *Integration of programs, policies and actions at the local level.* Adopting a decentralized approach that focuses decision-making at the local level has helped to overcome the complexity problems of earlier failed attempts at integrated rural development. A growing number of Municipal Councils in Northeast States are proactively seeking funding from and participating in decision-making over non-project sources of finance. Under the new project, Councils will be further encouraged through training and technical assistance to expand their input into broader local planning, with a view to achieving better integration of policies and programs and improving the impact of public resources available for poverty reduction. Integration will also be effected through partnerships between the STU, Federal, State and Municipal agencies, civil society and Municipal Councils to improve the planning and execution of community investments, deliver TA and training, leverage additional funding, promote mobilization and organization, and bring strategic resources to the project, all of which are crucial to rationalize human and financial resources for poverty reduction in an era of increasing fiscal austerity. The establishment of the Special Secretariat for the Development of *Vales do Jequitinhonha e Mucuri e Norte de Minas Gerais* (SEDEVAN) further catalyzes these efforts of local-level integration.
- *Targeting of resources.* One of the most important benefits of the project will come from community experience gained through managing an investment subproject and participating in decision-making in a Municipal Council. For that reason, a minimum level of funding has been allocated to each participating rural municipality in the project area, with proportionally higher levels targeted to the poorest municipalities with the greatest needs, as determined by the United Nations Human Development Index (HDI).
- *Environmental preservation and protection.* Sustainability of project-financed assets and of rural communities' physical "space" can be strengthened by actions which ensure appropriate subproject design and environmental oversight. The proposed project will provide access to environmental expertise via an in-house environmental specialist and partnerships for training and education activities through the State Forestry Institute (IEF) – responsible for environmental preservation and protection – and EMATER-MG – responsible for agricultural extension – to build awareness of sound natural resources management and environmental practices into community development agendas.

- *Rigorous monitoring and evaluation.* The predecessor R-NRDP project made substantial provision for piloting, testing, and M&E, and this was extremely helpful for continuous refinement of processes. Under the new project, an enhanced MIS and an evaluation framework based on best-practice will be implemented to measure impact through independently executed, repeater surveys of beneficiaries and control group panels, with a view to maximizing poverty reduction impact.
- *Information Technology.* The new project will use information technology to increase transparency by making available, in real time, information about the project itself, as well as using the Internet to connect communities directly to markets, both in Brazil and internationally.

B. PROJECT DESCRIPTION

1. Lending instrument

Total project cost is estimated at US\$46.8 million. A Specific Investment Loan (SIL) of US\$35.0 million is recommended.

2. Project development objective and key indicators

The project aims to assist the State of Minas Gerais to reduce high levels of rural poverty by: (a) improving well-being and incomes of the rural poor through better access to basic socio-economic infrastructure and services and support for productive activities, using proven community-driven development (CDD) techniques; (b) increasing the social capital of rural communities to organize collectively to meet own needs; (c) enhancing local governance by greater citizen participation and transparency in decision-making, through creation and strengthening of community associations and Municipal Councils; and (d) fostering closer integration of development policies, programs and projects at the local level, by assisting Municipal Councils to extend their role in seeking funding, priority-setting and decision-making over resource allocation, and by assisting the government to measure the efficiency and impact of its own programs to reduce rural poverty in rural space.

Key performance indicators include: (i) number of families benefited from subproject investments; (ii) increase in social welfare of rural communities; (iii) increase in social capital index of project Municipal Councils; (iv) number of Municipal Councils participating in priority-setting and decision-making on resource; (v) allocation of project and non-project funded development activities; (vi) increase in total project and non-project financing allocated through Municipal Council mechanism; and (vii) number of communities graduated from the program and successfully linked to other financing sources.

3. Project components

Component 1 – Community Subprojects – provides matching grants to rural community associations to finance approximately 1,860 socio-economic infrastructure and productive subprojects (up to US\$50,000 each) identified by these groups as priority investments that will improve community well-being and benefit around 93,000 families. After approval of subprojects by the State Technical Unit or project Municipal Councils, project funds are disbursed directly to the community associations, which manage subproject implementation, operation and maintenance. This component includes three subprograms – PAC, FUMAC and FUMAC-P.

- *State Community Schemes (PAC).* Under the PAC subprogram, rural communities submit their investment proposals directly to the State Technical Unit (STU), which screens and approves them and releases funds to the beneficiary associations. Under the proposed project, PAC will be used to respond to demands from communities in municipalities where a Municipal Council has not yet been created. It will also be retained as an option to which communities may occasionally resort in cases

where Municipal Councils are not functioning properly. The PAC scheme is expected to assist towards the creation of social capital. To achieve this, the STU will enroll the support of community associations who have benefited from PAC subprojects to help other communities to organize their own associations and to assist in the process of forming a Municipal Council in the municipality. The mechanics of this process are detailed in the project Operational Manual. PAC is expected to account for about 23 percent of the component cost.

- *Municipal Community Schemes (FUMAC).* Under FUMAC, decision-making on investment proposals is delegated by the State to project Municipal Councils, composed of community members and representatives of civil society and municipal authorities. A majority of Council voting members (i.e., at least two-thirds) are potential project beneficiaries or representatives of civil society. The Municipal Councils discuss and seek to build consensus on priorities and approve community proposals, in the context of an indicative annual budget amount determined by the State Technical Unit. After the Councils' recommendations are reviewed by the STU for consistency with guidelines in the project Operational Manual, funds are disbursed directly to the community associations. This subprogram will account for about 72 percent of total community subproject costs.
- *Pilot Municipal Community Funds (FUMAC-P).* The FUMAC-P is a more decentralized variant of FUMAC piloted under the RPAP with high-performing Municipal Councils, and will be tested in the Minas Gerais RPRP. The STU establishes an annual budget envelope, according to a distribution formula based on clear and measurable criteria (i.e., IDH). Based on this budget, Municipal Councils submit an Annual Operating Plan (*Plano Operativo Anual*) for STU review. Upon approval, funds are transferred to the Council, which is then responsible for managing its distribution to community associations and assisting them with implementation of subprojects. It is expected that under the new RPRP project, about 5 percent of total component resources would be used under the FUMAC-P subprogram.

Component 2 - Institutional development - will finance technical assistance and training to increase capacity of implementing entities including Municipal Councils, community associations and the STU. It also includes funds for technical assistance to support Minas Gerais in addressing state modernization, particularly in promoting the integration of state-level policy for poverty reduction and strengthening the management capacity of the state to better monitor the impact of its public expenditures to reduce poverty in the rural space. This component will also support the expansion of information technology to increase transparency and to connect communities and Municipal Councils to markets.

Component 3 - Project administration - will finance incremental costs (excluding salaries) of project administration and coordination, including supervision, monitoring and impact evaluation.

Component	Indicative Costs, Incl. Cont. (US\$M)	% of Total	Bank Financing (US\$M)	% Bank Financing
1. Community subprojects	40.70	86.97%	30.50	87.14%
(i) PAC	9.20	19.66%	6.90	19.71%
(ii) FUMAC	29.10	62.18%	21.80	62.29%
(iii) FUMAC-P	2.40	5.13%	1.80	5.14%
2. Institutional Development	3.30	7.05%	3.30	9.43%
3. Administration, Supervision, Monitoring and Evaluation	1.40	2.99%	0.85	2.43%
Front-end Fee	0.35	0.75%	0.35	1.00%
TOTAL	46.80	100.00%	35.00	100.00%

4. Lessons learned and reflected in the project design

Decentralization of investment decision-making and implementation from federal to state and local governments and to community organizations ensures efficient program administration and superior outcomes. Experience in Northeast Brazil shows that decentralized community-driven approaches can reduce bureaucracy, eliminate administrative bottlenecks and reinforce accountability for project performance by placing decision-makers near beneficiaries. Under the new project the institutional structure will be devolved, with delegation of duties to Municipal Councils and utilization of STU regional offices to promote more responsive and local level monitoring, data collection, coordination, and supervision.

Participation by beneficiaries in the selection, financing, execution, and O&M of subprojects has ensured in the experience of the Northeast Program that investments meet genuine community needs, generating cost savings, and increasing community 'ownership', thus leading to improved sustainability of investments. This methodology started with the R-NRDP in 1993, was further developed in the Northeast States that executed RPAP projects, and will be applied under the new project in Minas Gerais.

Poverty targeting mechanisms that are simple, verifiable and based on objective criteria, can foster transparency, minimize political interference in project resource allocation and ensure that project resources reach the poorest areas. Poverty targeting mechanisms under the Northeast Program to date have been notably effective in reaching the poorest rural populations in the Northeast. The *ex ante* socio-economic profile of project beneficiaries indicates that, on average, 40% are illiterate, 50% have insecure access to basic food and a majority has incomes below the poverty line. Under the new project, broad targeting will be undertaken at the municipal level, by allocating higher indicative budgets to the MCs of the municipalities with lower HDIs. At the community level, targeting will be applied by the Municipal Councils themselves, which will be encouraged and technically assisted to undertake a poverty ranking of the communities in their municipalities and to establish transparent criteria to prioritize subproject proposals.

Supervision has been found to be an indispensable determinant of success and sustainability. It needs to be reinforced at all levels and involve local entities closest to the communities, particularly Municipal Councils and NGOs. IDENE will decentralize supervisory responsibilities to its regional offices and to EMATER-MG staff, who will also be the entry point for community requests for subproject financing under PAC. Under the new project, supervision responsibilities will also be increasingly devolved to Municipal Councils, who will be supported with training and technical assistance. Measures will also be taken to provide computers and information technology to the Councils to allow them to receive and exchange information through the Internet and to modernize management.

A user-friendly *monitoring and evaluation system* facilitates the subproject evaluation process, provides feedback and necessary information to improve targeting and efficiency, and is an essential management and planning tool. Under the new project, an MIS drawing on the experience of the MIS used in the other Northeast States that implemented RPAP projects will be used in the Minas Gerais RPRP to ensure real time monitoring of the entire project cycle. A comprehensive impact evaluation component will also be introduced to measure income, welfare and social capital gains.

Dissemination of "best practices", such as experiences with NGOs in Rio Grande do Norte, EMATERCE in Ceara, FUMAC Councils in Bahia and Sergipe and FUMAC-P in Pernambuco can hasten learning and reward innovation. Under the new project, exchanges between states, municipalities and communities will be expanded further using more frequent training seminars, and workshops.

Standardization of subproject documents, technical designs and unit costs simplifies the subproject preparation and evaluation process, improves the quality of subprojects, facilitates the procurement of

goods and works, prevents over-design and enables participation by poorer communities. The existing database of standard designs and documentation coming from the RPAPs implemented in the Northeast States, which are being reviewed and technically updated and expanded where necessary, will be made available to IDENE, which already has some standard project designs and technical parameters developed under the R-NRDP. This database offers a valuable asset for the implementation of the new project in Minas Gerais, allowing this State to benefit from the accumulated experience of other Northeast States. Technical parameters and unit cost estimates useful for subproject design will be prepared and periodically updated, and will be disseminated to Municipal Councils and Community Associations.

Environmental protection criteria: The detailed environmental checklist developed under RPAP in the Northeast States will be used in Minas Gerais for the proposed project to optimize the criteria and procedures – and their application – for evaluating environmental impact of subprojects. Where environmental issues are a concern, standard subproject designs have been developed in the Northeast States and have been adopted by Minas Gerais to be used by communities and Municipal Councils for the design and implementation of subprojects. An environmental specialist will be maintained at the STU to provide additional technical assistance on environmental matters as well as provide training to increase environmental awareness of Municipal Councils and community groups. The project will also ensure that subproject investments abide by existing agro-ecological zoning already completed for Minas Gerais. Partnerships will be fostered with state and municipal environmental agencies (e.g., IEF) and NGOs to develop a culture of environmental awareness in the communities and Councils through training and education.

Technical assistance enhances the ability of Community Associations and Municipal Councils to identify, prepare and implement subprojects, thereby augmenting their capacity to compete for investment funds. Technical assistance needs to be targeted to weaker municipalities to improve their planning, management and financial capacity to participate in the project. Municipal Councils will also be equipped with computers to enhance their operational efficiency. Locating and developing sources of technical assistance in rural areas requires significant attention and needs to be monitored at the local level. Under the new project, attention will be placed on training at the community level. To this effect, funds will be made available for the recruitment on a competitive basis of independent technical advisors by the MCs in municipalities without presence of EMATER-MG, with preference to local providers. These advisors will be responsible for managing and coordinating local technical and training needs. Increasing efforts will also be placed on deeper involvement of civil society (e.g., NGOs, farmer and rural worker unions, and other civil and church groups), particularly with respect to increasing the flow of information, mobilizing the poorest groups and supporting training activities at the community level. Over and above the technical support and training provided by Municipal Councils, IDENE and EMATER-MG, Community Associations will be able to contract the technical assistance and training services that they deem necessary up to 8 percent of the value of the approved subproject.

A system of *checks and balances*, clearly-defined and well-disseminated, is essential to ensure proper use of funds and sound targeting of resources. Rules and procedures for such a system, including guidelines for performance incentives and penalties, will be developed and detailed in the Project Operational Manual. Performance incentives will include increasing Councils' indicative budget envelope; increasing the number of investments or investment volume permitted to a community association; or incentives for environmental or technologically innovative investments. Penalties would be attached to cases of mismanagement and diversion of funds and include removal from eligibility to participate, reduced availability of funds, and/or judicial penalties where appropriate. In addition to penalties, Municipal Councils include participation of local civil society (e.g., NGOs, Rural Workers' Union, the Church), representatives of public ministries and municipal officials, and Council meetings are publicly announced and open to broad participation. Finally, the project will install computers in the MCs, whose role, among others, will be to publicize Council decisions on their own and the Technical Unit's webpage. The above are designed to boost and institutionalize transparency.

Productive subprojects should be subjected to rigorous selection, preparation, technical assistance and supervision criteria. Under the new project, a 'one-shot' matching grant will be provided to eligible productive investments that (i) provide services for a large number of community members; (ii) whose collective use is regulated by strict operational guidelines (*regulamento de uso*); (iii) for which operation and maintenance is assured by charging adequate user fees to both association members and non-members; and (iv) include technical assistance to ensure the sustainability of the investment. Revised procedures for productive subprojects – none of which will be financed in environmentally sensitive areas – will be outlined in the Project Operational Manual.

Broaden role of Municipal Councils in local planning, by promoting integration between local governments and project Municipal Councils, and providing information to councils on other programs and alternative sources of grant and credit financing. Over 30 percent of project Municipal Councils in Northeast States with RPAPs already participate in some prioritization of other (non-project) resources. If carefully nurtured, not only with the right mix of technical assistance, information and funding support, but also by insisting that clear and transparent rules continue to apply to the functioning of the Councils, this democratic forum may well become one of the most valuable and durable institutions for rural development in the project area.

5. Alternatives considered and reasons for rejection

Reversion to more traditional, centralized approach to implementation using line agencies. Experience with integrated rural development projects in Northeast Brazil during the 1970s and 1980s conclusively demonstrated that more centralized approaches to planning and implementation of infrastructure and service delivery through public institutions are not effective in dispersed rural areas, due, *inter alia*, to high overhead costs, coordination difficulties, subprojects that do not accurately respond to community needs, and poor sustainability of investments. Instead, the proposed project builds on a successful CDD model, broadly recognized for its effectiveness in delivering rural infrastructure and services under Brazilian Northeast conditions (e.g., cost savings of 30-50 percent *vis-à-vis* comparable works executed by public agencies), its transparency in resource allocation, and strong performance in building social capital in rural communities.

Channeling resources directly to municipal governments. Decentralization of finance and program responsibilities to municipal governments, without also building capacity at the community level to interact effectively with these governments, carries the risk of merely repeating difficulties associated with centralized decision-making, albeit at a lower level. In the Northeast States where RPAP projects were implemented, project MCs are making a major contribution to improving transparency and participation in local development planning. The proposed project will build on this experience and transfer it to Minas Gerais, helping to build Municipal Councils which can get involved in decision-making over a broad range of poverty reduction programs, thereby helping indirectly to improve the quality and effectiveness of local government.

Elimination of the PAC sub-component. Given the encouraging results of the FUMAC and FUMAC-P subcomponents in RPAP projects in Northeast States, consideration was given to eliminating the PAC option entirely from the proposed project. Municipal Councils, namely Municipal Councils for Rural Development (CMDRs), are functioning in a majority of the rural municipalities of the project area, yet would require some adjustment to conform to RPRP rules of representation (i.e., two-thirds representation from potential beneficiaries). In view of this, it was decided to retain sufficient resources in the PAC subcomponent to allow for a transition period of creation and consolidation of project MCs in a large number of rural municipalities and for eventual use by communities in municipalities where MCs cannot be created.

Onlending to the states through a program loan to the Federal Government. Since initial and follow-up RPRP projects are likely throughout the Northeast region, as well as in some states with a high incidence of rural poverty elsewhere in Brazil, consideration was given to the alternative of a single large Bank loan to the Federal Government, to be on-lent to the States. However, there are very positive benefits in terms of demonstrated commitment and ownership when the states perceive that they are in the project driver's seat, reflected, *inter alia*, in generally timely and adequate counterpart funding and maintenance of strong technical teams at the STU level. Compared with the less than satisfactory performance under earlier, more centralized rural development programs, these benefits were judged to outweigh any apparent savings in the time and costs of processing individual state loans. Indeed, implementation delays that could result from more complex arrangements to transfer funds from federal to state level might offset such savings and would certainly undermine the credibility of the project on the ground (where communities now rely on timely decision-making and resource transfer).

C. IMPLEMENTATION

1. Institutional and implementation arrangements

Implementation period: Four years

Executing Entities:

Community Associations (CAs) are groups of rural citizens with a common interest, usually from the same community, who organize into legally-constituted civil associations. They identify, prepare, implement, supervise, operate and maintain their subprojects, assisted both by technical specialists whom they contract directly and by technical assistance and training made available by Municipal Councils and the State Technical Unit. Once subprojects are approved for financing, CAs can access a share of the costs for design and implementation assistance.

Municipal Councils (MCs) include representatives of beneficiaries and civil society (at least two thirds of membership), as well as local government (maximum one third of membership). The key organization for targeting of benefits and allocating project resources, MCs also provide a critical link to local government and have the potential to engage in other non-project activities. The MCs play a fundamental role in mobilizing communities and promoting their participation in local decision making. They receive, prioritize and approve subproject proposals from the CAs, within the ceiling of an indicative annual resource figure received from the State Technical Unit, during regularly scheduled and widely publicized meetings that the public is encouraged to attend, and then submit investment plans to the State Technical Unit.

The State Technical Unit. The *Instituto de Desenvolvimento do Norte e Nordeste de Minas Gerais (IDENE)* will be the State Technical Unit of the project. IDENE will be responsible for overall project coordination with the support of its regional and local units and with increasing delegation of duties to EMATER-MG. It will also gradually delegate supervision of community associations and subprojects to the MCs and concentrate instead on oversight of the MCs themselves, as well as general project coordination and promotion. The latter duties include continuous execution of information campaigns, project reporting, impact evaluation, Management Information System updating, and design and provision of tailored training modules for MCs and CAs on key project issues.

Subproject Cycle:

- CAs determine their local investment priorities and prepare subproject proposals for investment financing;
- Subproject proposals from CAs are submitted to the respective project MCs, where they are prioritized and approved, based on indicative resource envelopes (FUMAC). This step does not occur for PAC, where CAs submit subproject proposals directly to the STU for review.
- Subproject proposals from CAs (PAC) and MCs (FUMAC) are received and technically assessed by the regional offices of IDENE assisted by EMATER-MG. The regional offices send the assessed proposals to IDENE's central office, which confirms compliance with subproject technical, social and environmental guidelines established in the Operational Manual before releasing the funds.
- Subproject agreements (*convênios*) are signed between the STU and CAs (in the case of PAC and FUMAC) and between the STU and the MC (in the case of FUMAC-P). These agreements spell out the terms and conditions for the funding, execution, ownership, operation and maintenance of the approved subprojects.
- Resources for subproject implementation are then transferred directly from the project to the CA's bank account, except in the case of FUMAC-P, where funds are transferred to the Municipal Council;
- CAs are responsible for contracting goods, works and technical assistance for subproject execution. CAs also bear responsibility for operation and maintenance of all investments, and may request technical assistance to develop operation and maintenance programs and techniques.

Project Oversight: The Minas Gerais State Secretariat of Planning and Management (SEPLAG-MG) is responsible for project oversight. The Secretary of SEPLAG-MG represents the Borrower *vis-à-vis* the Bank. The Secretary delegates day-to-day project execution to IDENE, the STU.

Project Coordination: The STU, supported by its regional offices and by EMATER-MG will coordinate overall project activities, with the following specific duties: (a) review community subproject proposals for compliance with project guidelines and eligibility criteria in the project Operational Manual; (b) assess the degree of community participation in identifying, preparing and executing subprojects and quality of technical assistance; (c) supervise the MCs to ensure they adequately manage quality of subproject implementation and provide sufficient training support to communities; (d) implement introductory training and technical assistance programs for all MCs and CAs with approved subprojects (including training on subproject implementation, contracting, O&M and financial management); (e) monitor and apply performance incentives to reward efficiency, transparency and inclusiveness of community associations and municipal councils, and to penalize poor performance/misappropriation (e.g. legal action for fund misallocation); (f) monitor performance through the Management Information System and periodically report progress; (g) prepare annual implementation and physical performance reviews; (h) submit project POAs to the Bank for approval; (i) account for all Project's transactions using the accounting module of the MIS; (j) prepare the Project's Financial Statements in the agreed FMR format; (k) prepare the SOEs through the MIS and submit to the Bank for reimbursement of eligible expenditures; (l) supervise the financial/physical execution of the subprojects; (m) prepare TORs for external independent auditors and coordinate their work to comply with the Bank's requirements; and (n) coordinate the baseline study and the overall evaluation framework for the project. For the most common types of subprojects, standardized designs and cost indicators would be made available by the STU to ensure reasonable quality and costing for subproject implementation. Departures from these standard designs would have to be fully justified in the subproject proposal, as would proposed investments which fall outside the range of standardized costs. Finally, the STU will conduct a statewide information campaign to continuously disseminate information about the project and its guidelines to all potential beneficiary communities, thereby increasing awareness, transparency and participation in the program.

Project operational procedures: The project would be implemented according to detailed procedures defined in its Operational Manual. This Manual is based on lessons learned during the implementation of the R-NRDP in the northern part of Minas Gerais, as well other projects under the Northeast Program. A user-friendly synthesis of this document will be made available to MCs and CAs. *The final draft of the project Operational Manual, which was reviewed by and is satisfactory to the Bank, would be adopted by the State before the Federal Government authorizes Loan signing.*

Accounting, financial reporting and auditing arrangements: The financial management arrangements have been reviewed by a Bank Financial Management Specialist during project preparation for compliance with OP/BP 10.02. The Guidelines of Fiduciary Management for Community Driven Development Projects (CDD Guidelines) were taken into consideration where applicable. Based on this review, financial management arrangements were considered satisfactory, indicating that it complies with the Bank's minimum financial management requirements. Under the new project, the STU will implement an action plan within the first three months of project implementation to allow reporting in Financial Management Reporting (FMR) format and to adjust project accounting and reporting procedures to fully comply with Bank requirements. According to arrangements for Bank-financed projects in Brazil, the annual financial audit of the project accounts for the period January 1 to December 31 of the year will be carried out by an Independent Auditor acceptable to the Bank. The audit report will be submitted to the Bank no later than June 30 in the year following that for which the project accounts are audited. The year end FMR will also serve as the Financial Statement of the Project, on which the independent auditors will express their opinion. According to the new audit policy, the annual financial audit will include a single opinion encompassing the Project's accounts and the eligibility of expenditures disbursed on the basis of SOEs, as well as on the Special Account, compliance with all financial covenants. The auditors will prepare also a Management Letter on internal controls and recommendations.

2. Monitoring and evaluation of outcomes/results

Analysis of implementation will depend on a database of subproject information from the project Management Information System (MIS) operated and maintained by the STU. The MIS used under RPRP in Bahia offers a good template, which has been adapted as a base for the Minas Gerais MIS. The integrated database – which will monitor the entire subproject cycle – is organized in three general levels: (a) a subproject information module, which contains pertinent physical and financial information for each subproject; (b) a financial management module, from which Statements of Expenditure (SOEs) and Financial Statements in FMR format are generated; and (c) a project management module, from which all project reports are generated. The database will include community profiles, which will also be used to evaluate project impact. The MIS will also monitor the increase in share of the rural poor population that is covered with basic services (e.g., water, electricity, road access, social services), and the share of the rural poor that have received grant financing for productive subprojects and subsequently graduated to commercial credit. The Institutional Development component will also be monitored through tracking of training events, workshops and progress toward Annual Operating Plans (POAs) on the part of the project Municipal Councils, via indicators (to be designed in conjunction with the State) which relate project expenditures to efficiency gains in State administration. Finally, the MIS will allow real time data entry and monitoring directly on-line from the field and regional offices. The STU will be responsible for maintaining and regularly updating the MIS, including key project information (as agreed with the Bank). Through periodic processing of the database information, combined with field visits and inputs from project supervision reports, project contracted studies and audits, the STU would monitor project characteristics and trends, identify implementation problems and accomplishments and undertake or promote appropriate actions to improve project implementation. The Bank's Recife Office would also monitor project performance indicators through the online MIS, and with inputs from the State, review monthly disbursement summaries and supervise subproject implementation progress on a sample basis in the field.

Finally, the project would implement evaluation studies to assess the impact of the subprojects and provide feedback to improve project operations. These studies would include: (a) annual physical performance reviews to assess the quality and sustainability of common types of financed subprojects, including reviews of community-based procurement; (b) an evaluation/implementation review, carried out at mid-term, to include beneficiary consultations to evaluate project performance and impact as perceived by its beneficiaries; and (c) a rigorous and comprehensive impact evaluation. The impact evaluation will use repeated surveys of project beneficiaries, non-beneficiary households, and beneficiaries of similar projects with centralized delivery mechanisms to assess (a) poverty targeting of beneficiaries relative to the income distribution of the population at large; (b) household welfare; (c) social capital formation at the community level; (d) improved governance at the municipal level; (e) cost-effectiveness of infrastructure investments compared with traditional delivery mechanisms, and (f) cost-benefit of productive investments. In addition, community leaders and municipal leaders will be surveyed for the analysis of social capital and governance impacts. The first baseline field survey will be conducted within six months of project effectiveness. A resurvey, to be contracted at the same time as the baseline study will be conducted two years later, followed by another survey in the last year of the project.

3. Sustainability

Institutional sustainability: The institutional analysis of (i) the prior R-NRDP in Minas Gerais and (ii) the broader set of projects under the Northeast Program shows that, by assigning greater responsibility and influence to local-level organizations and municipal governments, the proposed project can successfully support decentralized resource allocation and the creation of social capital in rural Minas Gerais. Emphasis will be placed in the new operation on linking the FUMAC councils to local municipal planning and budgeting processes and programs, as well as alternative credit and financial services. The aim of this effort will be the graduation of communities who have accumulated sufficient assets and organizational capacity to gain access to mainstream financing and other services.

Sustainability of STU is not of concern because of the experience that its core technical team already has in rural development activities and the broad involvement of IDENE in other State and federal supported programs, and because of the technical and administrative capacity and autonomy which it enjoys.

Financial sustainability: Financial analysis and field investigation confirm the sustainability of the investment subprojects funded by the CDD mechanism. A sample of over 8,000 community subprojects in those Northeast States which executed CDD projects as of 1995 (under the R-NRDP) and 1997/98 (under RPAP) was reviewed by one of the Program evaluations in 2000. Eighty-nine percent of these subprojects were fully operational. More recent data from the field confirm these findings. Analysis of productive subprojects revealed that cost recovery through user fees by beneficiary associations was adequate to cover both operation and maintenance and replacement of the original investment long before the end of its useful economic life.

Physical sustainability: Beneficiary participation at all stages of the subproject cycle as well as significant levels of community contribution help to ensure subprojects are maintained. Further, the democratic process intrinsic to FUMAC ensures better selection and prioritization of subprojects by beneficiaries, enhancing long term sustainability. The proposed project requires the establishment of community funded operation and maintenance plans – only subprojects that have realistic maintenance plans would be approved and financed. Subproject maintenance would be monitored by Municipal Councils and STU during the Project. Performance incentives for proper operation and maintenance are included in project design. According to the experience of the Northeast Program, the operation and maintenance of infrastructure and social subprojects has been good, with community associations charging user fees sufficient to operate and maintain the investments. The Bank preparation mission for the new operation confirmed this finding. Field visits in Northern Minas were instructive because the R-NRDP, which ended in 1996, was not followed by an RPAP, as happened in other Northeastern states. The mission was

therefore able to examine the current situation of old investments, several years later – an *ad hoc* survey of the “after-project” situation. The mission observed – in five municipalities visited – was encouraging: all the previously-financed infrastructure and social subprojects were working well, properly maintained by the community association, and satisfying needs deeply felt by the communities.

4. Critical risks and possible controversial aspects

Risk	Risk Rating	Risk Minimization Measure
To PDO		
<ul style="list-style-type: none"> Erosion of local, state and national political support for CDD 	M	<ul style="list-style-type: none"> Continued demonstrated success of the program reinforcing ownership of program at all levels. Strengthen links between MCs and the local government for mutual benefit.
<ul style="list-style-type: none"> Politicization of MCs 	M	<ul style="list-style-type: none"> Membership of MCs with voting rights comprises at least two-thirds of beneficiary representatives and civil society. Use of IT for e-transparency.
<ul style="list-style-type: none"> CAs and MCs unable to implement and manage good quality subprojects. 	M	<ul style="list-style-type: none"> Systematic training and TA to both CAs and MCs targeting specific needs regarding subproject implementation, O & M. Standard designs and cost criteria will be provided for most types of subprojects. Greater emphasis on performance incentives and penalties. Technical and environmental assessment and oversight for all subprojects.
To Components		
<ul style="list-style-type: none"> Inadequate and/or untimely flow of counterpart funds 	M	<ul style="list-style-type: none"> Shared counterpart funding contributions between State, local government and beneficiaries. Continued efforts to reduce transaction costs affecting timely flow of funds.
<ul style="list-style-type: none"> Communities reluctant to adopt FUMAC options 	L	<ul style="list-style-type: none"> Active information campaign will be implemented at start of project. Widespread dissemination of project achievements to demonstrate the benefits of participation. STU efforts to establish additional MCs and to adjust existing Municipal Councils to RPRP rules.
<ul style="list-style-type: none"> MCs not given clear indicative budgets for decision making 	M	<ul style="list-style-type: none"> Strict Bank supervision of STU adherence to project rules concerning indicative budgets.
<ul style="list-style-type: none"> TA not available or not used by MCs and CAs 	M	<ul style="list-style-type: none"> Funds for TA provided to MCs and CAs; they are informed of funding availability. EMATER-MG collaborates with IDENE in the provision of TA to MCs and CAs. Appointment of salaried Technical Advisor to MC, paid by project funds, in municipalities where EMATER-MG is not present. STU will prepare and disseminate a list of reliable, experienced TA providers for CA and MC use. Seminar to encourage local service provider participation in the project.
<ul style="list-style-type: none"> Subprojects not properly maintained 	M	<ul style="list-style-type: none"> Subproject proposals must include an O & M plan, to be monitored by MCs. Performance penalties are included in project design to (i) ensure MC proper annual checking of O&M compliance by CAs; and (ii) ensure communities maintain investments satisfactorily.

5. Loan conditions and covenants

- Signing of a subsidiary agreement, satisfactory to the Bank, between the State and IDENE.

D. APPRAISAL SUMMARY

1. Economic and financial analyses

Specific investments under the proposed project will be selected and carried out by communities during implementation. It is thus not possible to know *ex ante* precisely how resources will be allocated among the types of subproject investments and therefore to make aggregate projections of cost-effectiveness, rate of return and fiscal impact. However, many of the subprojects would, in general, be similar to those financed under the previous project in Minas Gerais, as well as ongoing community-based rural development projects in other Northeast States. Based on the accumulated experience from these projects, the following aspects of subproject investments were assessed: (a) cost-effectiveness; (b) financial viability of infrastructure and productive subprojects; and (c) the overall fiscal impact.

Cost-effectiveness: Several aspects of project design help to ensure that subproject investments represent the least-cost, best alternative. First, the demand-driven nature of subproject selection helps to ensure that scarce resources flow where they are most needed and chosen subprojects are the best alternatives for local communities. Second, the use of standard technical designs (*projetos padrão*) and cost parameters for the most common types of subprojects – whether infrastructure, productive or social – ensures that community associations employ least-cost models for subproject implementation and decreases associated search and information costs. Third, the delegation of subproject implementation directly to the community associations has proven to generate cost savings, when compared to similar quality works implemented by public sector agencies. The contracting procedures in the Project Operational Manual allow direct contracting by community associations, requiring, for example, that they solicit three bids for the subproject. Based on the analysis of a random sample of subprojects (including ten categories which collectively represent some 80 percent of the types of subprojects financed under the R-NRDP and RPAP), it has been found that, for infrastructure and social subprojects, costs were 30-50 percent less than for projects of similar quality, implemented by the state. Recent case studies indicate that, while cost effectiveness of both State and Federal governments has improved in the delivery of these types of investments to the rural poor, community implementation is still at least 30% cheaper for the most common types of subprojects.

Ex-post internal rates of return have been estimated for the most common types of productive subprojects. In the Northeast overall, these exceeded, on average, 30 percent. Analyses were made assuming constant benefits over the subproject life cycle. In addition to these positive impacts, benefits are largely concentrated in the subprojects' beneficiary communities. Sensitivity analysis showed that these subprojects tend to be reasonably robust vis-à-vis decreases in output and prices and increases in production costs.

Benefit-cost ratios are high (greater than 2.0) for the main productive subprojects analyzed. Analysis of these subprojects also suggests that investments are generally financially sustainable. Although beneficiary associations do receive a one-time matching grant for productive subprojects, the investments tend to be sustainable because cost recovery through user fees by the average beneficiary association is normally adequate to cover both O&M and replacement of original investments before the end of their useful economic life.

The project's **direct fiscal impact** depends on what the State would have done in the absence of the project. If the State had attempted to provide the basic services through traditional delivery mechanisms, the fiscal savings are direct and significant (see cost effectiveness discussion above). Evaluations indicate that a significant fiscal contribution will also accrue from cost savings associated with the decreased need for state and local governments to provide certain services, due to project investments. Provision of better quality, more reliable water also has less quantifiable but nonetheless significant impacts on health, reducing public health costs of Municipal Governments. The project reduces the dependency of

municipalities on central and state government transfers by strengthening the capacity of local governments and communities to take responsibility for local economic and social development. Subproject O&M costs are typically paid by beneficiary communities, reducing the fiscal burden on municipalities and states (with few exceptions, e.g., electricity and some types of water supply, commonly maintained by state agencies and operated in return for a user fee). Direct fiscal impacts are likely to be small, since much of the incremental production of the subprojects is either self-consumed, not liable to taxation, and/or circulates in informal markets where tax is rarely paid. However, indirect impact could be significant, in that there can potentially be a significant increase in ICMS collected within the poor municipalities in which the project operates.

2. Technical

The technical viability of the project has been demonstrated under the successful projects under the Northeast Program to date. The new RPRP in Minas Gerais will adopt similar institutional and implementation arrangements. Investment cost estimates, physical contingencies, prices and estimates of inputs and outputs are based on actual historical data under these earlier projects (including the R-NRDP in Minas Gerais) and thus are considered reliable. Technical standards of specific subprojects will be ensured through standardized designs (including engineering aspects, technical, financial and economic feasibility, O&M, simple environmental guidelines and cost parameters) that cover approximately 80 percent of subproject types normally demanded by the communities. Field evidence demonstrates that these simple, practical standards have enhanced subproject quality, sustainability and cost-effectiveness. All subprojects will be screened by qualified staff in the STU and communities can contract technical assistance (up to 8 percent of subproject value) to assist in design and implementation of subprojects. Training programs are also being offered to develop community capacity to prepare, implement, operate and maintain projects, as well as acquaint them with existing environmental regulations at the state and federal level. During project preparation Bank specialists reviewed the quality and sustainability of a variety of community subprojects, including water, mechanization, housing and power subprojects funded by R-NRDP, and found them to be technically sound and sustainable.

3. Fiduciary

The financial management arrangements to be used by the project were reviewed by a Bank Financial Management Specialist during project preparation for compliance with OP/BP 10.02. Based on this review, the Project has satisfactory financial management arrangements in place to adequately monitor, control, account and report on Project's transactions.

During the project preparation, the financial management module of the MIS was reviewed. The MIS will be the overall management system for monitoring and controlling project execution and for financial management. It includes accounting, funds flow and control, payments, reporting, subprojects monitoring, special account, disbursements, SOE, and general administration of the STU. The MIS was adapted from The Bahia State Company for Development and Regional Action (CAR), the STU of the RPRP in that State, where it was also considered as satisfactory to monitor and report about the Project.

A procurement capacity assessment of the STU was conducted by the Project Team's Procurement Specialist and was cleared by the Regional Procurement Advisor's Office (RPA). The "Overall Procurement Risk" was assessed as "LOW". Procurement responsibilities will be carried out by IDENE's procurement staff that have performed successfully these functions during a previous similar loan and are well-versed in Bank procurement policies and procedures. With the exception of some technical assistance for the beneficiaries which will be procured by the STU, it is anticipated that all procurement financed by the Project will be carried out by the grants beneficiary associations. However, IDENE will procure goods and works on an exceptional basis on behalf of the beneficiaries which are deemed not to have sufficient capacity. It is anticipated that these procurement activities carried out by

the STU, if any, will be limited. The beneficiaries' administrative capacity will be demonstrated in the subproject proposals and evaluated by the Implementing Agency. In addition, IDENE will exercise overall quality control of procurement financed by the subprojects.

4. Social

Rural poverty in Minas Gerais is concentrated in the regions known as *Norte de Minas*, *Vale do Jequitinhonha* and *Vale do Mucuri*, located in the northern half of the State. Statewide, some 1.1 million households earn less than US\$2.5 per day. Nearly 32 percent of rural households in Minas Gerais lack piped water supply, about 25 percent are without sanitation services, and 20 percent without electricity, compared, respectively, with 4, 2 and 1 percent for urban Minas Gerais, and 7, 3 and 0.9 percent for urban Brazil as a whole. GDP per capita in the project area is less than half that of Minas Gerais as a whole, infant mortality is 29 per cent above the average level for the State, and the percentage of population without formal education is 86 percent above the corresponding statewide figure.

The proposed project seeks to improve the quality of life of the target population through small-scale social and economic infrastructure subproject investments, using a CDD approach, increasing the social capital of the rural communities participating in the project by strengthening community associations and municipal councils. Under the project's participatory approach, the wide inclusion of all potential beneficiaries, including women and minorities, would be assured through a state-wide information campaign designed to create awareness regarding the project's objective, operating guidelines and how to access project benefits. Identification and implementation of specific subprojects would occur through demand-driven mechanisms at the community level.

Communities are creating the demand for the new project, and are dictating the types of subprojects to be financed, demonstrating their high level of satisfaction with CDD delivery mechanisms. Detailed evaluations reinforce these findings (see Annex 9). Various evaluations cite the strong demand for subproject investments among the potential beneficiary population. High levels of beneficiary satisfaction, as well as strong economic impact of local infrastructure investments, were recorded.

Apart from meeting basic community investment needs, a major achievement of the Northeast Program to date has been to foster the creation of social capital within rural municipalities and their communities. This accumulation of social capital has increased with the introduction of the more decentralized FUMAC and FUMAC-P mechanisms. This is because the MCs have provided a new, representative and transparent forum for local government and community representatives to discuss and prioritize investment proposals. By providing communities the opportunity to address their needs through a genuinely participatory process of decision making and oversight, the MCs have succeeded in: (i) reducing clientelism and political interference; (ii) strengthening the capacity of both communities and municipal governments to select, prioritize and implement investment decisions; (iii) creating partnerships between communities, MCs and municipal governments and more generally, increased the community voice in the use of public resources; and (iv) fostering citizenship through increased awareness of social responsibilities of citizens, their representatives and public authorities in community and public matters.

All subprojects are identified, prepared, implemented (including procurement/contracting of works), supervised, operated and maintained by community associations. Funds are directly disbursed to community associations, which also contribute up to 10 percent of subproject costs. Intermediary NGOs, private firms and other civil groups may provide technical assistance, facilitate information dissemination to community associations and assist in mobilization and organization of communities. Local government participates in municipal council meetings, and directly facilitates the work of these councils. The STU offers capacity-building and training to community associations and municipal councils to

foster and enhance social capital. STU also forges links with a cadre of Federal, State and Municipal agencies to leverage mobilization, training and specialized expertise in project activities.

Experience under the previous project shows that the mechanisms to be used in the proposed project (particularly FUMAC and FUMAC-P) have promoted inclusion of all social groups. Under the RPAP, MCs and CAs had a strong representation of women and minority groups. In the proposed project, the policies of open access to program benefits, and widely dispersed information regarding program rules (using the information campaign) will continue to ensure equitable treatment of, and access for, all potential beneficiaries.

To further increase project impact, the following changes are being implemented to continue to promote and strengthen transparency and social inclusion:

- higher levels of funding for the poorest communities as determined by the United Nations HDI;
- greater emphasis on FUMAC and FUMAC-P, and minimization of PAC;
- training of MCs in targeting, and introduction of performance incentives for reaching the poorest; and
- promote sustainability by developing a strategy for linking communities to local governments, alternative funding from financial institutions and to other programs

The project Management Information System (MIS) will monitor subproject implementation, as well as number and location of beneficiaries. The MIS will track community mobilization activities, training courses offered for FUMAC and FUMAC-P councils, as well as periodic supervision of subprojects *in situ*. Annual physical performance reviews over the course of the project will assess, *inter alia*, the participatory approach pursued under the project, making recommendations where needed. Also, the overall project impact evaluation will serve to assess the poverty targeting of beneficiaries under the project, household welfare and social capital formation, at both the community and municipal level.

5. Environment

Experience under the previous Reformulated Northeast Rural Development Project in Minas Gerais was reviewed during project preparation and confirmed that few subproject investments have the potential for adverse environmental impact. An Integrated Safeguard Data Sheet was prepared for the project and reviewed by the LCSES Quality Assurance Team. Environmental Checklists –incorporated into the Project Operational Manual under the RPAP in other Northeast states – have been adapted and updated for the proposed project, for use in subproject preparation by potential beneficiary associations. These checklists would be completed by community associations to identify potentially adverse environmental impacts from subproject investments and methods to mitigate these impacts.

The proposed project is a Category B, indicating that its potential environmental impact on human populations and ecologically important areas is considered moderate/modest. Neither the State, nor the Bank, through the Project, will approve subprojects which cause degradation to essential natural habitats. No subproject agreement will be signed or funds transferred until the environmental viability of the subproject is determined. The subproject agreements eventually signed between IDENE and community associations will contain environmental compliance clauses.

The following main features regarding the environment are included in the project design: (i) environmental screening, using a strengthened Environmental Checklist, for each subproject proposal; (ii) a negative list, specifying those subprojects which are ineligible for financing under the project; (iii) technical capacity at the state level, by contracting of an environmental specialist by the STU; and (iv) environmental education and awareness, conducted through the statewide information campaign, and direct training of municipal councils and community associations, with guidance from the in-house

environmental specialist. Specifically, the environmental specialist would serve as a bridge between the STU and the state-level environmental agencies, assess subproject proposals and recommend mitigation measures, and supervise environmental awareness training for both Municipal Councils and Community Associations.

Key stakeholders consulted on environmental aspects during the preparation of the include (i) potential project beneficiaries, who inhabit rural areas of the state, (ii) representatives of civil society-at-large and (iii) public sector agencies charged with project oversight and coordination. Community associations and existing Municipal Councils - both of which encompass broad representation of interested stakeholders – and are the primary instruments for subproject prioritization and subsequent execution. Environmental screening is conducted directly by the project beneficiaries (i.e., community associations), via the completion of the environmental checklist for each subproject proposal. Data from the checklist will be reviewed by the in-house environmental specialist to monitor compliance with project guidelines set forth in the Operational Manual.

An information campaign (satisfactory to the Bank) will orient potential beneficiaries on the implementation arrangements under the project, including the due diligence required of the community associations in addressing environmental guidelines at the state and federal level. The project mid-term review will further assess the usefulness of the environmental checklist, including on-site inspection of subprojects, as well as the overall environmental screening and subproject supervision, and provide recommendations as necessary for improving monitoring of such activities.

6. Safeguard policies

Safeguard Policies Triggered by the Project	Yes	No
<u>Environmental Assessment (OP/BP/GP 4.01)</u>	[X]	[]
Natural Habitats (<u>OP/BP 4.04</u>)	[]	[X]
Pest Management (<u>OP 4.09</u>)	[]	[X]
Cultural Property (<u>OPN 11.03</u> , being revised as OP 4.11)	[]	[X]
Involuntary Resettlement (<u>OP/BP 4.12</u>)	[]	[X]
Indigenous Peoples (<u>OD 4.20</u> , being revised as OP 4.10)	[]	[X]
Forests (<u>OP/BP 4.36</u>)	[]	[X]
Safety of Dams (<u>OP/BP 4.37</u>)	[]	[X]
Projects in Disputed Areas (<u>OP/BP/GP 7.60</u>)	[]	[X]
Projects on International Waterways (<u>OP/BP/GP 7.50</u>)	[]	[X]

7. Policy exceptions and readiness

There are no policy exceptions and the project is ready for implementation.

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Annex 1: Detailed Project Description

Project Component 1 – Community Subprojects (US\$40.7 million):

The project would provide matching grants directly to rural community associations to finance priority, small-scale investments identified by community groups (up to US\$50,000 each). It is expected that approximately 1,860 subprojects will be financed under this component. This will comprise a broad range of subproject investments including infrastructure (e.g., rural electrification, local road improvements and water supply), social investments (e.g., health-related house improvement, day care centers, school or health post rehabilitation) and productive subprojects (such as small-scale community agro-processing, communal tractors and minor irrigation schemes). Subproject selection shall be demand-driven, however an indicative breakdown of investment types, based on perceived community demand suggests approximately 60 percent of financing shall be used for infrastructure, 25 percent for social activities, and 15 percent for productive investments.

Subproject proposals for all forms of investment would observe standard procedures, documentation and technical, economic, environmental and sustainability criteria to be set forth in a detailed Project Operational Manual. A short negative list¹ of subproject types ineligible for financing will be enforced, with particular emphasis on the application of rigorous eligibility criteria for productive subprojects to ensure proper targeting, and financial sustainability of this form of investment², also to be included in the Project Operational Manual

The identification, preparation and implementation of all subprojects financed under the project will be the responsibility of the beneficiary rural communities. Three different delivery mechanisms – incorporating increasing degrees of decentralization - distinguish how the subprojects are approved and financed:

- *State Community Schemes (PAC).* Under the PAC subprogram, rural communities submit their investment proposals directly to the State Technical Unit (STU), which screens and approves them and releases funds to the beneficiary associations. Whereas this was the predominant arrangement under the earlier R-NRDP projects, it receded in importance in the States which had RPAP projects, as decentralization from the state to local levels progressed. At the start of the RPAP projects in the Northeast States, it was expected that about one-third of community proposals would be processed under the PAC, but the actual share decreased steadily during implementation, in favor of the other two modalities described below. Under the proposed new RPRP project for Minas Gerais, the PAC will be used to respond to demands from communities in municipalities where a Municipal Council has not yet been created. It will also be retained as an option to which communities may occasionally resort in cases where Municipal Councils are not functioning properly, but it is expected to account for no more than 23 percent of all subprojects (or US\$9.2 million). The percentage of RPRP investment resources expected to be channeled through the PAC subprogram is larger in Minas Gerais than in other Northeast States, where it is 5–10 percent. The reason is that there are

¹ Those subprojects ineligible for funding include production of alcohol, tobacco and drugs, churches, and facilities for political activities.

² Productive subprojects, as with infrastructure and social subprojects, must be property of the association as a whole and not of select members. For each type of productive subproject, a set of operational guidelines (*regulamento de uso*), developed by the STU, would be provided to the association for adoption. In addition, each subproject proposal must identify the source of technical assistance for subproject implementation and subsequent operation.

proportionally many more rural municipalities with Municipal Councils in operation in these States than in Minas Gerais where there was no RPAP and the project area has been extended.

- *Municipal Community Schemes (FUMAC)*. Under this subprogram, decision-making on investment proposals is delegated by the State to project Municipal Councils, composed of community members and representatives of civil society and municipal authorities. At least two thirds of Council voting members are potential project beneficiaries and representatives of civil society. The Municipal Councils discuss, seek to build consensus on priorities and approve community proposals, in the context of an indicative annual budget amount determined by the state. After the Councils' recommendations are reviewed by the STU for consistency with guidelines in the project Operational Manual, funds are disbursed directly to the community associations. This became the preferred and hence the dominant subprogram under the RPRP in the Northeast States. Under the proposed RPRP for Minas Gerais this subprogram will account for about 71 percent (US\$29.1 million) of total community subproject cost.
- *Pilot Municipal Community Funds (FUMAC-P)*. The FUMAC-P is a more decentralized variant of FUMAC piloted under the RPAP with high-performing Municipal Councils, and will be tested in the Minas Gerais RPRP. The STU establishes an annual budget envelope, according to a distribution formula based on clear and measurable criteria (rural population, poverty levels and previous year's performance). Based on this budget, Municipal Councils submit an Annual Operating Plan (*Plano Operativo Anual*) for STU review. Upon approval, funds are transferred to the Council, which is then responsible for managing their distribution to community associations and assisting them with implementation of subprojects. As a pilot approach the FUMAC-P will also have the following characteristics: (i) it will discuss and transfer to the appropriate places community demands not covered by the RPRP whose objectives are complementary to those of the project; (ii) participating municipalities will be encouraged to contribute complementary funds to those supplied by the project; (iii) representatives from municipal programs or councils operating in rural areas in the fields of health, education, production and others will be encouraged to participate in the FUMAC-P Council; (iv) participating municipalities, in partnership with the project, will assist in the creation of a small technical unit which will provide operational support to the FUMAC-P Council. It is expected that under the new RPRP project, 6 percent of total component costs (US\$2.4 million) would be used under the FUMAC-P subprogram in at least ten municipalities.

Promotion. Each subcomponent described above (i.e., PAC, FUMAC and FUMAC-P) represents a greater degree of decentralization of decision-making and resource allocation responsibilities. As groups of communities become more organized they are 'promoted' from PAC to FUMAC to FUMAC-P, gradually gaining greater control over investment planning that goes beyond their specific community subproject. Communities with limited capacity, and/or those communities that reside within municipalities which have not yet formed a MC or that lack the capacity or political will to adopt FUMAC approach, may choose to enter the program through PAC. Other communities/ municipalities that are better organized, and/or have had experience with PAC, and are receptive to participatory decision-making processes, enter FUMAC. A Municipal Council is formed and resource allocation decisions start being made at the local level. This institutionalization of the participatory process has been shown to protect MCs from political fluctuation, and eventually leads to stronger partnerships between communities, their Municipal Councils and their respective municipal governments in determining the use of public resources.

Given the overwhelmingly positive response to FUMAC in other Northeast States that had RPAPs, it is expected that the need for the PAC subcomponent would diminish over the course of project implementation, with the FUMAC subcomponents gradually expanding. The existence of PAC is to facilitate subprojects during the beginning of the project while MCs are being created in the many municipalities that do not have one, as well as to facilitate participation in the project of those

communities within weaker municipalities which fail to adopt the FUMAC approach. Flexibility would be built into the project to reallocate funds among subprograms to accommodate the expansion of FUMAC and FUMAC-P as implementation proceeds. The PAC scheme, however, is expected to assist towards decentralization and the creation of social capital. To achieve this, the STU will enroll the support of community associations who have benefited from PAC subprojects to help other communities to organize their own associations and to assist in the process of forming a Municipal Council in the municipality. The mechanics of this process will be detailed in the project Operational Manual.

Targeting. The proposed project is targeted to the poorest communities in rural Minas Gerais. The project area includes 188 of the total 853 municipalities statewide. Some municipalities in the latter two regions, which are contiguous to *Norte de Minas*, bordering with its eastern part, were included in the R-NRDP as a pilot experiment during the last year of the project. These regions have now been included in the RPRP because of the incidence of rural poverty, which is similar to that of *Norte de Minas* and higher than in other regions of the State. All municipalities in these three regions are included in the targeted area. The funds for the Community Subprojects component will be allocated among municipalities in proportion to their rural population (including the population in municipal towns of less than 7,500 inhabitants, which are also part of the target group). According to this, an estimate of the order of US\$19.3 million of the Community Subprojects Component will be allocated to *Norte de Minas*, US\$12.0 million to *Vale do Jequitinhonha*, US\$7.6 million to *Vale do Mucuri* and US\$1.8 million to the *Central* region. Within each region, funds from the Communities Subprojects component will be allocated to the municipalities according to (a) the size of their rural population, and (b) their level of need shown by the index. The Operational Manual will indicate operational details of these allocation criteria.

At municipal level, Municipal Councils will be responsible of community targeting. This will be supported in various ways: (1) giving MCs an annual budget figure for the resources available to finance subprojects in their respective municipalities; (2) asking MCs to carry out poverty ranking exercises of the communities based on assessed needs and an inventory of community assets, and providing them with technical assistance to do so; (3) widely disseminating the RPRP program and activities, particularly among the poorest communities so as to promote their presentation of subproject ideas and their participation in Council meetings; and (4) direct advocacy, encouraging MC to prioritize poor communities. The effectiveness of this methodology will be assured by the establishment of clear and transparent rules and procedures for the Councils' functioning. Increased decentralization of subproject selection through the FUMAC subprogram is expected to further strengthen the project's capacity to reach the neediest communities in the project area. Continual implementation and revision of the information campaign for the project will also be used to expand opportunities for participation of the poorest communities in the target area. This information on project eligibility and procedures will be targeted to potential beneficiary communities to create a level playing field for access to project funds and to stimulate demand from potential beneficiaries across the state. Some communities already have significant levels of organization, either traditionally or from previous development projects in the area, and are poised to benefit immediately from the project. However, for those less organized communities, the project, through its institutional development component, would actively extend mobilization assistance through the services of NGOs or accredited agents who know the communities well and can serve as catalysts for organization (refer component B described below).

In order to be eligible to receive funding under the project – in compliance with Brazilian Law - beneficiaries must form legally-constituted civil associations (or 'community associations'). Disbursements to the beneficiary associations would occur through agreements (*convênios*) with the STU and/or project Municipal Councils, as per model agreements developed under RPAP. These agreements will be included in the Operational Manual for the new project. Beneficiary associations will be required to contribute either in cash, kind or labor, an amount of not less than 10 percent of the subproject cost, and will be responsible for the operation and maintenance (O&M) of the investments. The minimum

level of contributions expected from the beneficiaries, municipalities and the State Government is specified in a cost-sharing matrix detailed in the Project Operational Manual.

Project Component 2 – Institutional Development (US\$3.3 million):

The Institutional Development component will finance technical assistance and training, sufficient for each group participating in project implementation to acquire the capabilities needed to effectively carry out its responsibilities. This component will also finance the contracting of consultants and other entities to assist the STU in monitoring, supervision and evaluation tasks, and will provide technical assistance services to support State level modernization and reform. This project component will also support piloting of the use of information technology by community associations and MCs to increase transparency by making available, in real time, information about the program itself, as well as using the Internet to connect communities directly to markets, both in Brazil and internationally.

Using the demand-driven implementation mechanisms described in Component A, the project consolidates participatory institutions and processes at the municipal and community levels. In this process, well-organized communities with sound, carefully prepared proposals are provided with financial support for investments.

To encourage this process and reinforce the decentralized implementation framework, technical assistance and training will be provided for community associations, Municipal Councils, and the STU, as well as other entities participating in the project. Types of training and assistance will include support to communities in organization, subproject preparation and execution, as well as operation and maintenance techniques. Assistance will be provided to MCs to improve decision-making capacities, and to create capacity for investment planning and financial administration. At the STU level training will also be provided to enhance project coordination and supervision skills. Also, because the fiscal situation of the State affects both project implementation and state counterpart funding, technical assistance will be provided at the state level to analyze issues surrounding the reform of the State and to identify measures to improve the State's capacity to address the inherent causes of its fiscal situation. The instruments for achieving these various forms of capacity building will include a combination of workshops, technical exchanges, on-site training, and more traditional technical assistance, drawing upon local expertise within the state - technical consultants, universities, NGOs, and other local service providers-- as well as national and international technical assistance agencies. To this effect, the component would finance consultant services, training materials and courses, seminars, workshops, related studies and related operational costs.

The implementation of the institutional development component would be decentralized, and the provision of and accountability for technical assistance and training would occur increasingly at the local level. In particular, project Municipal Councils will play a critical role in overseeing the capacity-building activities for community associations in their jurisdictions. Technical assistance will increasingly be provided by MCs, and a local technical advisor will be competitively recruited for this purpose under the new project in those municipalities where EMATER-MG does not have enough installed capacity. Municipal Councils, provided with model terms of reference prepared by the STU, will contract technical assistance based on programs agreed with the STU, and then release funds for that purpose. Institutional development activities can be broadly categorized into five areas:

- a) *mobilization assistance and training for participating communities.* Assistance would be organized and contracted by the STU and Municipal councils, to support the organization and strengthening of community associations, identification of viable investments, subproject preparation, and operation and maintenance of investments;
- b) *capacity-building programs for Community Associations and Municipal Councils.* Organized by the STU, these programs will include intensive training on the role of Municipal Councils, explanation of

Operational Manual guidelines, techniques for subproject evaluation and supervision, as well as related topics such as environmental assessment of subprojects, participatory planning and financial management. Under the new project all MCs and community associations, with approved subprojects, will be required to participate in mandatory 'introductory training' covering the above-mentioned topics. In addition, all MCs will be gradually equipped with computers to assist them in performing their expanding functions;

- c) *specialized skills training for all participating entities.* Based on needs, local providers would be contracted by the STU, Municipal Councils and groups of community associations to provide expert advice and "on-the-job training", in areas such as investment-related technical support, the use of standard designs, monitoring techniques, and financial management;
- d) *technical assistance for State reform.* SEPLAG-MG will have access, through the STU, to technical assistance funds in support of the implementation of the State's modernization reforms, particularly in promoting the integration of the State's policy for poverty reduction and strengthening its management capacity to better monitor the impact of its public expenditures to reduce poverty in the rural space; and
- e) *workshops and seminars for the Municipal Councils and beneficiary associations, to exchange experience under the project.* These "best practice" exchanges may also extend to seminars to forge links between all STUs of the ten Northeastern states, and to disseminate successful experiences across states.

Project Component 3 – Administration, Monitoring and Evaluation (US\$1.4 million):

This component would support overall project coordination and supervision and would help to strengthen the effectiveness and quality of project operations. It would finance the incremental operating costs of the STU (excluding salaries), which is responsible for overall coordination of project activities in partnership with community associations and with FUMAC municipal councils. As part of its duties, the STU will conduct an ongoing statewide information campaign to continuously disseminate information about the project and its guidelines to all potential beneficiary communities, thereby increasing awareness, transparency and participation in the program. This campaign will be organized in two phases: the first will take place during the launching of the project and will be oriented to disseminating widely its objectives and characteristics in the project area, while the second will take place during the entire the life of the RPRP and will be oriented to promoting as much implementation transparency as possible, through the regular dissemination of information on all relevant activities and aspects of the project. For this campaign, the project would finance: (a) local technical assistance in the design and development of the campaign; and (b) the implementation costs, including appropriate, simplified posters, leaflets, radio spots and videos.

Given the importance of supervision to the overall impact of the program, project supervision will be intensified under the project and half of its cost will be financed under this component. Project supervision will provide the STU with the necessary information on project performance to make managerial decisions, such as the provision of technical assistance or training and the correction of departures from project guidelines. In line with the increasing emphasis on decentralization under the new project, the responsibilities for the supervision of operations in each region will be deconcentrated to the regional offices of IDENE. At the local level, supervision will be increasingly devolved to MCs with the STU focusing on supervision of the MCs, 'spot-checks' of community associations to verify performance, and overall project coordination. Each subproject will be supervised at least three times: (i) after its approval and before the disbursement of funds, in which occasion the obligations of the incumbent community association will be clearly established; (ii) mid-way during the implementation of the subproject; and (iii) at the end of the construction of the works, in the case of infrastructures, when the finalization of the works will be certified. Supervision activities to be financed under the project include

operational expenses for field visits and subcontracted services from NGOs and other participating agencies.

This component would also finance the establishment of a monitoring system, including the maintenance and use of a Management Information System (MIS). To function as an efficient management tool, the project MIS, will be more user-friendly and performance-oriented. It would allow regional offices to enter data and monitor on-line real time flow of subprojects. The MIS would be expanded to contain key technical, financial and socio-economic information on subprojects (planned and actual), as well as cost and other physical indicators, and quantitative variables for impact monitoring. MIS-generated project reports, including monthly disbursement reports and semi-annual progress reports, would facilitate subproject tracking and generate appropriate feedback on project performance. Project performance and impact indicators would be regularly updated to take stock of project implementation and will be included in the semi-annual progress reports. A Project Implementation Plan and a matrix of Project Performance Indicators were finalized and agreed during project preparation. This component would finance operating costs for monitoring activities, as well as finance experts in information technology and project management: (a) to improve the MIS; and (b) to collect and analyze data on cost indicators and physical parameters from the most frequently approved types of subprojects, so as to calculate a range of values for these indicators and to adjust subproject eligibility criteria accordingly. These adjustments will be incorporated into the Project Operational Manual.

Finally, the project would finance consultant services to develop and implement studies to evaluate the impact of the subprojects and provide feedback to improve project operations, including the following: (a) annual physical performance reviews, to assess the quality and sustainability of common types of subprojects financed by the project, including reviews of community-based procurement; (b) an implementation review, carried out at the mid-term, to include beneficiary consultations so as to generate an evaluation of project performance and impact as perceived by the ultimate beneficiaries; and (c) a comprehensive impact evaluation, which would include a baseline evaluation to establish indicators of socio-economic impact and a follow-on final evaluation of the project using these indicators to measure (i) aggregate project impact on social indicators; and (ii) cost/benefit of demand driven vs conventional approaches to rural development. During project preparation, an execution chronogram was agreed.

Project Coordination: IDENE will be responsible for overall project coordination with the support of its regional and local units and with increasing delegation of duties to EMATER-MG. It will also gradually delegate supervision of community associations and subprojects to the MCs and concentrate instead on oversight of the MCs themselves, as well as general project coordination and promotion. The latter duties include continuous execution of information campaigns, project reporting, impact evaluation, Management Information System updating, and design and provision of tailored training modules for MCs and CAs on key project issues. It will have the following specific duties: (a) review community subproject proposals for compliance with project guidelines and eligibility criteria in the project Operational Manual; (b) assess the degree of community participation in identifying, preparing and executing subprojects and quality of technical assistance; (c) supervise the MCs to ensure they adequately manage quality of subproject implementation and provide sufficient training support to communities; (d) implement introductory training and technical assistance programs for all MCs and CAs with approved subprojects (including training on subproject implementation, contracting, O&M and financial management); (e) monitor and apply performance incentives to reward efficiency, transparency and inclusiveness of community associations and municipal councils, and to penalize poor performance/misappropriation (e.g. legal action for fund misallocation); (f) monitor performance through the Management Information System and periodically report progress; (g) prepare annual implementation and physical performance reviews; (h) submit project POAs to the Bank for approval; (i) account for all Project's transactions using the accounting module of the MIS; (j) prepare the Project's Financial Statements in the agreed FMR format; (k) prepare the SOEs through the MIS and submit to the Bank for reimbursement of eligible expenditures; (l) supervise the financial/physical execution of the subprojects;

(m) prepare TORs for external independent auditors and coordinate their work to comply timely with the Bank's requirements; and (n) the completion of the baseline study and the overall evaluation framework for the project. Using standardized cost indicators, reasonable costing for subproject implementation would be ensured. Departures from standard designs would have to be fully justified in the subproject proposal, as would proposed investments which fall outside the range of standardized costs.

Project Oversight: The Minas Gerais Secretariat of Planning and Management (SEPLAG-MG) is responsible for project oversight. The Secretary of SEPLAG-MG represents the Borrower *vis-à-vis* the Bank. The Secretary delegates day-to-day project execution to IDENE, the STU. IDENE will implement the project in partnership with EMATER-MG, Community Associations and Municipal Councils. It will receive and approve the Annual Operating Plans for the project Municipal Councils, and will receive and approve community subproject proposals in the case of PAC. IDENE will be responsible for day-to-day project oversight with respect to monitoring, supervision of municipal councils, evaluation and required reporting under the project.

Monitoring and evaluation arrangements: Analysis of implementation will depend on a database of subproject information from the project Management Information System (MIS) operated and maintained by the STU. The MIS used by the Bahia State Rural Poverty Reduction Project offers a good template, and has been adapted for use under the proposed project in Minas Gerais. The integrated database – which will monitor the entire subproject cycle – is organized in three general levels: (a) a subproject information module, which contains pertinent physical and financial information for each subproject; (b) a financial management module to monitor financial execution of the subprojects and other components of the Project and from which the Financial Statements in FMR format and the Statements of Expenditure (SOEs) will be generated; and (b) a project management module, from which all project reports are generated. The database will include community profiles, which will also be used to evaluate project impact. The MIS will also monitor the increase in share of the rural poor population that is covered with basic services (e.g., water, electricity, road access, social services), and the share of the rural poor that have received grant financing for productive subprojects and subsequently graduated to commercial credit. Finally, the MIS will allow real time data entry and monitoring directly on-line from the field and regional offices. The STU will be responsible for maintaining and regularly updating the MIS, including key project information (as agreed with the Bank). Through periodic processing of the database information, combined with field visits and inputs from project supervision reports, project contracted studies and audits, the STU would monitor project characteristics and trends, identify implementation problems and accomplishments and undertake or promote appropriate actions to improve project implementation. The Bank's Recife Office would also monitor project performance indicators through the online MIS, and with inputs from the State, review monthly disbursement summaries and supervise subproject implementation progress on a sample basis in the field.

Accounting, financial reporting and auditing arrangements: The Special Account will be established in a commercial bank, and the project accounts will be maintained and audited annually in accordance with the audit TORs. According to arrangements for Bank-financed projects in Brazil, the annual audit of the project accounts for the period January 1 to December 31 of the year (or, in the first year of operation, from the date of start of the project to December 31 of that year) will be carried out by independent auditors acceptable to the Bank. The audit report will be submitted to the Bank no later than June 30th in the year following the year for which the projects accounts are audited. The Auditor's TOR will be based on current audit policies and practices for World Bank financed activities. The audit reports will express a single opinion on the Project's accounts, on the Special Account and on the SOE's Statement including comments as necessary on the methodology employed in the compilation of the statements of expenditure (SOEs), their accuracy, the relevance of supporting documents, eligibility for financing in terms of the project's legal agreements and standards of record keeping and internal controls related to the foregoing. With respect to withdrawals on the basis of SOEs, such audits would include a review of the SOEs,

together with the procedures involved in their preparation, and of the supporting documentation to check upon the eligibility of all expenditures submitted for financing.

Project Reporting: Periodic processing of the database information will permit the monitoring of the characteristics and evolution of project implementation. The STU will be responsible for reporting on the project performance indicators.

- *Annual Physical Performance Reviews:* The Annual physical performance review would be conducted on a sample of community subproject beneficiary communities. Variables assessed during the Review would include: *quality of investments*, as assessed by beneficiaries and qualified professionals, *cost-effectiveness*, as compared with similar public sector investments, and *procurement*, such as local contracting of goods and services.
- *Implementation Review:* The Implementation Review would be held annually, together with the Physical performance review. The Review would take place in advance of the approval of next year's Annual Operating Plan. The range of studies to be prepared for each of these reviews would be agreed upon on a rolling basis, at appraisal for the first review, and at each annual implementation review for the subsequent implementation review.

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Annex 2: Major Related Projects Financed by the Bank and/or other Agencies

Sector Issue	Project ¹	Latest Supervision (ISR) Rating	
		<u>PDO</u>	<u>IP</u>
Ongoing Projects			
Community-Driven Development	RPAP Paraíba (Ln. 4251-BR)	S	S
	RPRP Bahia (Ln.4623-BR)	S	S
	RPRP Ceará (Ln. 4626-BR)	S	S
	RPRP Pernambuco (4625-BR)	S	S
	RPRP Piauí (Ln. 4624-BR)	S	S
	RPRP Rio Grande do Norte (Ln. 4667-BR)	S	S
	RPRP Sergipe (Ln. 4649-BR)	S	S
Water Resource Mgt.	Water Res. Mgt. Project (Ln. 4232-BR)	S	S
Health	Bahia Dev. Health (Ln. 7182-BR)	S	S
Education	FUNDESCOLA III (Ln. 7122-BR)	S	S
	Bahia Dev. Ed. 2 nd APL (Ln. 7186-BR)	S	S
Land Reform	Land-based Poverty (Ln. 7037-BR) ²	S	MU
OED Ratings			
Closed Projects		Implementation	Sustainability
Community-Driven Development	R-NRDP Minas Gerais (Ln 2861-BR)	S	Likely
Land Reform	Land Reform Pilot (Ln. 4147-BR)	S	Likely

¹ A Maranhão Integrated Project: Rural Poverty (Ln 4735-BR) has been approved by the Board and is awaiting Effectiveness.

² Implementation progress rated unsatisfactory due to delays in disbursements. The quality of work on the ground is satisfactory, and the State of Minas Gerais has been an active participant in the project.

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Annex 3: Results Framework and Monitoring

Results Framework

PDO	Outcome Indicators	Use of Outcome Information
Community associations of the rural poor in Minas Gerais access basic social and economic infrastructure, contributing to an increase in HDI-M	1,860 subproject implemented and maintained by community associations	YR 1: Baseline survey designed and implemented YR 2-3: Mid-term evaluation to determine uptake among intended beneficiaries and assess need for possible adjustments to project design. Y4: <i>ex post</i> evaluation and mainstream of CDD methodology
Intermediate Results One per Component	Results Indicators for Each Component	Use of Results Monitoring
Component One: Rural communities self-select to access, implement and maintain subprojects in education, health, cultural, environmental and other productive investments	Component One: Household surveys to verify targeting effectiveness, changes in household welfare and income, attributable to the project. Social Capital assessment to quantify participation and construct Community Participation Indices.	Component One: YR 1: Track geographic expanse and municipal depth of investment, as gauge of information campaign. YR 2-3: Determine links between subprojects chosen and HDI parameters. YR 4: Assess effectiveness of municipal council decision-making and prioritizing community subprojects
Component Two: CAs, MCs, and IDENE staff receive training and technical assistance for subproject execution, roles and responsibilities as described in the project operational manual, and environmental and social dimensions of the project.	Component Two : MIS tracks number and type of training events Bank and IDENE supervision missions to determine likelihood of physical, financial, environmental sustainability of subprojects IDENE semi-annual reports	Component Two: YR 1: Determine compliance with project operational manual re: subproject preparation and safeguards. YR 2-4: Reassess training as needed and update revise Op. Manual
Component Three: Subprojects, community associations and municipal councils evaluated regarding effectiveness of CDD methodology and sustainability of basic services delivery.	Component Three: Annual project audit to confirm compliance with internationally accepted practices of financial management and Bank guidelines for procurement under the project.	Component Three: YR 1-4: Determine extent of integration across programs, sectors, and policies for rural poverty reduction

Arrangements for results monitoring

Outcome Indicators	Data Collection and Reporting							Responsibility for Data Collection
	Baseline	YR1	YR2	YR3	YR4	Frequency and Reports	Data Collection Instruments	
% of rural poor self-selecting into the project, identifying and implementing subprojects (cumulative).	Assessed in YR 1 as CA's enter project	3%	5%	8%	10%	Continuous updating of MIS; semi-annual cumulative reports	Community profiles Subproject proposals IDENE supervision reports	IDENE/Community Associations/ Municipal Councils
Results Indicators for Each Component								
Component One :								
1,860 subproject investments implemented and maintained by community associations	0%	35%	32%	23%	10%	Continuous updating of MIS; semi-annual cumulative reports	Community profiles Subproject proposals IDENE supervision reports	IDENE/Community Associations/ Municipal Councils
Component Two :								
training events, seminars for: % CAs receiving training in subproject management and operation; %MCs receiving training in HDI-M and investment priority-setting; %IDENE staff receiving TA training for CAs and MCs	0% 0% 0%	30% 30% 30%	50% 50% 50%	80% 80% 80%	100% 100% 100%	Continuous updating of MIS; semi-annual cumulative reports;	Training evaluations, focus groups, interviews	IDENE/Community Associations/ Municipal Councils
Component Three:								
Baseline Study MTR Final Evaluation	- - -	X	X		X	YR 1 YR 2 YR 4	Survey MIS, Survey MIS, Survey	Consultants IDENE/Community Associations/ Municipal Councils

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Annex 4: Project Costs

Project Cost By Component and/or Activity	Local US \$million	Foreign US \$million	Total US \$million
1. Community Subprojects			
PAC	8.40	0.90	9.30
FUMAC	26.80	2.65	29.45
FUMAC-P	2.20	0.20	2.40
Subtotal Component 1	37.40	3.75	41.15
2. Institutional Development	2.30	0.80	3.10
3. Administration, Monitoring and Evaluation	0.90	0.30	1.20
Total Baseline Cost	40.60	4.85	45.45
Physical Contingencies	0.40	0.20	0.60
Price Contingencies	0.30	0.10	0.40
Total Project Costs	41.30	5.15	46.45
Front-end Fee		0.35	0.35
Total Financing Required	41.30	5.50	46.80

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Annex 5: Financial Management and Disbursement Arrangements

Financial Management and Disbursements

The financial management arrangements to be used by the project were reviewed by a Bank Financial Management Specialist during project preparation for compliance with OP/BP 10.02. Based on this review, the Project would have, by effectiveness, satisfactory financial management arrangements in place to adequately monitor, control, account and report on Project's transactions.

During the preparation Mission, the financial management module of the MIS was reviewed. The MIS will be the overall management system for monitoring and controlling project execution and for financial management. It includes accounting, funds flow and control, payments, reporting, subprojects monitoring, special account, disbursements, SOE, and general administration of the STU. The MIS was adapted from the Bahia State Company for Development and Regional Action (CAR), the STU of the RPPP that State, where it was also considered as satisfactory to monitor and report about the Project. Personnel from the IDENE who will operate the system will be trained in all aspects of financial management module, including SOE preparation.

Implementing Entity. IDENE is a semi-autonomous agency of the Special State Secretariat for the Development of the *Jequitinhonha Mucuri* Valleys and Northern Minas Gerais (SEDEVAN) and has sufficient financial and administrative autonomy to (i) flexibly operate the proposed project and (ii) provide the project with a network of infrastructure and human resources both at central and regional levels consistent with its responsibilities. There is an Operations Manual which is kept current and updated, and internal controls are adequate and efficient. A good filing system is in place.

Project's Financial Management System. The State Technical Unit for the *Produzir* project (in the State of Bahia) operates with the MIS that will be used under the project in Minas Gerais. This MIS is the overall management system for monitoring and controlling project execution and financial management, including accounting, payments, reporting, SOEs preparation. The MIS has been operational in Bahia for many years and, subsequent to the RPAP there, was upgraded to increase its efficiency.

Financing requests from the communities for all loan categories applicable to subprojects are entered through MIS, and after initial registration and management approval, the projects are implemented, monitored and controlled with all pertinent information stored in the MIS data base. MIS data base is used for the preparation of SOEs and all reports required by management. For the new Loan, a special screen will be added for the preparation of FMR for reporting purposes. The MIS records budgets, estimates and goals as per POA and compares these with actual figures and performance.

Furthermore, IDENE has in place adequate internal controls, is adequately staffed and has its own accounting system, which is necessary to comply with Corporate Law (Law 6404/76). This system is not integrated with MIS.

Reporting. Agreement was reached with regard to the format, content, and frequency of FMRs. IDENE will prepare quarterly Financial Monitoring Reports (FMRs) exclusively for project financial monitoring purposes. The FMRs were reviewed and designed in such a way that they can be used as the year-end Financial Statements for auditing purposes.

The following quarterly FMRs will be prepared:

- RSF – 1 - Sources and Uses of Funds, by disbursement cost categories, cumulative (project-to-date; year-to-date and for the period) vs. actual expenditures, including a variance analysis;
- RSF – 2 – SOE Statement. This Report will reconcile disbursements with Sources of Funds as per RSF –1 and with Bank’s Client Connection site;
- RSF – 3 – Special Account Statement.

Supervision. Financial management supervision will take place every six months and will include (a) reviewing of quarterly FMRs; (b) reviewing of the auditors’ reports and follow-up of issues raised by auditors in the management letter, as appropriate; (c) participation in project supervision; (d) following up on any financial reporting and disbursement issues; (e) updating the financial management rating in the Implementation Status and Results Report (ISR).

Funds flow. Funds will be deposited by the Bank from the Loan account to a special account with Banco do Brasil New York. An equivalent account will be opened in Belo Horizonte to receive funds upon withdrawal from the Special Account. From this account funds will be converted to R\$, according to project needs, and transferred to an operational account in Banco do Brasil for application in the individual subprojects or contracts PAC, FUMAC, FUMAC-P. Any balance left in the US\$ special account will be invested in the international financial market and interest will be credited to the project in due course. Funds will be invested by IDENE up to 30 days after withdrawal from special account, and SOEs for its replenishment will be submitted upon transfer of funds from the special account, according to the Fiduciary Guidelines for Community Driver Development Projects. Counterpart funds from the State of Minas Gerais will be requested by the STU and deposited in the project operational account. The communities’ contributions to subproject investments will be defined in the agreement (*convênio*) between the project Technical Unit and the beneficiary community association. This contribution will be computed as part of counterpart finance of the project. Simple, standard records, whose format will be included in the project Operational Manual, will be completed by a designated community representative. They will be used to record cash contributions, which will be directly paid to suppliers, materials and labor inputs, and will be subject to project audit procedures.

Disbursements. The borrower has decided that disbursements will adopt traditional, transaction-based disbursements mechanisms. Accordingly, disbursements will be made on the basis of SOEs/SOTs, except for goods and works exceeding US\$100,000 equivalent; contracts with consulting firms above US\$100,000 equivalent; and with individuals above US\$50,000, which will be supported by Summary Sheets (SS). The information required for the compilation of SOEs/SOTs, as well as all relevant supporting documentation, will be maintained in the MIS data base. All SOEs/SOTs disbursement applications will be forwarded to the World Bank in Brasília. At this stage, it is not envisaged that the Borrower will consider converting to report-based disbursements.

A special account, with a maximum authorized allocation of US\$3,500,000 (10% of Loan), will be opened to ensure a timely flow of funds and smooth project implementation. No disbursement trigger is required to raise the special account to its maximum authorized allocation.

The proposed Bank loan will be disbursed over a period of four years. The project is expected to be completed by the project’s Closing Date of January 31, 2010. The allocation of loan proceeds by disbursement category is shown in Table A.

Accounting Basis, Procedures and Policies. Project financial statements will be prepared, on a cash account basis, every quarter and annually. These statements will be prepared by IDENE, in accordance

with standards agreed during preparation phase, in line with accounting norms and guidance acceptable to the Bank. As part of the Operational Manual, a financial procedures manual will be prepared, and will provide guidance with regard to all financial and administrative routines.

Auditing Arrangements. Annual project financial statements will be audited by independent auditors, to be selected in accordance with acceptable auditing standards and in line with IFAC's norms and guidance, which is acceptable to the Bank, and according to the new Bank's audit policy. The external audit will be conducted under Terms of Reference acceptable to the Bank. Auditors will be required to issue a single opinion on project's financial statements, as per the guidelines "*Annual Financial Reporting and Auditing for World Bank-financed activities*", of June 30, 2003. Auditors will also have to produce a management letter, where relevant internal control weaknesses will be identified, which will contribute to the strengthening of the control environment. The auditor's report will be submitted to the Bank no later than six months after the closing of the borrower's fiscal year. If the loan becomes effective only on the second semester of 2005, it is possible that the first audit will cover a period up to 18 months, from the date of the first disbursement from the loan account (front end fee excluded) through December 31, 2006. This first audit would then be due on June 30, 2007.

Table A: Allocation of Loan Proceeds by Project Category

Expenditure Category	Project Cost in US\$ million	Financing Percentage	Allocation of Loan Proceeds in US\$ million
1. Grants for Community Subprojects (investments, technical assistance and start-up grants)			
(a) PAC Grants	8.60	75%	6.45
(b) FUMAC Grants	27.36	75%	20.52
(c) FUMAC-P Grants	2.67	75%	1.70
2. Consultants' services for Parts B and C of the Project	1.40	100%	1.40
3. Training for Parts B and C of the Project	1.50	100%	1.50
4. Administrative Costs			
(a) incremental operational costs	0.90	20%	0.18
(b) project supervision and monitoring costs	0.50	50%	0.25
5. Fee	0.35		0.35
6. Unallocated	3.87		2.65
Total	46.80		35.00

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Annex 6: Procurement Arrangements

A. General

Procurement for the proposed project would be carried out in accordance with the World Bank's "Guidelines: Procurement under IBRD Loans and IDA Credits" dated May 2004; and "Guidelines: Selection and Employment of Consultants by World Bank Borrowers" dated May 2004, and the provisions stipulated in the Legal Agreement. The general description of various items under different expenditure category is described below. For each contract to be financed by the Loan, the different procurement methods or consultant selection methods, the need for pre-qualification, estimated costs, prior review requirements, and time frame are agreed between the Borrower and the Bank project team in the Procurement Plan as applicable. The Procurement Plan will be updated at least annually or as required to reflect the actual project implementation needs and improvements in institutional capacity.

Procurement of Works: Works procured under this project, would include: (i) small works, costing less than US\$50,000, embodied in subprojects demanded by community associations and will vary according to the nature of the investment subproject, such as rural electrification, small dams, water supply systems, localized rural road improvement, housing improvement, among many others. Procurement of works under subprojects costing less than US\$50,000 equivalent would be carried out mainly through community participation which may include direct contracting by the communities. This procurement method is appropriate because most subprojects: (a) would be small and/or implemented in scattered or remote areas and therefore it will be difficult to obtain competitive proposals; (b) can be managed directly by rural communities, which will also contribute directly to the work through the donation of unskilled labor and local materials; (c) will be selected on the basis of willingness of the beneficiary communities to contribute to and physically supervise works execution; and (d) would provide means by which communities could play an active role in the local development process. Procurement of works under subprojects estimated to cost more than US\$50,000 equivalent and less than US\$100,000 equivalent, up to an aggregate amount of US\$1.1 million for works, would follow national shopping procedures. Contracts for subprojects estimated to cost more than US\$100,000 equivalent are subject to Bank no objection and would be awarded on the basis of National Competitive Bidding (NCB) procedures satisfactory to the Bank. All details of procurement to be carried out by community associations are fully described in the Project's Operational Manual.

When applicable, procurement will be done using Bank's Standard Bidding Documents (SBD) or National SBD agreed with the Bank.

Procurement of Goods: Most of the goods procured under this project, as in the case of works, are part of the subprojects demanded by community associations and will vary according to the nature of the investment subproject, such as farm tractor and implements, small product processing units, irrigation kits among many others. The vast majority of community subprojects involve both, works and goods. Normally goods and works come together and shall be procured as described above for works.

In addition to goods to be procured by community associations for the approved subprojects, IDENE, the STU, is expected to acquire some goods, such as computer equipments for the Project's MIS and training events, and vehicles for field supervision and monitoring work. Additional procurement of goods estimated to cost less than US\$100,000 equivalent, up to an aggregate amount of US\$1.7 million would follow national shopping procedures. Contracts estimated to cost more than US\$100,000 equivalent per contract would be awarded on the basis of National Competitive Bidding (NCB) procedures satisfactory to the Bank. Procurement of goods by communities is also described in the Operational Manual.

Procurement of non-consulting services: as in the case of works and goods, non-consulting services are part of the subprojects demanded by community associations and will vary according to the nature of the investment subproject, such as services provided by skilled and unskilled workers, among many others, and will be procured as described above for works and goods. As in the case of goods, IDENE is expected to acquire some non-consulting services, such as those required for training events and project dissemination campaigns. Shopping will be used for contracts estimated to cost less than US\$100,000 equivalent and Bank's SBD or National SBD agreed with the Bank for contracts estimated to cost more than US\$100,000 equivalent.

SELECTION OF CONSULTANTS:

Firms: The loan would finance contracts with consulting firms for an information campaign, technical assistance, studies and capacity building for the beneficiary communities and the State Technical Unit – IDENE. These contracts would be awarded following a Quality and Cost Based Selection (QCBS) process, in accordance with Section II of the Consultant Guidelines. However, services estimated to cost less than US\$200,000 equivalent per contract may be procured following Least Cost Selection procedures in accordance with provisions for paragraphs 3.1 and 3.6 of the Consultant Guidelines.

Individuals: The consulting services required for the Project include specialized advisory services and services to support project monitoring, such as MIS experts, which are appropriate for individual consultants. Individual consultants would be selected by comparison of qualifications of three candidates and retained in accordance with the provisions of Paragraph 5.1 through 5.3 of the Consultant Guidelines, or may be selected on a sole-source basis in accordance with Paragraph 5.3 and 5.4 of the Consultants Guidelines, subject to prior approval from the Bank. The competitive process followed to select individual consultants would be described in further detail in the Project Operational Manual.

Universities, Government Research Institutions, Training Institutions, NGOs and national and international technical assistance organizations are expected to be invited to participate in the selection process for the contracting of services, notably for provision of technical assistance and carrying out of studies, such as impact and result evaluation, physical performance study and various special studies. Whenever the short list includes a mix of categories of firms/groups the selection would be either quality-based (QBS) or based on the consultant's qualifications (CQS).

Community Participation: Goods and works costing \$50,000 equivalent or less per contract under Community Subprojects, may be procured in accordance with procedures acceptable to the Bank as provided for in paragraph 3.17 of the Guidelines (including direct contracting) and as set forth in the Operational Manual.

Operational Costs:

Sundry items, utilities and other incremental recurring costs would be financed on a 20 percent basis and would be procured using IDENE's administrative procedures which were reviewed and found acceptable to the Bank. In addition, the Bank would finance 50 percent of IDENE's incremental staff costs required for project supervision and monitoring.

B. Assessment of the agency's capacity to implement procurement

Project administration and monitoring will be the responsibility of the Minas Gerais Northern and Northeastern Development Institute, IDENE, the State Technical Unit (STU). A procurement capacity assessment of the STU was conducted by the Project Team's Procurement Specialist and was cleared by the Regional Procurement Advisor's Office (RPA). The "Overall Procurement Risk" was assessed as "LOW". Procurement responsibilities will be carried out by the IDENE's procurement staff that have performed successfully these functions during a previous similar loan and are well versed in Bank procurement policies and procedures. With the exception of some technical assistance for the beneficiaries which will be procured by the STU, it is anticipated that all procurement financed by the Project will be carried out by the grants beneficiaries. However, IDENE will procure goods and works on an exceptional basis on behalf of the beneficiaries which are deemed not to have sufficient capacity. It is anticipated that these procurement activities carried out by the STU, if any, will be limited. The beneficiaries' administrative capacity will be demonstrated in the subproject proposals and evaluated by the Implementing Agency. In addition, IDENE will exercise overall quality control of procurement financed by the subprojects.

C. Procurement Plan

A Procurement Plan was developed during appraisal. For the procurement to be carried out by the communities, it is not feasible to prepare a realistic plan as the subprojects are demand driven and their average value is expected to be less than the equivalent of US\$30,000. The Procurement Plan for IDENE will be updated in agreement with the Project Team annually to reflect the actual project implementation needs and improvements in institutional capacity.

D. Frequency of Procurement Supervision and Prior Review

Prior review will be required for all NCB contracts. In addition, the Bank will review the first contracts procured through shopping procedures for goods and works, respectively. Contracts with consulting firms estimated to cost US\$100,000 or more and with individual consultants estimated to cost US\$50,000 or more would be subject to the Bank's prior review. Assignments of a critical nature and amendments raising contract values above the said thresholds will also be subject to prior review.

Although the level of Bank prior review of procurement will be overall low, it will be compensated in several ways. First, reviews of procurement by community contracting will be carried out yearly during project implementation, under terms of reference agreed during project preparation. Second, cost comparisons of similar subprojects will be conducted using the project MIS in order to detect possible procurement problems and determine whether prices paid under community procurement were reasonable. Third, the project's annual physical performance evaluation will verify the physical implementation of subprojects and analyze procurement issues. Finally, during Bank supervision, additional random reviews will be conducted of subprojects, including field visits and review of subproject documentation.

Specific procurement supervision missions will take place every twelve months during the implementation period of the Project to visit the field to carry out post review of procurement actions. All regular bi-annual supervision missions will look at procurement aspects of the project and their findings will be reflected on the Implementation Status Reports (ISRs).

Attachment 1

Details of the Procurement Arrangements

1. Goods and Works and non consulting services

Types of contracts which will be procured following Direct Contracting, Local Shopping and NCB (SBD agreed with the Bank):

1 Ref. No.	2 Contract (Description)	3 Estimated Cost	4 Procurement Method	5 Review by Bank (Prior / Post)	6 Comments	7 Est'd Cost of Community Subprojects
1	Individual Community Subprojects	<US\$50,000 per subproject	Community Participation (3.17)	Post, during project field supervision on a sample basis	Some 1,823 community subprojects expected to be financed during the entire period of implementation of the Project	Estimated Total cost of these 1,823 subprojects: US\$39.0 million
2	Individual Community Subprojects	>US\$50,000 and < US\$100,000 per subproject	Same as above	Prior by IDENE of any contract over \$50,000	Up to 30 community subprojects of this size may be demanded during the entire period of implementation of the Project	Estimated Total Cost of these 30 community subprojects: US\$1.7 million
3	Individual Community Subprojects	>US\$100,000 per subproject	Same as above	Prior by IDENE of any contract over \$50,000	Up to 7 community subprojects of this size may be demanded during the entire period of implementation of the Project	Estimated Total Cost of these 7 community subprojects: US\$1.4 million
4	Goods and non consultant services to be contracted by IDENE	Total of Up to US\$ 3.2 million equivalent	Local shopping up to US\$100,000 equivalent and NCB for > US\$ 100,000 equiv.	Post, during supervision on sample basis Prior of NCBs only	Small individual acquisitions will occur during the entire period of implementation of the Project Few number of individual acquisitions expected	Estimated total cost of Up to US\$ 2.0 million equivalent Estimated total cost of up to US\$ 0.6 million equivalent
				Post review of shopping	Few number of individual acquisitions expected	Estimated total cost of up to US\$0.6 million equivalent

Consulting Services.

(a) List of Consulting Assignments

1	2	3	4	5	6	7
Ref. No.	Description of Assignment	Estimated Cost	Selection Method	Review by Bank (Prior / Post)	Expected Proposals Submission Date	Comments
1	Services to be provided by individual consultants	Individual contracts costing < US\$50,000 Individual contracts costing > US\$50,000	Section V of the Guidelines	Prior review for contracts over \$50,000 Post review for contracts less than \$50,000	Various contracts during the entire period of implementation of the project Some contracts during the entire period of implementation of the project	Estimated Total Cost: US\$1.4 million equivalent Estimated Total Cost: US\$0.5 million equivalent
2	Services to be provided by firms	contracts costing < US\$100,000 Individual contracts costing > US\$100,000	Least Cost , QCBS and single source selection QCBS Least Cost	Prior review of single source selection, post review for the rest Prior review	Some contracts during the entire period of implementation of the project Some contracts during the entire period of implementation of the project	Estimated Total Cost: US\$0.5 million equivalent Estimated Total Cost: US\$0.7 million equivalent

1 Services estimated to cost less than US\$200,000 may be procured following Least Cost Selection procedures

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Annex 7: Impact Analysis

Specific investments to be carried out under the proposed project will be decided by communities during implementation. As such, it not possible to know *a priori* how available resources will be allocated, or to estimate *ex ante* their cost-effectiveness, rate of return and associated fiscal impact. However, subprojects to be financed would, in general, be similar to those financed under previous and ongoing community-based rural development projects, both in Minas Gerais specifically (as under the R-NRDP) and across the wider Northeast Program³ more generally.

Several evaluations of the Northeast Program have taken place since its inception. In this Annex, a summary of the findings of these evaluations is presented, including preliminary findings of evaluations currently under implementation by researchers from the University of Campinas (FECAMP) and the University of São Paulo.

Background

Community-based activities were first introduced to Northeast Brazil in 1985 as a small-scale pilot component of the World Bank-financed Northeast Rural Development Program (NRDP). For several years following effectiveness, this community-based component - *Apoio às Pequenas Comunidades Rurais* (APCR) - was the only activity under the NRDP to disburse effectively and achieve positive results on the ground. The APCR, at a total component cost of US\$106 million, represented one of the most significant attempts of the Bank to make rural development projects more participatory. By relying on rural communities to organize, prioritize needs, and plan, execute and manage subprojects, this innovative component produced results that were both encouraging and replicable, demonstrating that by involving communities, poverty reduction could be achieved at a low per family cost. Equally important, the APCR demonstrated the ability of municipal governments – which were not originally included as project participants – to mobilize additional resources at a time of severe fiscal austerity

In late 1993, drawing on lessons from the APCR and similar schemes elsewhere in Latin America, the NRDP was reformulated into a full-scale community-based development program (R-NRDP). Significant features of the reformulation were: (i) decentralized decision-making, (ii) state and community counterpart funding responsibilities and (iii) delegated implementation from the Federal Government to the State and local levels. Subsequent evaluation of the Northeast program has confirmed that not only was it an effective model for rural poverty alleviation, but also became a key tool of the Northeast States for promoting organized decentralization, local development and community participation.

After field-testing the R-NRDP model for over three years, eight Northeast State Governments⁴ scaled-up the use of the methodology and ushered in the follow-on Rural Poverty Alleviation Projects (RPAPs), beginning in 1995/96, followed by a third generation of sub-national projects, now operational since 2001. Today, these projects are consolidating gains made under the previous generations of the Northeast program, while simultaneously integrating activities of the project municipal councils with the local government and, through more focused investment linked to the Human Development Index (HDI) and integrated with other State- and Federal-level interventions, promoting asset accumulation of the poorest.

³ In this annex, the Northeast Program refers to the set of CDD-based rural poverty reduction projects implemented since 1993 in the ten states of Northeast Brazil (which includes Northern Minas Gerais).

⁴ Bahia, Ceará, Maranhão, Paraíba, Pernambuco, Piauí, Rio Grande do Norte and Sergipe

Main conclusions of Evaluation studies

Northeast Program: Physical and Financial Performance

Since 1993, nearly 50,000 community subprojects have been financed under the Program, as demanded by over 40,000 community associations and benefiting approximately 2.5 million rural poor families in the ten Northeast States of Brazil (see Table 1). Overall, some US\$1.4 billion have been invested in the rural Northeast over this time period, of which the Bank has contributed US\$0.93 billion. Nearly 650,000 families have benefited from rural electrification investments (30% of all subprojects), while some 800,000 families now have access to safe water following the implementation of more than 13,500 water supply subprojects (27% of total). Additionally, some 25% of subprojects have opened income-generation opportunities for over 825,000 families. The implementation of the Northeast Program has depended heavily on strong project municipal councils, some 1,400 of which now operate across the 1,600 rural municipalities of the Northeast. These Councils, with majority participation composed of representatives from community associations, are decision-making bodies that prioritize community demands for the purposes of financing under the Program.

Table 1: Aggregate Results, Northeast Program (1993-present)

	<u>R-NRDP</u>	<u>RPAP</u>	<u>RPRP</u>	<u>Total</u>
Total Loan Resources Disbursed (US\$ million)	339	434	162	934
Total Project Resources (US\$ million)	616	578	214	1,408
Subprojects Implemented	17,860	23,573	8,317	49,750
Families Benefited	890,000	1,244,477	388,129	2,522,606
Community Associations	14,900	19,154	6,930	40,984
Rural Electrification Investments	5,040	8,537	1,372	14,949
Communities with Electricity	4,200	7,198	1,143	12,541
Families with Electricity	246,960	357,272	42,477	646,709
Water Supply Investments	2,700	7,786	3,093	13,579
Communities with Water Supply	2,250	6,528	2,578	11,356
Families with Water Supply	110,250	524,108	168,176	802,534
Productive Investments	5,893	4,887	1,806	12,586
Communities with Productive Investments	4,910	4,072	1,505	10,487
Families with Productive Investments	262,506	414,034	149,720	826,260

Source: MIS data from respective state projects

Effective Poverty Targeting: Various studies support the emphasis on self-targeting by community associations under the Northeast Program and confirm that the rural poor are being reached. In FECAMP (2004), the *ex ante* status of beneficiary communities (i.e., at the time they began their participation in the Program) was assessed across several demographic parameters: education, housing, employment and place of work, living conditions, household assets, and income. Using household surveys, the study found that 73% of beneficiary families had mean monthly incomes of less than one-half of the monthly minimum salary of R\$180. For another 25% of these households exceeded this figure, but in all cases was below R\$300. Given a median family size of five individuals, this translates into an *ex ante* per-capita income of US\$0.50 per day for nearly three-fourths of beneficiary families under the Program. An assessment of household food security for these same beneficiaries found that about 60% were “food-insecure”, with intermittent periods of hunger, prior to their participation in the Northeast Program (FECAMP 2004). This socio-economic profile of beneficiary families and their food security confirms that the Northeast Program is succeeding in targeting

rural poor families.⁵ Earlier findings from Van Zyl (2000) similarly validate the *ex ante* poverty status of these rural communities. Only 41% had access to electricity, while some 36% had minimal sanitation services – such as latrines. About one-fourth had access to (i) safe drinking water and (ii) local health services. Finally, about 40% of individuals in these beneficiary families were illiterate.

In terms of absolute reach of the Northeast Program, nearly one-half of the rural Northeast poor have benefited from subproject investments. In Bahia alone under its first-phase RPRP, some 45% of the rural poor participated in and benefited from subprojects, while about 10% of the rural poor in Pernambuco have benefited under the Program during 2002 and 2003. In Ceará, from 1995 through 2003, about 60% of the rural poor population had taken part in and benefited from subprojects financed under the Northeast Program.

Quality of Life

Despite difficulty of addressing issues of attribution and selection bias, there are strong indications of positive changes in the quality of life for those households which have benefited under the Northeast Program. FECAMP (2004) sampled 300 households across 130 municipalities in three Northeastern states to assess changes in living conditions among Program beneficiaries from 2000 to 2003. More than 80% of households indicated that their quality of life had improved as a result of the subproject investment, particularly in the areas of family health, physical living conditions (e.g., housing, sanitation, and durable goods) and nutrition. Mean household income also increased, especially in subprojects which financed housing upgrades and piped water. Overall, some 45% of beneficiary families had accessed to safe water and more than 70% had obtained electricity. Electrical appliance use increased by about 30%, while a majority of households also reported increased housing values. Greater access to safe water led to improved water quality (reported by 55% of respondents), reduced sickness caused by having to search for water and greater physical comfort (73% of respondents), more leisure time (70% of respondents) and reduced incidence of water-borne disease (50% of respondents). Some 20% of respondents further reported increased agricultural production as a result of subprojects which financed small dams in their community (FECAMP 2004).

Khan (2002) surveyed Northeast Program beneficiary households in 1998 -- the early stage of the RPAP -- and returned to these same households in 2001. A comparison of these two data sets revealed a marked increase in income, health and education, access to basic services and civic participation. Mean household incomes increased 79% over the three-year period among Program beneficiaries, at a time when per-capita incomes for the rural population as a whole were actually declining. In regard to health, Khan (2002) finds that the mean occurrence of household sickness declined from 1.4 to 0.4, while the incidence of diarrhea (as a proxy for water-borne diseases) decreased from 20% to 0.8%. The use of latrines increased from 17% to 41%, homes with piped water from 9% to 26%, and increase of 42% in home refrigerators, and a more than 100% increase in the purchase of motorcycles.

The bulk of subproject investments under the Northeast Program have been of the infrastructure type (72 percent), while social subprojects comprised less than 3 percent. Most of these subprojects are in the realm of core public services (water, sanitation, electrification, social investments). Numerous studies show that these basic services provide benefits that justify their universal provision. The cumulative experience of the Program has shown that the CDD approach to rural infrastructure and service delivery targeted to the rural poor can work in a cost effective manner in the Brazilian Northeast. Several aspects of project design help to

⁵ FECAMP (2001), drawing on National Household Survey data, compared *ex ante* demographics between the beneficiaries of the Bank-financed Land Reform and Poverty Alleviation Pilot Project (*Cédula da Terra*) and corroborated the self-selection targeting under this CDD project in that project beneficiaries clearly demonstrated worse socio-economic conditions, when compared to the general rural population.

ensure that the CDD mechanism to deliver communal infrastructure and social investments represents the least-cost, best alternative. First, the demand-driven nature of each subproject permits scarce resources to flow where they are most needed. Community participation, under the direction of the project Municipal Councils, ensures that the chosen subproject is the best alternative for the local community. Furthermore, the Program has, in the Municipal Councils, a democratic mechanism to prioritize the use of the resources available at the municipal level. Second, the use of standard technical designs (*projetos padrão*) for the most common types of infrastructure and social subprojects (including corresponding cost parameters) ensures that community associations employ least-cost models for subproject implementation. These standard designs also decrease search and information costs for community associations by providing established patterns of initiating and completing a subproject. The technical quality of these investments has been uniformly satisfactory. Third, the delegation of subproject implementation directly to the community associations has proven to generate cost savings, when compared to comparable quality works implemented by public sector agencies. The contracting procedures prescribed in the Project Operational Manual require direct contracting through competitive processes on all subprojects: the community association solicits three bids for the subproject and chooses the least-cost bid. These characteristics have contributed to the cost-effectiveness of the subprojects financed under the Program.

Based on the analysis of a random sample of subprojects (including ten categories which collectively represent some 80 percent of the types of subprojects being financed), the costs for infrastructure and social subprojects were found to be 30-50 percent less than projects of similar quality, when financed by the State. State-level Program evaluations have also examined the quality of (i) the materials used, (ii) overall implementation, and (iii) subproject operation. In all states surveyed, the majority of subprojects were found to be technically satisfactory and of good quality. Beneficiaries expressed their satisfaction with the quality of their subprojects and regarded more than 90 percent of all investments as being satisfactory overall.

The operation and maintenance of infrastructure and social subprojects has been also been satisfactory, with community associations charging user fees sufficient to operate and maintain the investments. Van Zyl (2000), based on information provided by the Project State Technical Units, found that a sample of 8,123 subprojects financed from 1995-98, finding that 7,240 of them, or 89 percent, were fully operational in March 2000. Furthermore, the same review found that there was no substantial difference in terms of sustainability across infrastructure, productive and social subprojects. Of 6,064 infrastructure, 1,820 productive and 239 social community subprojects, 89, 87 and 88 percent, respectively, were fully operational at the time of the study.

Financial Viability of Productive Subprojects

Benefit-cost ratios are high (greater than 2.0) for the principal types of productive subprojects analyzed. Analysis of selected productive subprojects also suggests that the investments are generally financially sustainable (see Table 2). Although beneficiary associations receive a one-time grant for their productive subproject, this investment is financially sustainable because cost recovery through user fees by the average beneficiary association is, in general, adequate to cover both O&M and replacement of the original investment long before the end of its useful economic life.

For illustrative purposes, twelve productive subprojects representing some of the most typical productive investments carried out under the Program were selected for financial analysis. Activity models were constructed for these subprojects, based on field interviews with the managers of the subprojects, supervision and project preparation missions, and consultation of standard project designs (*projetos padrão*) prepared by the State Technical Units. The subprojects analyzed are as follows:

Manioc Mill. Middle-size construction equipped with mill, press, oven and other equipment required to process cassava into flour. Investments include a pack animal to transport produce to and from the plant. The mill serves a local community of some 30 to 40 farming families. The plant operates around 100

days per year processing some 120 tons of cassava into approximately 30 tons of *farinha* and 4.8 tons of starch, employing one person to operate the plant during those days. Farmers are charged a users' fee of 15 percent of output. Association members normally pay a smaller fee than non-members.

Communal Tractor. 75 HP Tractor, plus trailer, grain sheller, grader and other equipment, including a garage. The tractor benefits an association of some 65 farming families. The tractor works for members and non-members providing land preparation, grain shelling and transport services. It works approximately 1,700 hour per year serving some 300 ha. User fees for members are smaller than prices charged by private tractor owners and fees charged to non-members. The subproject employs a full-time motorist hired by the association.

Small Irrigation 1. Purchase of 18 localized irrigation kits for 38 families to pump water to irrigate a total of some 29 ha (0.8 ha per family). The irrigation is accompanied by the introduction of a new technical package and two new cash crops, *chuchu* and *quiabo* (two high-price Brazilian vegetables with good local markets), which replace the existing traditional cultivation of corn, beans and bananas, providing a very good return.

Small Irrigation 2. Sprinkling irrigation system to irrigate 10 ha of previously uncultivated land with water pumped from a permanent water source, benefiting 10 farming families. Most of the irrigated land is used for traditional subsistence crops, corn and beans, although a cash crop-- watermelon -- is planted on one-third of the new area. Two crops are obtained per year.

Goat Production. Production of goats by a group of some 30 farmers, with an investment consisting of 120 breeding females and 4 breeding males. A pen, a fence and other facilities are constructed and 85 ha of improved pastures are installed. Income is derived from the sale (or self-consumption) of incremental animals and the sale (or self-consumption) of milk.

Animal Feed Production Equipment. Grinding machine and complementary equipment to produce animal feed from crop residuals, together with a small construction to shelter the machine. Farmers pay a small amount (R\$ 1.5) per hour to use the machine. From these payments, electricity and maintenance costs are covered and a small fund is formed. The machine works approximately six months per year. Raw materials and labor to operate the machine are supplied by users. The organization and supervision of machine use is freely supplied by association leaders.

Honey Production. Purchase of 340 beehives plus 2 decanters, 2 centrifuges and other apiculture and honey processing equipment to benefit an association of some 23 members with no previous apiculture experience. Training is provided along with the equipment. The beehives, located in 8 sites, are maintained by association members. They yield an annual output of some 8,200 kg of honey which is sold wholesale.

Local Bakery. Middle-size construction (120 sq. m) equipped with a gas oven and other baking facilities to produce various types of bread, with an average output of 130 kg of bread per day. Employment generated consists of a master baker and two full-time workers. Bread is sold locally in the surrounding communities.

Fish Farm. Five fish ponds of 2,200 m² each, with a capacity for 8,500 tilapia fish each. Ponds are rotated, with 4 ponds being permanently used at a time. Two harvests are collected per pond in a year, with a total output of 24,000 kg. of fish. Output is sold locally to middle-men. One person is employed half-time to feed the fish and another is employed half-time as watchman. Part-time labor is used to harvest the fish.

Cashew Processing Plant. Middle size plant plus equipment to process cashew nuts. Some 200 tons of cashew nuts are processed annually into 46 tons of roasted and packed cashew almonds, which are then sold wholesale. It operates during ten months of the year, employing around 6 operators. Cashew nuts are bought from surrounding farmers serving some 150 farmers with 1 to 5 ha of cashew trees each.

Jam Production Plant. Plant to process various local fruits into different types of jams and other confectionery products, producing an average of 175 kg per day of these products. Fruit and other inputs are bought by the plant. Products are sold retail locally and also wholesale to retailers. The subproject employs a plant manager and three permanent workers.

Small Dairy Plant. Middle size plant (155 sq. m) equipped with a pasteurization kit, cooling chamber and other facilities to pasteurize milk, with a capacity of 1,200 l. per day. The plant is supplied by around 400 cows with an average daily output of 3 liters per cow belonging to some 60 dairy farmers in a radius of 6 km. Employs a plant manager and 4 permanent workers.

The results of the financial analysis are summarized in Table 2.

Table 2: Results of the Financial Analysis of Selected Productive Subprojects

Type of Activity	Investment (R\$)	IRR (%)	NPV (at 10%)	Net Annual Income (R\$)	Years to Recover the Capital Invested
Manioc Mill	18,450	15.8	5,377	3,970	5.6
Communal Tractor	39,752	37.6	35,141	18,075	2.4
Small Irrigation 1	44,054	>50	327,366	90,781	0.9
Small Irrigation 2	28,311	28.1	23,573	15,238	3.3
Goat Production	43,346	16.5	16,925	12,180	5.8
Feed Production Equipment	6,730	15.4	1,831	1,149	5.9
Honey Production	26,102	16.8	9,112	7,252	5.5
Local Bakery	43,352	35.0	56,868	29,575	2.8
Fish Farm	46,104	15.6	13,739	13,162	5.6
Cashew Processing Plant	64,964	>50	288,790	72,195	1.1
Jam Production Plant	41,123	41.7	69,062	35,008	2.4
Small Dairy Plant	62,583	19.7	30,223	34,591	4.7

The investment cost of the subprojects ranges from around R\$7,000 to R\$65,000, which is typical of productive investments under the Program. All subprojects show satisfactory internal rates of return, some of them being very high. Less than six years are needed to recover the investment in all cases and less than 3.5 in half of the cases. The net incremental annual income or value-added generated by the subprojects (at full development) ranges from R\$1,149 for the feed preparation equipment to R\$90,781 in the case of one of the irrigation subprojects, with an average value of around R\$28,000 for an average investment of around R\$ 39,000. The Internal Rates of Return (IRRs) of these productive subprojects compare favorably with the real cost of borrowing by the Brazilian Government.⁶

Three categories of projects can be identified in the above illustrative sample. First among these are communal processing equipment or livestock activities which are simple to operate and well-known to farmers, meet community-wide needs, and directly benefit a majority of families in the community. The manioc mill, communal tractor, feed production equipment and goat production subprojects fall into this

⁶ A reference for such borrowing is the Long-term Interest Rate (TJLP).

category. The results summarized in Table 2 illustrate that these types of investments can be profitable. Their financial returns, however, are not high because benefits are passed on to farmers in the form of moderate user fees or because the activity in question is intrinsically not very profitable as in the case of small-scale goat rearing. These subprojects have the advantage of building on activities familiar to farmers, and have therefore little training requirements and simple management needs. They also have low marketing requirements since the community itself is the market for the service, and the outputs produced with the help of the service normally have regular marketing channels or are self-consumed.

The second category of subprojects are those promoting off- or on-farm productive activities which generate full time employment and considerable income for a particular group of farmers in the community. The small irrigation subprojects, as well as the honey production, jam production, fish farm and bakery subprojects, belong in this category. New activities producing a final consumption good to be sold in markets outside the community, exemplified by the honey production, fish farming and jam production subprojects, can be profitable and offer a source of income and employment to some members of the community; however, these subprojects tend to be demanding in terms of marketing and managerial skills. Other popular subprojects in this category are clothes-making and the production of different artisanal goods such as embroideries. These subprojects are normally part of industries where the entry cost is low and competition high, leaving small operating margins. The lack of working capital and the difficulty to establish a brand name to differentiate the product and place it in the best-paying markets are two common constraints.

Local bakeries, which are popular subprojects in some states, have little training and marketing requirements, and are similar to cassava mills or communal tractors to the extent that they cater for a local need and have therefore a local market, although in this case it is that of a final good rather than of a productive service, but they only offer employment and income to a reduced number of community members. The irrigation subprojects illustrate well that, whenever possible, irrigation together with the introduction of cash crops and an improved technical package is a profitable and cost-effective way of increasing income and employment in the semi-arid areas of the Brazilian Northeast, which can be successfully operated by local farmers at a very small scale. The contrast between the very high returns to investment of the first subproject, where new cash crops and technology were introduced alongside with irrigation, and the moderately high ones of the second subproject highlights the impact of profiting from the availability of irrigation water to introduce wider changes in the cropping system.

The last category of subprojects consists of processing plants requiring comparatively higher capital investment, which operate on a scale bigger than the communal equipment included in the first category, benefiting also farmers outside the local community and hence with impact at a more regional level. The dairy and cashew processing plants exemplify this type of subprojects.

To complete the financial analysis of productive subprojects, a weighted average is calculated for the IRRs of the activity models included in the sample. The shares of each of the twelve types of illustrative models (which were taken to represent other similar ones) in the total amount invested in community productive subprojects were used as weights. The resulting average IRR is 30.2 percent. This figure gives an indication of the overall profitability of the productive subprojects normally financed under the Program, but should not be taken as an *ex ante* estimate of the aggregate profitability of the productive investments, since it is not known *a priori* which type of subprojects will be most requested by beneficiary communities during the new project.

Sensitivity Analysis/ Switching Values of Critical Items: To examine the financial robustness of the productive subprojects, a sensitivity analysis was conducted on the illustrative activity models. Three scenarios are considered. In the first one, production is assumed to be 20 percent below the base case, because of, say, marketing problems. A 20 percent decrease in output causes a 20 percent decrease in revenue, but this is, to some extent, matched by a reduction in the use of inputs and hence in variable costs. In the second scenario, the price decreases 20 percent and revenue also decreases by the same proportion

without any compensating element. Finally, in the third scenario, an increase of 20 percent in the price of variable costs is assumed. The results of the sensitivity analysis are shown in Table 3.

Table 3: Results of the Sensitivity Analysis, Productive Subprojects

Type of Subproject	Base Case	Scenario 1 - 20% output	Scenario 2 - 20% price	Scenario 3 + 20% costs
Manioc Mill				
IRR (%)	15.8	11.5	10.1	14.4
NPV (R\$)	5,377	1,385	132	4,124
Communal Tractor				
IRR (%)	37.6	17.2	< 0	16.8
NPV (R\$)	35,141	10,836	-23,602	10,221
Small Irrigation 1				
IRR (%)	>50	>50	39.4	>50
NPV (R\$)	327,366	163,375	77,015	154,646
Small Irrigation 2				
IRR (%)	28.1	7.4	4.6	13.0
NPV (R\$)	23,573	-2,965	-6,057	3,546
Goat Production				
IRR (%)	16.5	12.8	11.5	15.2
NPV (R\$)	16,925	7,097	3,847	13,395
Feed Production Equipment				
IRR (%)	15.4	11.2	10.2	14.4
NPV (R\$)	1,831	397	62	1,496
Honey Production				
IRR (%)	16.8	10.0	7.2	11.6
NPV (R\$)	9,112	42	-3,635	2,162
Local Bakery				
IRR (%)	35.0	20.1	< 0	15.8
NPV (R\$)	56,868	22,451	-21,559	12,859
Fish Farm				
IRR (%)	15.6	9.3	< 0	< 0
NPV (R\$)	13,739	-1,732	-39,886	-26,024
Cashew Processing Plant				
IRR (%)	>50	> 50	48.3	>50
NPV (R\$)	288,790	210,642	132,561	201,015
Jam Production Plant				
IRR (%)	41.7	24.0	< 0	12.7
NPV (R\$)	69,062	29,690	-33,720	5,652
Small Dairy Plant				
IRR (%)	19.7	2.0	n.d. (*)	n.d. (*)
NPV (R\$)	30,223	-23,493	-138,697	-84,981

Social Capital: The Northeast Program has proven instrumental in sparking and promoting the formation and development of social capital, both within poor rural communities and as a contributing factor to good governance in those municipalities covered under the Program. Existing traditional solidarity and cooperation networks at the community level provide a foundation which is itself strengthened by the CDD approach pursued under the Northeast Program. As such the Program makes a quintessential contribution toward breaking down clientelistic relationships at the local level (which require the intervention of the

political elite) and forging a new dynamic – *horizontally*, by building ties among community associations representing the rural poor, and *vertically*, between the rural poor and the State (Costa and Rizvi 2003).

The Program has also been a primary force in the formation of a dense network of community associations, as evidenced by: (i) the growth in number of families joining and participating in organized civil society, (ii) the intensity of said participation and (iii) the increased role of these associations in representing the rural poor in local policy dialogue. Studies (Costa and Rizvi 2003) indicate that this transformation in *structural social capital* takes place more intensely in those communities which have implemented subprojects under the Northeast Program, in that the attainment of these immediate and concrete benefits prove indispensable to maintaining the organizational goals of the community association beyond the mere implementation of the investment. Fecamp (2003) and Costa and Rizvi (2003) also evaluated the legitimacy of these associations have universally observed a unidirectional transformation, in that, over time, these representative bodies are successful in significantly reducing intended manipulation by local traditional political elites and strengthening their sense of civic duty. When compared with community associations without subprojects, those associations benefited under the Program are more capable of: (i) responding to communal demands, (ii) resolving internal conflicts, (iii) effectively advocating for their membership, (iv) mobilizing financial and human resources and (v) solving local problems of the community. Community associations are increasingly viewed as “reference points” for the rural population, and are a primary source of help in time of need, often surpassing the more traditional kinship and friendship networks in this regard.

Experience under the Northeast Program has shown that social capital accumulation is both a benefit in its own right as well as an element of the success of rural CDD initiatives seeking poverty reduction. Household surveys and field observations reveal that more than two-thirds of beneficiaries agree that subproject implementation helped to unite the community and increased participation in the community association (Costa and Rizvi 2003). Several studies affirm that, since the 1980’s, community mobilization has been on the rise among the Northeast rural poor, and more so since the 1990’s, coinciding with the reformulation of the NRDP in 1993 into a participatory CDD mechanism (see van Zyl 2000, Costa and Rizvi 2003).

Forthcoming impact evaluations

A set of studies currently underway will apply a quasi-experimental model, combining both existing and new data sets. These studies will take advantage of the fact that, at the end of the RPAP, there was a significant backlog of fully evaluated and approved community subprojects, for which implementation was delayed due to lack of funds until the RPRP became effective. By comparing the difference between this “control group” and the “treatment group” of communities whose projects were funded in the last two years of the first round, the impact of the subprojects can be assessed on a number of indicators which are already available in the community profiles which accompany each subproject application. Measurement of community and individual capital stock will also be attempted, using recall to recover the time when the community subprojects were first approved. The differences between the two groups in the community indicators and in the capital stocks will provide a measure of the impact of the Northeast Program.

Some of the expected indicators to be assessed in this study are: (i) value of assets, consumption and production (household and community level), as indicator of wealth, (ii) Education (e.g., years in school), (iii) Health (e.g., incidence of illnesses), (iv) access to basic services (e.g., water, electricity, schools, health); and (v) Social capital (e.g., organizational capacity, collective action, network building and capacity to access other sources of funding/programs).

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Annex 8: Project Preparation and Supervision

	Planned	Actual
First Identification Mission	08/01/2001	08/2001
Appraisal	11/25/2001	11/2001
Negotiations	06/15/2003	07/2005
Board/RVP approval	09/2003	09/06/2005
Planned date of effectiveness	07/31/2005	09/30/2005
Planned date of mid-term review	07/01/2007	01/31/2008
Planned closing date	01/31/2010	07/31/2010

Key institutions responsible for preparation of the project:

State Secretariat of Planning and Management (SEPLAG)

Bank staff and consultants who worked on the project included:

Name	Title	Unit
Luis Coirolo	Lead Sector Specialist, Team Leader	LCSER
João Barbosa de Lucena	Consultant	LCSRE
Tulio Barbosa	Consultant	LCSRE
Edward Bresnyan	ET Consultant	LCSER
Raimundo Caminha	Consultant	LCSRE
Anna Roumani	ET Consultant	LCSER
Claudio Mittelstaedt	ET Consultant	LCOAA
Mariana Montiel	Senior Council	LEGLA
Marta Molares-Halberg	Lead Council	LEGLA
Jose Augusto Carvalho	Consultant	LEGLA
Luiz Gazoni	Lead Procurement Specialist	LCOPR
Irani Escolano	Procurement Analyst	LCSES

Peer Reviewer:

Klaus Deininger	Lead Economist	DECRG
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Bank funds expended to date on project preparation:

1. Bank resources: 174,434
2. Trust funds: -0-
3. Total: 174,434

Estimated Approval and Supervision costs:

1. Remaining costs to approval: 7,500
2. Estimated annual supervision cost: 80,000

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Annex 9: Documents in the Project File

- A. Project Implementation Plan
 - Draft Operational Manual for Minas Gerais

- B. Bank Staff Assessments
 - Sector Issues and Concept
 - Government of Minas Gerais Project Document (March 2001)
 - Project Economic and Financial Analysis
 - Cost-Benefit Analysis for selected Subprojects
 - Fiscal Impact
 - Project Implementation Arrangements
 - Community Organizations
 - State Technical Units (STUs)
 - Secretariat of Planning
 - Secretariat of Agriculture, Supply and Fisheries
 - NGOS
 - Private Sector
 - Social Capital Assessment
 - Project Monitoring
 - Project Database
 - Monitoring Activities
 - Project Reporting

- C. Background Studies (see also references in Annex 7)
 - Mid Term Review of Rural Poverty Alleviation Program in Bahia, Ceara and Pernambuco.
 - Rural Development Programs for Brazil's Northeast: An Interim Assessment

*Including electronic files.

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Annex 10: Statement of Loans and Credits

Project ID	FY	Purpose	Original Amount in US\$ Millions						Difference between expected and actual disbursements	
			IBRD	IDA	SF	GEF	Cancel.	Undisb.	Orig.	Frm. Rev'd
P082523	2006	BR-Human Development TA	8.00	0.00	0.00	0.00	0.00	8.00	0.00	0.00
P082142	2006	BR-Ceara Multi-sector Social Inclus Dev	149.00	0.00	0.00	0.00	0.00	149.75	0.00	0.00
P069934	2005	BR-PERNAMBUCO INTEG DEVT: EDUC QUAL IMPR	31.50	0.00	0.00	0.00	0.00	31.50	3.50	0.00
P078716	2005	BR(CRL1)Prog Growth for Housing	502.52	0.00	0.00	0.00	0.00	502.52	0.00	0.00
P076924	2005	BR-(Amapa) Sustainable Communities	4.80	0.00	0.00	0.00	0.00	4.80	0.04	0.00
P082328	2005	BR-Integ.Munic.Proj.-Betim Municipality	24.08	0.00	0.00	0.00	0.00	23.95	2.98	0.00
P083533	2005	BR TA-Sustain. & Equit Growth	12.12	0.00	0.00	0.00	0.00	12.12	1.00	0.00
P086525	2005	BR PRGM. FISCAL REF - SOCIAL SEC REFORM	658.30	0.00	0.00	0.00	0.00	658.30	0.00	0.00
P087711	2005	BR Espirito Santo Wtr & Coastal Pollu	36.00	0.00	0.00	0.00	0.00	33.82	0.42	0.00
P060573	2004	BR Tocantins Sustainable Regional Dev	60.00	0.00	0.00	0.00	0.00	57.40	15.40	0.00
P087713	2004	BR (CRL1) Bolsa Familia 1st APL	572.20	0.00	0.00	0.00	0.00	464.34	-10.76	0.00
P080830	2004	BR Maranhao Integrated: Rural Dev	30.00	0.00	0.00	0.00	0.00	30.00	5.20	0.00
P083013	2004	BR Disease Surveillance & Control APL 2	100.00	0.00	0.00	0.00	0.00	99.00	-0.50	0.00
P058503	2003	GEF BR Amazon Region Prot Areas (ARPA)	0.00	0.00	0.00	30.00	0.00	22.68	20.00	0.00
P076977	2003	BR-Energy Sector TA Project	12.12	0.00	0.00	0.00	0.00	12.00	6.00	0.00
P054119	2003	BR BAHIA DEVT (HEALTH)	30.00	0.00	0.00	0.00	0.00	26.48	11.48	0.00
P070827	2003	BR-2nd APL BAHIA DEV. EDUCATION PROJECT	60.00	0.00	0.00	0.00	0.00	28.59	18.91	0.00
P080400	2003	BR-AIDS & STD Control 3	100.00	0.00	0.00	0.00	0.00	91.88	38.18	0.00
P049265	2003	BR-RECIFE URBAN UPGRADING PROJECT	46.00	0.00	0.00	0.00	0.00	44.39	10.21	0.00
P074777	2003	BR-Municipal Pension Reform TAL	5.00	0.00	0.00	0.00	0.00	4.91	4.91	0.41
P060221	2002	BR FORTALEZA METROPOLITAN TRANSPORT PROJ	85.00	0.00	0.00	0.00	0.00	111.47	74.02	0.00
P043869	2002	BR SANTA CATARINA NATURAL RESOURC & POV.	62.80	0.00	0.00	0.00	0.00	55.82	21.14	0.00
P057665	2002	BR-FAMILY HEALTH EXTENSION PROJECT	68.00	0.00	0.00	0.00	0.00	42.00	36.40	0.00
P057653	2002	BR- FUNDESCOLA IIIA	160.00	0.00	0.00	0.00	0.00	122.39	-99.88	0.00
P055954	2002	BR GOIÁS STATE HIGHWAY MANAGEMENT	65.00	0.00	0.00	0.00	0.00	26.59	26.59	-0.49
P074085	2002	BR Sergipe Rural Poverty Reduction	20.80	0.00	0.00	0.00	0.00	1.23	-0.77	0.00
P051696	2002	BR SÃO PAULO METRO LINE 4 PROJECT	209.00	0.00	0.00	0.00	0.00	156.89	147.69	-5.11
P066170	2002	BR-RGN 2ND Rural Poverty Reduction	22.50	0.00	0.00	0.00	0.00	11.60	8.40	0.00
P070552	2002	GEF BR PARANA BIODIVERSITY PROJECT	0.00	0.00	0.00	8.00	0.00	6.06	6.91	0.00
P073192	2002	BR TA Financial Sector	14.50	0.00	0.00	0.00	0.00	9.30	9.30	0.00
P073294	2001	BR Fiscal & Fin. Mgmt. TAL	8.88	0.00	0.00	0.00	0.00	6.74	5.78	0.00

P059566	2001	BR- CEARA BASIC EDUCATION	90.00	0.00	0.00	0.00	0.00	61.18	-28.82	0.00
P050881	2001	BR PIAUI RURAL POVERTY REDUCTION PROJECT	22.50	0.00	0.00	0.00	0.00	4.11	4.11	-0.49
P050880	2001	BR Pernambuco Rural Poverty Reduction	30.10	0.00	0.00	0.00	0.00	6.87	6.87	0.00
P050875	2001	BR Ceara Rural Poverty Reduction Project	37.50	0.00	0.00	0.00	0.00	1.82	1.82	0.00
P050772	2001	BR LAND-BASED POVRTY ALLEVIATION I (SIM)	202.10	0.00	0.00	0.00	58.13	150.32	152.74	0.00
P006449	2000	BR CEARA WTR MGT PROGERIRH SIM	136.00	0.00	0.00	0.00	0.00	57.16	57.16	14.20
P035741	2000	BR NATL ENV 2	15.00	0.00	0.00	0.00	6.00	1.93	7.93	4.74
P047309	2000	BR ENERGY EFFICIENCY (GEF)	0.00	0.00	0.00	15.00	3.10	1.57	4.67	1.64
P050776	2000	BR NE Microfinance Development	50.00	0.00	0.00	0.00	0.00	21.20	16.30	0.00
P039199	2000	BR PROSANEAR 2	30.30	0.00	0.00	0.00	6.40	18.81	25.21	18.81
P048869	1999	BR SALVADOR URBAN TRANS	150.00	0.00	0.00	0.00	32.00	53.95	85.95	0.00
P050763	1999	BR- Fundescola 2	202.00	0.00	0.00	0.00	10.86	4.24	15.10	0.00
P006474	1998	BR LAND MGT 3 (SAO PAULO)	55.00	0.00	0.00	0.00	10.00	33.16	43.16	30.28
P042565	1998	BR PARAIBA R.POVERTY	60.00	0.00	0.00	0.00	0.00	4.47	4.47	0.00
P043420	1998	BR WATER S.MOD.2	150.00	0.00	0.00	0.00	125.00	19.33	144.30	7.53
P043421	1998	BR RJ M.TRANSIT PRJ.	186.00	0.00	0.00	0.00	27.78	79.07	106.85	11.14
P057910	1998	BR PENSION REFORM LIL	5.00	0.00	0.00	0.00	0.50	1.49	1.99	0.90
P038895	1998	BR FED.WTR MGT	198.00	0.00	0.00	0.00	40.00	47.31	87.31	32.63
P043868	1997	BR RGS LAND MGT/POVERTY	100.00	0.00	0.00	0.00	0.00	1.97	1.97	0.00
P043873	1997	BR AG TECH DEV.	60.00	0.00	0.00	0.00	0.00	14.09	14.09	14.09
P034578	1997	BR RGS Highway MGT	70.00	0.00	0.00	0.00	0.00	13.72	13.72	-1.02
P006532	1997	BR FED HWY DECENTR	300.00	0.00	0.00	0.00	50.00	44.15	94.15	0.00
P037828	1996	BR (PR)R.POVERTY	175.00	0.00	0.00	0.00	10.00	22.23	32.23	-7.78
P006210	1996	GEF BR-NATL BIODIVERSITY	0.00	0.00	0.00	10.00	0.00	1.36	1.31	0.72
Total:			5,474.62	0.00	0.00	63.00	379.77	3,514.03	1,257.14	122.20

BRAZIL
STATEMENT OF IFC's
Held and Disbursed Portfolio
In Millions of US Dollars

FY Approval	Company	Committed				Disbursed			
		IFC				IFC			
		Loan	Equity	Quasi	Partic.	Loan	Equity	Quasi	Partic.
2005	ABN AMRO REAL	7.00	0.00	0.00	0.00	7.00	0.00	0.00	0.00
2001	AG Concession	0.00	15.00	15.00	0.00	0.00	14.07	0.00	0.00
2002/05	Amaggi	30.00	0.00	0.00	0.00	15.00	0.00	0.00	0.00
2002	Andrade G. SA	25.67	0.00	10.00	15.15	25.67	0.00	10.00	15.15
2001	Apolo	7.21	0.00	0.00	0.00	4.71	0.00	0.00	0.00
2005	Aracruz	50.00	0.00	0.00	0.00	50.00	0.00	0.00	0.00
1998	Arteb	20.00	0.00	0.00	18.33	20.00	0.00	0.00	18.33
1999	AutoBAn	22.73	0.00	0.00	17.25	22.73	0.00	0.00	17.25
1998	BSC	1.33	0.00	0.00	0.55	1.26	0.00	0.00	0.55

1996	Banco Bradesco	0.68	0.00	0.00	1.00	0.68	0.00	0.00	1.00
2001	Brazil CGFund	0.00	20.00	0.00	0.00	0.00	2.60	0.00	0.00
1994/96	CHAPECO	1.78	0.00	0.00	5.26	1.78	0.00	0.00	5.26
2002/04	CN Odebrecht	25.00	0.00	0.00	0.00	25.00	0.00	0.00	0.00
2003	CPFL Energia	0.00	0.00	40.00	0.00	0.00	0.00	40.00	0.00
1992	CRP-Caderi	0.00	0.17	0.00	0.00	0.00	0.17	0.00	0.00
1996/97	CTBC Telecom	0.00	6.54	0.00	0.00	0.00	6.54	0.00	0.00
1999	Cibrasec	0.00	3.22	0.00	0.00	0.00	2.71	0.00	0.00
2004	Comgas	45.00	0.00	0.00	45.00	12.50	0.00	0.00	12.50
1997/00	Coteminas	0.00	0.18	0.00	0.00	0.00	0.18	0.00	0.00
1980/92	DENPASA	0.00	0.06	0.00	0.00	0.00	0.06	0.00	0.00
1998	Dixie Toga	0.00	10.36	0.00	0.00	0.00	10.36	0.00	0.00
1997	Duratex	3.24	0.00	3.00	2.55	3.24	0.00	3.00	2.55
1999	Eliane	19.20	0.00	13.00	0.00	19.20	0.00	13.00	0.00
1998	Empesca	5.00	0.00	10.00	0.00	5.00	0.00	10.00	0.00
2000/04	Fleury	20.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
1998	Fosfertil	4.55	0.00	0.00	16.70	4.55	0.00	0.00	16.70
1998	Fras-le	5.33	0.00	9.99	0.00	5.33	0.00	6.69	0.00
1994	GAVEA	0.00	0.00	5.50	0.00	0.00	0.00	5.50	0.00
	GP Cptl Rstrctd	0.00	3.02	0.00	0.00	0.00	2.95	0.00	0.00
2001	GPC	0.00	0.00	9.00	0.00	0.00	0.00	9.00	0.00
1997	Guilman-Amorim	20.99	0.00	0.00	28.74	20.99	0.00	0.00	28.74
1998	Icatu Equity	0.00	5.79	0.00	0.00	0.00	4.42	0.00	0.00
1999	Innova SA	12.50	5.00	0.00	30.00	12.50	5.00	0.00	30.00
1980/87/97	Ipiranga	23.62	0.00	0.00	39.75	23.62	0.00	0.00	39.75
1999	Itaberaba	0.00	2.28	0.00	0.00	0.00	2.28	0.00	0.00
2000/02	Itau-BBA	83.63	0.00	0.00	0.00	51.48	0.00	0.00	0.00
1999	JOSAPAR	7.57	0.00	7.00	0.00	2.57	0.00	7.00	0.00
1995	Lojas Americana	2.00	0.00	0.00	0.00	2.00	0.00	0.00	0.00
1992/99	MBR	12.50	0.00	0.00	0.00	12.50	0.00	0.00	0.00
2002	Macaé	38.27	0.00	10.00	31.25	38.27	0.00	10.00	31.25
2002	Microinvest	0.00	1.25	0.00	0.00	0.00	0.42	0.00	0.00
2002/05	Net Servicos	0.00	7.37	0.00	0.00	0.00	7.37	0.00	0.00
1994	Para Pigmentos	6.45	0.00	9.00	0.00	6.45	0.00	9.00	0.00
1996	Perdigao	2.19	0.00	0.00	0.00	2.19	0.00	0.00	0.00
1994/00/02	Portobello	0.00	1.15	0.00	0.00	0.00	1.15	0.00	0.00
2000	Puras	1.33	0.00	1.00	0.00	1.33	0.00	1.00	0.00
2003/04	Queiroz Galvao	0.60	0.00	0.00	0.00	0.08	0.00	0.00	0.00
	Randon Impl Part	3.27	0.00	3.00	0.00	3.27	0.00	3.00	0.00
1997/03	SP Alpargatas	30.00	0.00	0.00	0.00	15.00	0.00	0.00	0.00
1997	Sadia	5.84	0.00	3.67	37.06	5.84	0.00	3.67	37.06
2002	Salutia	0.00	0.01	0.00	0.00	0.00	0.00	0.00	0.00
1997	Samarco	5.40	0.00	0.00	0.00	5.40	0.00	0.00	0.00
1998	Saraiva	3.46	2.40	0.00	0.00	3.46	2.40	0.00	0.00
2003	Satipel	12.86	0.00	10.00	0.00	12.86	0.00	10.00	0.00
2000	Sepetiba	26.68	0.00	5.00	0.00	11.68	0.00	5.00	0.00
1999	Sudamerica	0.00	7.35	0.00	0.00	0.00	7.35	0.00	0.00
2001	Synteko	15.43	0.00	0.00	0.00	15.43	0.00	0.00	0.00
1998/04	Tecon Rio Grande	8.10	0.00	0.00	8.10	0.00	0.00	0.00	0.00

2001/03	Tecon Salvador	0.00	0.56	0.00	0.00	0.00	0.55	0.00	0.00
2004	TriBanco	10.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
2002	UP Offshore	11.60	10.00	0.00	30.00	0.00	3.00	0.00	0.00
2002/04	Unibanco	20.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Total portfolio:		658.01	101.71	164.16	326.69	470.57	73.58	145.86	256.09

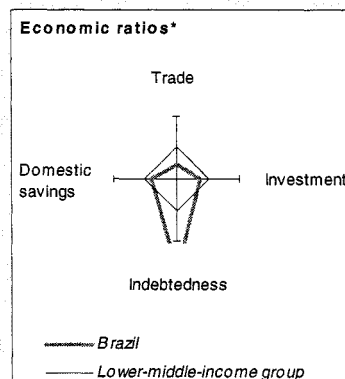
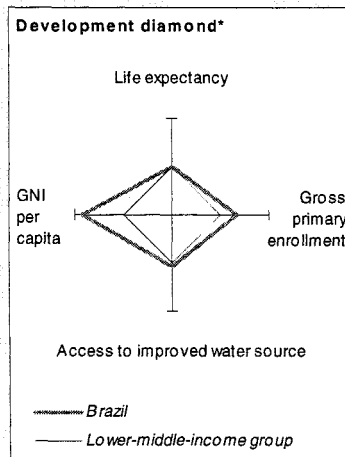
FY Approval	Company	Approvals Pending Commitment			
		Loan	Equity	Quasi	Partic.
2005	ABN AMRO REAL	0.03	0.00	0.00	0.00
2000	BBA	0.01	0.00	0.00	0.00
2002	Banco Itau-BBA	0.00	0.00	0.00	0.10
1999	Cibrasec	0.00	0.00	0.00	0.00
2005	Cosan SAIC	0.05	0.02	0.00	0.00
2005	Embraer	0.04	0.00	0.00	0.10
2005	GP Capital III	0.00	0.02	0.00	0.00
2005	LOJAS II	0.04	0.00	0.00	0.00
2002	Suape ICT	0.01	0.00	0.00	0.00
2004	TermoFortaleza	0.06	0.00	0.01	0.11
Total pending commitment:		0.24	0.04	0.01	0.31

BRAZIL

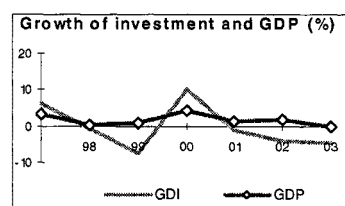
Rural Poverty Reduction Project - Minas Gerais

Annex 11: Country at a Glance

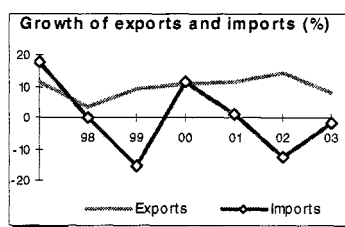
	Brazil	Latin America & Carib.	Lower-middle-income		
POVERTY and SOCIAL					
2003					
Population, mid-year (millions)	176.6	534	2,655		
GNI per capita (Atlas method, US\$)	2,720	3,260	1,480		
GNI (Atlas method, US\$ billions)	479.5	1,741	3,934		
Average annual growth, 1997-03					
Population (%)	1.3	1.5	0.9		
Labor force (%)	1.6	2.1	1.2		
Most recent estimate (latest year available, 1997-03)					
Poverty (% of population below national poverty line)	22	..	..
Urban population (% of total population)	83	77	50		
Life expectancy at birth (years)	69	71	69		
Infant mortality (per 1,000 live births)	33	28	32		
Child malnutrition (% of children under 5)	6	..	11		
Access to an improved water source (% of population)	87	86	81		
Illiteracy (% of population age 15+)	14	11	10		
Gross primary enrollment (% of school-age population)	148	129	112		
Male	153	131	113		
Female	144	126	111		
KEY ECONOMIC RATIOS and LONG-TERM TRENDS					
	1983	1993	2002	2003	
GDP (US\$ billions)	203.3	438.3	460.8	492.3	
Gross domestic investment/GDP	16.7	20.8	19.8	20.1	
Exports of goods and services/GDP	11.4	10.5	15.5	16.9	
Gross domestic savings/GDP	19.1	22.3	21.8	23.8	
Gross national savings/GDP	..	20.2	18.5	20.7	
Current account balance/GDP	-3.4	-0.1	-1.6	0.8	
Interest payments/GDP	3.9	0.6	2.9	2.7	
Total debt/GDP	48.5	32.9	49.6	48.0	
Total debt service/exports	54.7	24.4	70.3	65.1	
Present value of debt/GDP	52.6	..	
Present value of debt/exports	329.6	..	
	1983-93	1993-03	2002	2003	2003-07
(average annual growth)					
GDP	2.4	2.3	1.9	-0.2	3.9
GDP per capita	0.6	1.0	0.7	-1.4	3.2



	1983	1993	2002	2003
STRUCTURE of the ECONOMY				
<i>(% of GDP)</i>				
Agriculture	10.9	7.6	5.8	5.8
Industry	44.0	41.6	20.6	19.1
Manufacturing	33.2	25.0	12.4	11.4
Services	45.1	50.8	73.5	75.1
Private consumption	71.2	60.1	58.1	56.9
General government consumption	9.7	17.7	20.1	19.3
Imports of goods and services	9.0	9.1	13.4	13.1

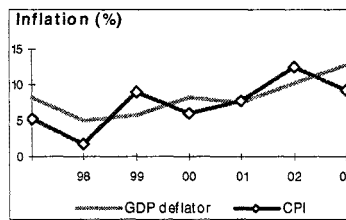


	1983-93	1993-03	2002	2003
<i>(average annual growth)</i>				
Agriculture	2.4	3.9	5.0	5.5
Industry	1.2	1.8	2.6	-1.0
Manufacturing	0.0	1.4	1.4	2.7
Services	3.0	2.5	1.6	-0.2
Private consumption	0.8	1.9	-0.4	-3.3
General government consumption	6.4	2.0	1.0	11.6
Gross domestic investment	4.9	1.2	-4.3	-4.5
Imports of goods and services	5.9	4.0	-12.3	-1.9



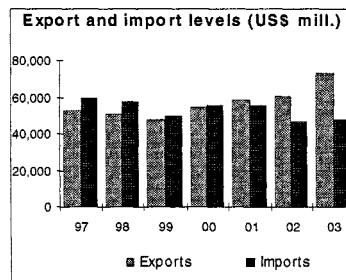
PRICES and GOVERNMENT FINANCE

	1983	1993	2002	2003
Domestic prices				
<i>(% change)</i>				
Consumer prices	135.0	1,928.0	12.5	9.3
Implicit GDP deflator	140.2	1,996.6	10.2	12.8
Government finance				
<i>(% of GDP, includes current grants)</i>				
Current revenue	..	..	23.9	23.7
Current budget balance	..	..	2.8	3.0
Overall surplus/deficit	..	..	..	..



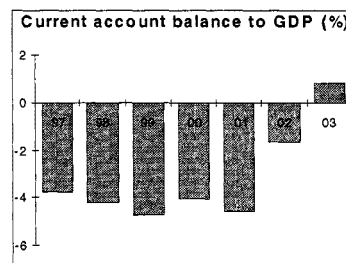
TRADE

	1983	1993	2002	2003
<i>(US\$ millions)</i>				
Total exports (fob)	..	38,563	60,362	73,084
Coffee	..	2,466	3,049	3,456
Soybeans	..	3,074	3,032	4,290
Manufactures	..	25,935	33,000	39,653
Total imports (cif)	..	25,256	47,237	48,260
Food	..	1,089	1,085	924
Fuel and energy	..	2,139	6,240	6,577
Capital goods	..	8,369	11,643	10,348
Export price index (1995=100)	80	91	88	95
Import price index (1995=100)	57	67	91	90
Terms of trade (1995=100)	140	136	97	105



BALANCE of PAYMENTS

	1983	1993	2002	2003
<i>(US\$ millions)</i>				
Exports of goods and services	23,611	41,616	69,913	83,567
Imports of goods and services	19,534	31,795	61,709	63,819
Resource balance	4,077	9,821	8,204	19,748
Net income	-11,022	-12,099	-18,191	-18,552
Net current transfers	108	1,686	2,390	2,867
Current account balance	-6,837	-592	-7,597	4,063
Financing items (net)	4,946	9,805	-6,003	-963
Changes in net reserves	1,891	-9,213	13,600	-3,100
Memo:				
Reserves including gold (US\$ millions)	4,563	32,211	37,823	49,296
Conversion rate (DEC, local/US\$)	2.10E-10	3.22E-2	2.9	3.1



EXTERNAL DEBT and RESOURCE FLOWS

	1983	1993	2002	2003
<i>(US\$ millions)</i>				
Total debt outstanding and disbursed	98,525	144,104	228,662	236,245
IBRD	3,628	6,575	8,585	8,588
IDA	0	0	0	0
Total debt service	13,304	10,883	51,636	56,793
IBRD	507	1,858	15,191	2,010
IDA	0	0	0	0
Composition of net resource flows				
Official grants	16	59	0	..
Official creditors	1,576	-1,033	916	..
Private creditors	2,659	10,073	-9,541	233
Foreign direct investment	1,609	1,292	0	..
Portfolio equity	0	6,570	0	..
World Bank program				
Commitments	2,067	636	1,276	1,217
Disbursements	1,204	471	1,384	1,291
Principal repayments	270	1,279	1,063	1,633

