Report No. PID9725

Project Name	Mongolia-Sustainable Livelihoods Project
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Sector	Livestock;Decentralization; Other Social Protection
Project	MNPE67770
Borrower(s)	MONGOLIA
Implementing Agency(ies)	HOUSEHOLD LIVELIHOODS SUPPORT PROGRAM OFFICE Address: Khuvsgalchdyn Avenue, Ulaanbaatar-38, Mongolia Contact Person: Mr Ch. Khurelbaatar, Director Tel: 976-11-323500, 322465 Fax: 976-11-328107 Email: mppl@magicnet.mn
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1. Country and Sector Background

Increasing poverty and inequality

Following the exceptionally difficult years of the early 1990s, and despite four years of reasonable growth and low inflation in the mid- to late-1990s, poverty and inequality continue to be serious problems in both rural and urban areas. The Living Standards Measurement Surveys conducted in 1995 and 1998 found that the overall headcount of poor people remained stable over 1995-98 at around 36% of the population; the depth and severity of poverty, however, worsened over this period.

The findings of the Bank-supported Participatory Living Standards Assessment 2000 (PLSA) are consistent with these trends and confirm that polarization between rich and poor intensified between 1995 and 2000. While some households managed to improve their living standards and climb out of poverty over the period 1995-2000, it appears that many more fell behind, and those already below the poverty line fell even further behind. Vulnerability to risk was regarded as the most important dimension of poverty to address. Analysis of the various shocks and stresses that triggered a downward trend of impoverishment among 180 low-income middle, poor and very poor households suggests that loss of employment, natural hazards (dzud), and the cost of health and education were the most common risk factors. Fuel-price increases leading to declining producer terms of trade, theft of assets (especially livestock), and other lifecycle events (e.g. death, illness) were other commonly experienced factors that could trigger a process of impoverishment. A clear, common perception emerged from over 200 focus group discussions conducted throughout the country that by 2000, in urban areas, poor and very poor households accounted for the majority of residents; while in rural areas, the poor and very poor made up around half of all households. These

findings suggest that government efforts should be stepped up to ensure that the gains from economic growth are more widely shared.

Between 1994 and 2000, the principal means by which poverty reduction was pursued in Mongolia was through the National Poverty Alleviation Program (NPAP), a US$19 million inter-sectoral program supported by a range of multilateral and bilateral agencies and international NGOs. World Bank was the major donor to NPAP, contributing US$10 million through the Poverty Alleviation for Vulnerable Groups Project (PAVGP) (Cr. 2760-MN) from 1996 to 2000. The intensive-learning ICR for this project and a joint Government-donor evaluation of NPAP as a whole concluded that NPAP had provided valuable support to local governments for the rehabilitation of social and economic infrastructure, but the direct income-generation support to poor households was much smaller than ought to have been realized, and benefited perhaps not more than 20% of poor households. Achievements in reducing rural poverty were particularly limited. NPAP was unable to reduce poverty on a significant scale in the absence of a supportive economic policy environment. Since July 2000, however, the new Government has made poverty reduction one of the highest priorities in its Action Plan and has begun to address marked rural-urban disparities with a stronger focus on rural development. The Interim Poverty Reduction Strategy Paper (I-PRSP) has been completed and the full PRSP is in preparation. Government anticipates that the proposed Sustainable Livelihoods Program will make a major operational contribution to the achievement of the PRSP's goals.

Ambiguous institutional structure

During the early years of economic transition in the early 1990s, poverty was considered mainly a 'social policy' issue affecting 'vulnerable groups' such as orphans, the disabled, the elderly, the unemployed, low-income households with many children, and female-headed households. Accordingly, a single line ministry (currently named the Ministry of Social Welfare and Labor) was designated under the Law on Government to take the lead on poverty issues. The Poverty Alleviation Program Office (PAPO) - the executing agency for NPAP - was constituted as "an autonomous entity under the supervision of the National Poverty Alleviation Commitee (NPAC), reporting directly to the Minister of MoSWL in his capacity as Deputy Chairman of NPAC". This proved to be ambiguous in practice. MoSWL considered PAPO to be under its own authority, while the donors considered PAPO to be an autonomous entity reporting to NPAC as an inter-ministerial committee responsible for coordinating anti-poverty efforts. Throughout the course of NPAP, MoSWL's repeated efforts to block decisions taken by PAPO proved highly disruptive to implementation. In an effort to resolve the issue in early 1996, GoM issued a statement that PAPO would thereafter report directly to the Prime Minister, in his capacity as Chairman of NPAC, thus making PAPO operationally independent of the MoSWL. This failed to resolve the issue, however, and inter-agency struggles for control over NPAP seriously threatened PAPO's status at several points, at significant cost to effective program management.

Although the original intention was that NPAP should embrace all government activities pertaining to poverty reduction, with NPAC acting as a Cabinet committee on poverty, in practice, NPAP served as a unified 'window' for attracting international donor support for poverty reduction. NPAC dealt solely with oversight of NPAP rather than with government actions and policies that influence poverty as a whole. As a result, NPAP came to be seen

as the totality of those internationally financed projects for poverty reduction that were brought under the unified management of PAPO, which acted as Secretariat to NPAC. Opportunities were missed to address two of the other original objectives of NPAP: (a) to coordinate the poverty-related actions of all government ministries and agencies; and (b) to establish closer links between policy-making at central level and the on-the-ground realities at local level. The Government's current efforts to prepare a Poverty Reduction Strategy Paper (PRSP), with the support of World Bank and IMF, should be seen in this light, since the PRSP aims to achieve precisely what NPAP failed to do: namely, to 'mainstream' poverty reduction in the Government's overall program.

Inadequate capacity building

Solid progress was made under NPAP in building local capacity to implement development projects, through inter-departmental Poverty Alleviation Councils (PACs) at aimag and sum levels and their equivalents (duureg and khoroo respectively) in the capital city, Ulaanbaatar. However, since GoM was reluctant to use loan funds for capacity building, PAVGP had to rely on parallel financing from UNDP and bilateral donors for this purpose. Donor support focused primarily on capacity building at national and aimag levels, while from 1998 the sum and khoroo level became the main locus of decisions concerning income-generation projects. The situation was exacerbated by high turnover of sum and khoroo PAC members as the incoming political party replaced all local-level line ministry department heads in the wake of national elections.

Weakness in pastoral risk management

Events of the 1999/2000 and 2000/2001 winter/spring periods heightened awareness of the importance of pastoral risk management among the Government, donors, and civil society. The last two winter/spring dzud emergencies were perhaps the worst in living memory, in both cases following severe summer drought. In 1999/2000, livestock mortality was close to three million head, or around 9% of the national herd, concentrated in six south-central and western aimags (see Map 2). In winter/spring 2000/2001, drought was again followed by an even worse dzud. This resulted in the loss of over four million additional animals, amounting to almost 14% of the national herd. The devastating impact of these consective years of dzud was exacerbated by historically high stocking rates. Having remained at a relatively stable level of around 25 million head for several preceding decades, largely owing to high autumn off-take encouraged by state-guaranteed livestock- and meat-marketing under agricultural collectivization, total livestock numbers increased by 33% over the six-year period 1993-99, reaching a peak of over 33 million head.

It would be wrong to view dzud as simply 'natural disasters', however. The impacts of dzud have become more severe as a greater proportion of the national population has come to depend on livestock for a livelihood, and as herding livelihoods have themselves become more vulnerable to risk. In the absence of alternative livelihood opportunities, many former state-sector employees turned to herding to support their families. The number of herding families more than doubled from 75,000 in 1990 (accounting for 351,000 people, or 17% of the total population) to 192,000 in 2000 (representing 824,000 people, or 35% of the national population). By comparison with existing herders, the new herders tended to be less skilled and experienced in herding. Their herds were, on average, smaller and less likely to increase

over time as new herders were more likely to slaughter animals to meet immediate livelihood needs. They also tended to move less frequently than more experienced herders, and to remain closer to urban settlements, roads, and other points of market access.

Under the collectivized planning of agriculture that prevailed until 1991, the former State Emergency Fodder Fund (SEFF) and other forms of State assistance to affected areas during dzud conditions did a great deal to minimize livestock mortality. This system was heavily subsidized, and collapsed once Soviet support was withdrawn in the early 1990s, which shifted the burden of risk management from the agricultural collectives to individual herding households. Customary land management practices involving the seasonal separation and rotation of pastures, which were maintained under collectivization, also began to disintegrate from the early-mid 1990s as the number of herding families and total livestock numbers rose, and as pastoral mobility and administrative support for livestock production declined.

Little investment was made in the 1990s in developing an alternative strategy for mitigating and responding to risk in the livestock sector. Until 1999/2000, the need for such a system was not seriously put to the test, as there had not been a serious dzud in Mongolia since 1993, when the remnants of the SEFF still functioned to some extent. The Democratic Coalition government between 1996 and 2000 was opposed to State intervention in pastoral risk management, whereas the new Mongolian People's Revolutionary Party (MPRP) Government (since June 2000) has clearly outlined a role for the State to complement herders' individual efforts to prepare for and better manage the effects of dzud. In May 2001, GoM Resolution No. 47 enacted a policy for the protection of livestock against drought and dzud. GoM requires external financial support to enable it to fully operationalize and implement this new policy. Key elements of the program include: pasture land tenure and management; hay and fodder production, conservation and marketing; livestock marketing; early-warning and emergency response systems; and livestock productivity-enhancing investments such as livestock breeding, veterinary and other livestock services.

Considerable experience has been gained in developing household herd-restocking programs as the main approach to reducing rural poverty in Mongolia, in combination with efforts to diversify the livelihoods of those who are unlikely to achieve sustainable livelihoods based on livestock production. These programs have been piloted since 1995 with initial financial and technical assistance from FAO, IFAD, and Save the Children Fund (UK). World Bank (under the PAVGP) supported the extension and scaling-up of the approach in five of the most severely affected aimags in response to the 1999/2000 dzud. Common elements of the approach developed in Mongolia are that it is organized as an in-kind credit scheme administered by local governments, with repayments in the form of animals or cash; procurement of animals is done locally, often within the same communities (i.e. richer herders sell animals to externally financed projects for on-lending to poorer, eligible herders), thereby ensuring that animals are already adapted to local ecological conditions, and that there is a neutral impact on local animal stocking densities; and a transparent, community-driven process of selecting eligible beneficiaries is followed.

While restocking provided an important short-term safety-net in rural Mongolia in the late 1990s, GoM and donors have now come to appreciate that

it also raises serious concerns about long-run sustainability. The main concerns relate to the disincentive effect of state-led restocking for risk management in livestock production (a 'moral hazard' issue), and for the wider development of the micro-finance industry. The gains from restocking could easily be wiped out by future dzud events. The areas in which restocking had initially been piloted escaped the most serious impacts of the 1999/2000 dzud, and it still remains to be seen how restocked households would cope with future risk episodes. In principle, livestock insurance is the primary means by which risk is offset under Mongolian restocking programs, but in practice voluntary coverage has been near-zero. The commercial viability of the conventional approach to livestock insurance, which attempts to cover losses at the individual household level, is seriously questioned. There is an urgent need for further work to develop and implement an alternative approach to livestock insurance in Mongolia. The most promising approach would base indemnities on some form of index, perhaps based on weather data, which is independently verifiable and which would promote rather than undermine incentives for good livestock management.

Inadequate community participation, sustainability and decentralization

As a social fund-type mechanism, the Local Development Fund (LDF) under NPAP suffered from two serious problems. The first was that genuine community participation in decision-making remained weak, with the notable exception of the community-based restocking initiatives undertaken in 2000. The Poverty Alleviation Councils reach down only as far as district-level administration which, as the PLSA revealed, community members regard as remote and unresponsive to their needs. Under NPAP, resources tended to be allocated equally to all areas for a pre-defined, and rather limited, menu of sub-projects. Another weakness was the lack of sustainability. Community participation was intended as a key objective and mechanism under the LDF, but was not always achieved beyond contributions of short-term, wage-labor inputs.

Inadequate community participation is also correlated with the low level of fiscal decentralization, which prevents local communities from actively making local development decisions because of limited self-generated revenues or inter-governmental transfers over which they have discretionary control. While each of the three levels of government nominally have independent budgets, the fiscal structure of Mongolia remains highly centralized, as revealed by a Decentralization Assessment conducted in support of project preparation. In 1997, for example, revenues accruing to central government accounted for 77% of total government revenue, and central government accounted for 71% of total public expenditure (excluding transfers to sub-national governments). Although this left only 29% of total public spending in the hands of sub-national governments, half of this amount still came from central government transfers. In other words, only half of the already small fraction of total public spending that sub-national governments control is generated from local revenue sources, and essentially all of this goes to meet recurrent expenditures. In fact, there is circular relationship between community participation and fiscal decentralization. The currently low level of fiscal decentralization inhibits the voice and influence of local communities over public expenditure, while inadequate community participation makes fiscal decentralization less feasible because local capacity remains under-developed.

Decentralization in policy and practice

After coming to power in June 2000, the current Government set out in its Action Program an ambitious agenda to promote decentralization. The mechanisms envisaged included the promotion of regional and rural development, in part to address the over-concentration of economic opportunity in the capital city and central, more market-accessible regions of the country; increasing accountability in the public sector; increasing the capacity of local governments to generate revenues over which they have discretionary control; and offering citizens greater opportunity to directly monitor the performance of their elected citizen's assemblies (khurals) at various levels.

The proposed Public Sector Management and Finance Law seeks to increase the accountability of public sector institutions at all levels, including civil service reform linked to the budgeting process and overhaul of the existing system of inter-governmental transfers. Government's 'Good Governance for Human Security Program' also refers to 'decentralizing and empowering local self-governance and local administration', and aims to support 'stakeholder consultation, voice, and participation' in the broader policy process, including 'monitoring citizen satisfaction and recommendations with regard to services, rights, and government responsiveness to citizen demands'. The I-PRSP echoes the broad theme of raising public accountability, notably through greater public voice in and scrutiny of the budget process.

To date, however, decentralization in Mongolia remains both imbalanced and incomplete in practice. The Decentralization Assessment conducted in association with project preparation shows that, measured against a set of standardized criteria developed through international comparative benchmarking, Mongolia is currently characterized by substantial though incomplete political decentralization, but little administrative decentralization and virtually no fiscal decentralization. Administrative decentralization follows a deconcentrated pattern in which governors and their staffs report upwards to the next highest level of government. There is little opportunity for elected assemblies to exert any influence over technical department staff and quality of service delivery at their respective level of government, and therefore little incentive for local populations to express their views to their elected representatives. Evidence from the PLSA reveals that community members are widely dissatisfied with the extent to which local governors take account of their interests.

Current efforts of Government, with the support of IMF and ADB, are focusing on fiscal 're-centralization' in the interests of fiscal control and to improve the overall tax collection rate. In parallel, however, efforts are being made to develop a transparent, formula-driven approach to determining inter-governmental transfers, which account for the vast majority of most local authority revenues, particularly in rural areas. The formula is still under discussion, but is likely to include an element of poverty-targeting. Once a transparent basis for inter-govermental transfers is established, it is then imperative to ensure that expenditure allocation at the local level - between sectors and between alternative investments within individual sectors - takes local needs and aspirations into account.

Under-development of financial systems, particularly in rural areas
Mongolia's financial system, at this point in its transition, is small, fragile, and highly dysfunctional, with recurring insolvencies in the banking system and a high level of vulnerability to economic shocks and crises. These

weaknesses, together with the narrow range of available financial services, seriously constrain private sector development and growth. In a recent World Bank-funded survey of Mongolian entrepreneurs, 96% reported the lack of long term financing and 65% reported inadequate working capital as the main constraints to their business operations. An IFC-supported study found that although the informal sector is estimated to generate economic activity equivalent to as much as 30% to 38% of official GDP, informal sector operators obtain their finance mainly from personal and family savings (82%), followed by individuals (11%), and only 0.5% from bank loans. Mongolia's financial system is characterized by the following themes, as summarized by a recent IFC report: (a) lack of confidence in banks; (b) predominant state ownership and concentration of assets; (c) collapse of financial services in rural areas; (d) poor corporate governance; (e) lack of management experience and skill; and (f) serious rent-seeking behavior. Furthermore, it was estimated around 1999 that some 95% of cash circulating in Mongolia's economy was concentrated in the capital, Ulaanbaatar; the vast proportion of trade in rural areas remains on a barter basis. Until very recently, those in rural areas, and the poor virtually everywhere, had practically no access to financial services of any kind, with the exception of micro-loans being provided by NPAP through the PACs. The environment for micro-finance service delivery has improved dramatically over the last two years, however, with the restructuring of the Agriculture Bank (now opening new rural branches) and the remarkable success of the (still largely urban-based) XAS-Bank which has rapidly achieved financial and institutional sustainbility in micro-credit. Government is committed to increasing outreach of financial services to poor and near-poor households on a sustainable basis, both in rural and in peri-urban areas. A new micro-finance law is under preparation.

2. Objectives

The development objective of the project - referring to the first four-year phase of the overall program - is: "an effective approach to promoting improved, secure, and sustainable livelihood strategies developed, demonstrated, and validated in selected areas, and institutional capacity created so that these strategies can be replicated and scaled-up in Phase II of the Program".

The project would be national in scope, with intensive pilot-testing of certain institutional innovations in eight selected aimags (see Map 1). In parallel with the pilot-testing of new approaches, selected NPAP activities would continue to be implemented nation-wide, with the aim of facilitating convergence between the new approaches and existing anti-poverty interventions over the medium term. The outputs that in combination will contibute to achieving the project development objective are:

a) Pastoral Risk Management: an integrated strategy developed, piloted, and adopted in eight selected aimags for managing covariant risk in pastoral livestock production, with a primary emphasis on risk preparedness. In combination with other project components, this component would aim to assist in addressing the underlying causes of rising vulnerability to drought and dzud ('winter disasters');

b) Micro-Finance Outreach: the outreach of financially and institutionally sustainable micro-finance services (including savings, credit, and insurance) to targeted poor and vulnerable non-poor households and individuals in rural areas of selected aimags achieved;

c) Local Initiatives Fund: efficient, socially inclusive, and transparent community-driven mechanisms identified and established to facilitate community prioritization, selection, co-financing, and execution of investments in basic infrastructure and social services provision in rural areas, combining local resource mobilization with matching government grants based on clear and transparent criteria for inter-governmental transfers; and

d) Project Management: a decentralized project management framework realized through the progressive devolution of project management responsibilities to aimag and sum (rural district) levels within local governments, while retaining overall coordination, monitoring and evaluation, and fiduciary oversight at national level.

3. Rationale for Bank's Involvement

The value added through Bank support for this project is fourfold:

First, the Bank brings broad international experience and technical knowledge to bear in several areas critical to project success: (a) community-driven development, including Africa Region's Community Action Programs, demand-driven rural investment programs particularly in EAP and LAC Regions, and social funds more broadly; (b) social risk management (particularly through the Social Protection Family); (c) micro-finance services and strategies, particularly through the Bank's close association with CGAP; and (d) pastoral development, particularly through the Animal Resources and NRM Institutions thematic groups.

Second, the Bank has made a long-term commitment to supporting poverty-reduction efforts in Mongolia, and acts as the lead development agency in this field. The proposed project builds directly on lessons learned under NPAP, for which the Bank was the major financier through PAVGP; and it is provided for in the CAS. Continuity of support for poverty reduction from the Bank is regarded as a priority by GoM, and is reinforced through the PRSP process. The Bank is in a strategic position to help government coordinate donor efforts with respect to livelihood-based poverty reduction, designing and financing a local initiatives fund, strengthening the decentralization process, and securing sustainable financing mechanisms for maintenance.

Third, this would be the first major investment program in international experience designed explicitly according to Sustainable Livelihoods concepts and principles. It should yield important lessons on how to translate such a concept into a concrete set of investments, while respecting the need for flexible design in order to accommodate community initiatives, process-based iterative learning, and to explicitly plan for external shocks the timing and intensity of which are difficult to predict.

Fourth, the Bank would be the first international financial institution to support the establishment of an integrated pastoral risk management system on national scale, building on lessons learned under the Kenya Arid Lands Resource Management Project. Should the pilot initiatives under Phase I of SLP prove successful, it would open up possibilities for replication not only in Mongolia but among pastoral peoples of Northwestern China and Central Asia as well as in drought-prone areas such as the Horn of Africa.

4. Description

Pastoral Risk Management: an integrated strategy developed, piloted, and

adopted in eight selected aimags for managing covariant risk in pastoral livestock production, with a primary emphasis on risk preparedness. In combination with other project components (particularly the index-based livestock insurance scheme under the MFO component, promotion of 'exit strategies' for new herders through access to micro-finance, and demand-driven support for public goods in agriculture through the LIF), this component aims to reduce the vulnerability of herders and enhance their resilience to drought, dzud and other shocks through four sub-components: (i) risk forecasting and contingency planning (improving coverage of weather forecasting data, broadening the range of data used in semi-annual early warning system bulletins and enhancing their dissemination to local authorities and herders, and development of sum-level contingency plans); (ii) grazing and pasture management (support for community-based pasture management, including mapping and re-instituting seasonal pasture rotation with credible sanctions for non-compliance, provisions for negotiating access with other herding communities during times of drought or dzud, and mechanisms for conflict resolution; rehabilitation of emergency grazing reserves at inter-aimag and inter-sum levels; and group-based well rehabilitation in areas of high quality yet currently under-utilized pasture); (iii) herder self-help initiatives (organizational strengthening with time-bound, matching loans to assist groups in establishing revolving funds for livestock productivity-enhancing investments such as breeding and veterinary services, fodder purchase and/or production, livestock product marketing); and (iv) hay and fodder enterprise development (testing business models for hay-making and feed concentrate production under alternative technological and market-demand conditions). Implementation would begin in 16 pilot sums in the first year of the project, expanding to all 143 sums in the eight core aimags by the end of project, with the relative emphasis among sub-components and activities varying according to ecological and market-access conditions.

Micro-Finance Outreach: the outreach of financially and institutionally sustainable micro-finance services to targeted poor and vulnerable non-poor households and individuals achieved in remote rural areas of the eight core aimags. This objective would be met through three sub-components: (i) creation of a Micro-Finance Development Fund (MDF, the Fund) as a wholesale lending facility to accredited Micro-Finance Institutions (MFIs) for on-lending to the target population (sub-loans), with the aim of expanding and diversifying livelihood sources and rural incomes. The day-to-day management and operation of the MDF would be carried out by the Micro-Finance Management Office (MMO, the Management Office), to be established within the Bank of Mongolia (BoM, the Borrower's Central Bank), in accordance with a Micro-Finance Policy Manual (the Policy Manual) acceptable to the Bank. This MMO would be supervised by a Micro-Finance Development Board (MDB, the Board), which would review the operation of the Fund, the credit activities (loans and sub-loans), and the strategic decisions on policy matters. The Board would comprise representatives of the GOM (MoFE, BoM, HLSPO), the private sector (Banking Association, commercial banks and micro-finance institutions), and academia. Proceeds accrued from the repayment of the subsidiary loans by the MFIs would be maintained in the MDF for re-lending for the same purposes and under the same terms and conditions as those under the original IDA credit. The sub-component would also include substantial technical-assistance resources to promote the strengthening of the MFIs and to support the development of the microfinance industry in Mongolia, including: (i) to help selected MFIs prepare and implement adequate business

plans; (ii) to identify (through market research) and develop new micro-finance products tailored to local demand and market conditions; and (iii) to develop the legal and regulatory framework required for the efficient operation of non-banking financial institutions (NBFIs) as micro-finance intermediaries. As conditions for the disbursement of the IDA funds allocated to this sub-component for the micro-finance loans (Category 4, for a total equivalent to US$3 million), the Borrower would: (a) adopt a Policy Manual acceptable to IDA for the implementation of the sub-component; (b) establish and maintain during project implementation the Micro-Finance Development Fund (including the Board and the Management Office) in terms and conditions satisfactory to IDA; and (c) accredit MFIs (at least one) and sign Subsidiary Loan Agreements (SLAs) for the disbursement of subsidiary loans, in compliance with the accreditation criteria and the terms and conditions set forth in the Policy Manual.

(ii) Strengthening of Revolving Loan Funds (RLFs) so as to improve the operational performance and financial health of the existing, local government-owned and -operated micro-credit RLFs that were created at the sum level under NPAP. The process of strengthening these RLFs would include: (i) review of their governance and management arrangements; (ii) collection and analysis of information on current operations and on-lending arrangements, quality of loan portfolio, and financial statements; (iii) selection of best-performing RLFs, which have the best chances of achieving financial sustainability; (iv) design of business plans for the selected RLFs to help them improve their efficiency; (v) provision of loans from the Borrower to help the selected RLFs implement their business plans and improve their financial situation; and (vi) eventual privatization of the best-performing RLFs. As a condition for the disbursement of the IDA funds allocated to the provision of loans to the selected RLFs (Category 5, for a total equivalent to US$ 500,000), the Borrower would prepare a detailed Action Plan for the use of these funds, acceptable to the Bank. This Plan would include the institutional arrangements and responsibilities, the on-lending terms and conditions, the criteria for the selection of RLFs eligible to receive new loans, the purposes and uses of the funds, as well as the steps to be taken towards the eventual privatization of these RLFs.

(iii) Development of an index-based livestock insurance scheme. A risk index would be developed during the first year of the project, on the basis of which participating private insurance companies would offer livestock insurance to individual herders. The index, based on weather and/or livestock mortality data, would differentiate relative risk at an appropriate level (most likely using sum-level data). Indemnities under the scheme would be based on the sum-level index rather than on losses at the household level. All holders of insurance would therefore receive payments whenever given thresholds in the index were exceeded in their locality, irrespective of their individual losses, thereby preserving incentives for good livestock management. The project would also finance training workshops for participating insurance companies and the Government officials involved, and a nation-wide information campaign to publicize the scheme and attract clients. The scheme would be launched during the second year of the project, and would be expected to become profitable by the end of the project. During the start-up phase (project years 2 to 4), Government would offer a stop-loss provision to participating insurance companies, financed from the proceeds of the Credit, to limit their losses in the event of a major dzud. This provision would take the place of international reinsurance, which would be

unlikely to be attracted until commercial viability of the scheme could be demonstrated. A condition of disbursement of IDA funds to finance the stop-loss provision (Category 6, for a total equivalent to US$ 1,000,000) would be that a methodology, including eligibility criteria for participating insurance companies, institutional responsibilities, and flow of funds, has been elaborated in a manner acceptable to the Bank. Under Phase II of the Program, the index-based insurance scheme would be expected to operate in a financially and institutionally sustainable manner, without the need for Government to offer a stop-loss provision. Insurance companies offering index-based livestock insurance would then be expected to seek international reinsurance.

Local Initiatives Fund: efficient, socially inclusive, and transparent community-driven mechanisms identified and established to facilitate community prioritization, selection, co-financing, and execution of investments in basic infrastructure and social services provision in rural and peri-urban areas, combining local resource mobilization with matching government grants based on clear and transparent criteria for inter-governmental budget transfers. Three sub-components would deliver this output: (i) two separate investment funds: the Local Initiatives Fund (LIF), a new facility that would be piloted in the eight core aimags and one pilot duureg (peri-urban district of Ulaanbaatar); and, in modified form, the Local Development Fund (LDF) which was initiated nation-wide under NPAP, in the 13 other aimags and 8 other duuregs in the country; (ii) training and capacity-building activities, focusing primarily on the sum and bag levels in the eight core aimags, for orientation, skills development in administration and management (including community-based procurement and disbursement), study tours and exchanges, refresher training, and the development of training materials; and (iii) a fiscal decentralization initiative, comprising a three-year action-research program to explore operational modalities for a needs-driven approach to public expenditure allocation at the local level. Implementation of the LIF would begin in the 16 pilot sums in the first year of the project, expanding to cover all 143 sums in the eight core aimags by the end of project.

Project Management and Policy Support: an efficient, decentralized, and capacity building-oriented project management system operational and policy framework for promoting sustainable livelihoods improved. The project would not support new or additional project management arrangements at central, aimag, or sum/duureg levels. Rather, in order fully to capitalize on the experience and skills developed under NPAP, the project would make use of and build on existing program management structure for project implementation. Strengthening existing institutional capacity would be the main priority. Under the technical and policy guidance of the three Working Groups for each of the above three components, and ultimately reporting to the National Committee on the Household Livelihoods Capacity Support Program (NCHLCSP), the Household Livelihoods Support Program Office (HLSPO) would have overall responsibility for project implementation and coordination. Local governments and community groups would carry the main responsibility for executing the project through the aimag and sum Household Livelihoods Support Councils (HLSCs). Under this component, the project would finance: (i) the investment and recurrent costs of the HLSPO, including incremental staff as long-term consultants on fixed-term contracts at central, aimag and sum levels; (ii) policy advocacy and legislative support activities; (iii) information dissemination and communications; (iv) project orientation workshops and

training; (vi) monitoring and evaluation; and (vii) auditing.

Pastoral Risk Management
Micro-Finance Outreach
Local Initiatives Fund
Management and Policy Support

5. Financing
Source (Total (US$m))
BORROWER ($3.39)
IDA ($18.73)
Total Project Cost: $22.12

6. Implementation
A number of principles have guided the design of institutional and implementation arrangements for the project: (a) work within the existing government structure and institutions; (b) build upon the capacity already created under NPAP; (c) recognize that creating capacity takes time and is not uniform, therefore build flexibility into the phasing-in of project activities; (d) keep initial procedures and processes simple so that the project can innovate and test new approaches for broader adoption in later stages; (e) establish the management structure in a step-wise fashion, allowing time to test and refine procedures and develop the necessary training material and train trainers before expanding to other areas; (f) use the sum (district) as the primary focus for most project decision-making and implementation; and (g) create a transparent set of procedures that facilitates participation by communities, and the poor and vulnerable households within those communities, so that prioritization and uptake of project activities is driven by them. The institutional structure for program/ project oversight, coordination, capacity building and implementation is further articulated in Annex 13 and in the form of organograms in Annex 15.

Institutional Structures: Overall project oversight will be provided through the National Committee for the Household Livelihood Capacity Support Program (NCHLCSP). This inter-ministerial body supersedes NPAC, which performed the same function for the NPAP. It includes senior representation from all the relevant ministries (including Finance and Economy (MoFE), Food and Agriculture (MoFA), Social Welfare and Labor (MoSWL), Infrastructure (MoI), Health (MoH), Education (MoSTEC), and Nature and Environment (MoNE)); representative NGOs/ civil society institutions; and directors of other major poverty-related operational programs.

Coordination of project implementation at the central/ national level will be the responsibility of the Household Livelihoods Support Program Office (HLSPO). This office supersedes PAPO, which served as the program implementation unit for NPAP, and will implement project activities under the guidance of the NCHLCSP. Incremental staff (as long-term consultants on fixed-term contracts), office equipment, and a small number of vehicles would be financed from the proceeds of the Credit for the four year duration of the project. Some of the key staff proposed for the HLSPO also held key positions in PAPO and are already familiar both with the lessons from NPAP experience and with the relevant World Bank policies and procedures concerning procurement, disbursement, and reporting. The HLSPO has two divisions: 1) a program implementation division with a full-time coordinator for each of the

three main project components (pastoral risk management, micro-finance outreach, and the LIF/LDF) and an officer responsible for ensuring coordination among these components; and 2) a division responsible for the fiduciary aspects of project management, including: (a) financial management; (b) procurement; (c) monitoring and evaluation; (d) information dissemination, training coordination, and public relations; (e) donor coordination; and (f) overall project planning and budgeting. HLSPO would be responsible for procurement of all goods to be centrally procured, all works subject to NCB (rehabilitation of two irrigation schemes under the PRM component), and all consultant contracting.

For each of the three main components, technical Working Groups at national-level will provide technical guidance and oversight, and would ensure consistency with sectoral policies. The PRM Working Group is led by MoFA and includes members from MoNE, MoSWL, and civil society. The LIF Working Group is led by MoFE and includes representation from all the ministries listed above plus civil society. The MFO 'working group' is the Board of the MDF. Two HLSPO staff members participate in the Working Groups as ex officio members; each component coordinator serves as the secretary of their respective working group.

Execution of program/project activities at the aimag, sum and duureg levels will primarily be the responsibility of sub-national (aimag) and local (sum, duureg) governments. The existing Poverty Alleviation Councils (PACs) at each of these levels, which served as inter-departmental steering committees for program implementation under NPAP, will continue to perform the same function under the proposed program/project, under the new name Household Livelihoods Support Councils (HLSCs). Their membership will also be broadened as appropriate, notably to ensure greater involvement of the agriculture and environment-related technical staff whose involvement is key to successful implementation of at least the PRM component. HLSCs in the sums of the eight core aimags selected for pilot activities would be considerably strengthened. At aimag level, technical Working Groups for the PRM and LIF components, analogous to the national-level Working Groups, will be constituted from the relevant line departments to advise on their respective detailed work plans and budgets. At bag level and below, civil society community mobilizers will work with the sum HLSC to facilitate, inter alia, herder-group formation for self-help initiatives, community-based pasture management, and well-rehabilitation under the PRM component; and identification and prioritization of potential sub-projects to be financed under the LIF.

Implementation Arrangements: The PRM and LIF components would begin activities in two pre-selected, pilot sums in each of the eight core aimags during the first year of the project (a total of 16 sums), and thereafter scale-up to include all 143 sums in the eight core aimags over project years 2-4. Full implementation in all sums will only begin once the processes and procedures have been adequately developed, modified and refined, and all staff have been trained (including training trainers) over the initial 12 month period. The particular activities to be implemented in each sum under the pastoral risk management component will vary according to local ecological and market-access conditions. The MFO component would work with sum RLFs in the eight core aimags, progressively expanding the number covered in line with the capacity to provide training to them. In the non-core aimags and duuregs, project activities would be very similar to those implemented under the LDF (of NPAP), and the HLSCs would operate in the same way as did

the PACs under NPAP, in all sums and duuregs over the full four years of the project.

Micro-Finance Development Fund (MDF). The daily management and operation of the MDF (as a commercial wholesale banking facility) would be the responsibility of the Micro-Finance Management Office (MMO), to be established within the Bank of Mongolia (BoM), and which will be adequately budgeted, well-equipped, and staffed with qualified individuals to be able to perform its duties and responsibilities. The MMO would maintain separate accounts (according to internationally acceptable accounting practices) for the sub-component (to be audited annually by private auditors), and would present quarterly progress reports to the HLSPO concerning its operations, as well as the documentation required to fully support the disbursements from the credit account. MMO would handle day-to-day operations of the funds in accordance with a Micro-Finance Policy Manual (the Policy Manual) acceptable to the Bank. The main sections of the Policy Manual include: (i) governance and management of the MDF; (ii) eligible sub-projects; (iii) type of financial institutions to be eligible to participate in the project; (iv) qualifying (accreditation) criteria for MFIs; (v) uses of funds (lending and sub-lending); (vi) terms and conditions (currency, lending rates, maturity, sub-project financing, collateral, default, and prepayment) for loans to MFIs and sub-loans to final beneficiaries; and (vii) environmental protection, audit, supervision and reporting. A draft Policy Manual was reviewed at appraisal and found to be satisfactory. In order to ensure a full coordination and efficient use of credit resources, MMO's policies and lending operations would be supervised by a inter-institutional Micro-Finance Development Board (MDB), to be established with representatives from the Borrower's MoFE (as chair), HLSPO, and BoM, as well as representatives from the private sector (i.e. Mongolian Banking Association, commercial banks, and MFIs), and academia. The Director of the MMO would serve as Secretary of the Board. As part of the Project's Mid-Term Review, the Borrower and the Bank agreed to carry out a comprehensive assessment of the institutional and financial performance of the Micro-Finance Outreach component in general, and of the MDF in particular. Based on the results of this review, Terms of Reference would be prepared for a more detailed and in-depth study of the micro-finance sector in Mongolia, with the special objective of outlining alternative options for the future of the MDF. One of the main options to be explored would be the privatization of the MDF, where the resources available could be used by the GoM as its contribution to the equity of a new independent and financially autonomous apex micro-finance institution. Consequently, one of the conditions for the implementation of the Phase II of this APL could be the agreement of a specific Plan of Action to implement the recommendations arising from this privatization study.

Uses of Funds. The funds under the MDF would be lent to accredited MFIs, according to a pre-agreed selection criteria, under signed Subsidiary Loan Agreements (SLAs) acceptable to IDA. Proceeds accrued from the repayment of the principal of the subsidiary loans by MFIs would be used to establish and maintain MDF as a revolving fund for re-lending for the same purposes and under the same terms and conditions as those under the proposed IDA Credit. These MFIs would provide mainly short-term sub-loans to project beneficiaries in the target areas (individual households and micro-enterprises) to finance working capital for their viable initiatives. If needed, medium-terms loans (up to three years) to finance small capital investment would also be granted. Sub-loans under this sub-component would not exceed the equivalent

of US$400 for individual households and US$1,000 for micro-enterprises (employing at least two persons outside the immediate family members). IDA financing under the loans to MFIs would not exceed 75% of total sub-project costs; therefore, at least 25% of the total subproject cost would be provided by either the MFIs or the final sub-borrowers from their own funds.

On-lending Arrangements. The proceeds of the IDA credit allocated to this sub-component (Category 4, amounting to around $3 million) would be made available to MDF directly from the Special Account. The Project's HLSPO would disburse and transfer to the MDF account the amounts (in local currency) required in accordance to the terms of SLAs signed with accredited MFIs. These funds in MDF would the used for providing loans to selected MFIs (under signed SLAs), under lending terms to be adjusted periodically according to criteria that fully reflect market interest rates. The lending variable rate of interest will be adjusted monthly and intended to be equal to the adjusted cost of medium-term deposits in the local market to avoid introducing distortions in the local market or discouraging the mobilization of savings by the financial intermediaries. A market-based indicator, reflecting the actual cost of loanable funds in the banking system, to be used as a reference for setting and adjusting these interest rates would be agreed upon, as indicated in the Policy Manual, in a manner acceptable to the Bank. The Borrower would assume the full foreign exchange risk and the interest rates on the loans to MFIs would cover this foreign exchange risk, as well as all administrative costs incurred in the establishment and operation of the MMO, and the credit risk associated with the subsidiary loans to MFIs. The on-lending terms from MFIs to final sub-borrowers (on the sub-loans) would be determined freely by the MFIs, according to market forces and their assessment of the associated credit risks and adequate margins. These rates should be sufficient to cover the cost of funds and their operating expenses, as well as provisions for possible loan losses and adequate level of profits, to allow for further lending expansion to the target population without undermining their prudent equity to risk asset ratio. The Borrower, through MDF/MMO, would exchange views and discuss possible adjustments with: (i) the Bank, on the interest rates on subsidiary loans to participating MFIs; and (ii) the participating or potential candidate MFIs, on the level of interest rates charged by them on sub-loans to final sub-borrowers. This would be done at least once a year, around June 30, commencing on June 30, 2002.

Monitoring & Evaluation. The monitoring, evaluation and reporting system for the project will comprise performance and impact monitoring and evaluation, building on the participatory techniques developed and used under NPAP. It will continue to rely on a combination of project staff and contracted specialists from NGOs/research institutions for its execution. A Planning/M&E Officer within the HLSPO will be charged with overseeing the M&E system, consolidating the reports from the three components, and compiling information on management and policy support activities. S/he will be responsible for providing project management with timely and regular information on performance and impact. The majority of the inputs for the project's M&E system will come from M&E systems of the three components. Each component will rely on the aimag and sum HLSCs to carry out day-to-day monitoring of component activities, with the aimag HLSCs carrying prime responsibility for component evaluation. The backbone of the system will be a newly developed MIS. The more interactive, qualitative methods, incorporating bag-level working groups and the use of community scorecards, will be

combined with the compilation of formal information geared to component performance and achievement of targets as specified in annual work programs and budgets.

Financial Management: To the maximum extent possible, financial management of the project would rest with the sum-level HLSC coordinators/secretaries, with the aimag level providing financial oversight and supervision. Overall responsibility would rest with the HLSPO, which would ensure an adequate flow of funds to each component, supervise the financial management of the central and sub-national project management units, and be responsible for consolidating financial reports, audits and reporting to GoM (NCHLCSP) and the World Bank. The most demanding element of the financial management system would be the implementation the LIF and the processes involved in reviewing, screening, verifying, and approving sub-projects. The cornerstone of the system would be an annual funding ceiling allocated to each sum. Within this ceiling, the sums (and the pilot duureg) would identify and submit sub-projects for financing. The initial amount of the funding ceiling would be based on the population of the sum. In subsequent years, the ceiling would be adjusted according to a formula reflecting agreed performance criteria.

7. Sustainability

Pastoral Risk Management: The PRM component has been designed to ensure the social, economic, financial, institutional, and environmental sustainability of all activities under the component. All activities have been designed with an exit strategy in mind and with the aim of enabling local people to implement the activities themselves, even in the absence of project support, by the end of project. In designing pilot activities, the concern was to gain four years of experience in a reasonable number of field sites in order to assess sustainability in both dzud and non-dzud years. The grazing and pasture management sub-component would promote sustainable livestock-based livelihoods through the sustainable management of herds and natural resources. The sustainable management of wells, and the rangeland around the water points, would be ensured by pilot-testing and adopting a community-based approach to well rehabilitation. The community would own the wells and form well-user groups that would charge user fees in order to cover the cost of operation and maintenance. They would also be responsible for conducting monitoring water quality and quantity, and monitoring vegetation changes around the wells in accordance with guidelines to be devised in a participatory manner.

The herder self-help initiatives sub-component would build socially viable and sustainable forms of cooperation at community level as a basis for implementing joint activities such as grazing management, well-rehabilitation, hay growing, fodder stock-piling and veterinary care. Veterinary services such control of parasites that threaten animals' winter survival would be offered to herders for a fee. The purpose of creating multi-purpose revolving funds at herder-group level would be to test whether a group-level risk fund could be run and managed by herders themselves on a self-sustaining basis. This might involve buying in and reselling hay at a profit to cover transport costs and to keep the fund turning over year after year.

The main objective of the hay and fodder enterprise development sub-component is to pilot-test various business models to guage whether commercial hay and fodder making can be financially self-sustaining, not only in dzud years when

demand for fodder is high, but also in non-dzud years when demand is low. Likewise, the purpose of the aimag-level emergency fodder reserve pilots is to discover whether they can be run as revolving funds on a financially sustainable basis. This would involve holding part of the stocks of feed concentrates over their 3-4 year shelf life, and selling part of the stock in non-dzud years to renew the stock and to cover operating expenses.

Micro-Finance Outreach: At the development objective level, the micro-finance outreach component would contribute to sustainability within the livestock sector as a whole by providing an 'exit strategy' for the newcomers to herding, and would enhance livelihood security and sustainability for this group specifically. It is envisaged that the Micro-Finance Development Fund would become an autonomous apex institution under Phase II of the program, which would represent a strong move towards sustainability within the micro-finance industry. In the meantime, the MDF and supporting technical assistance services would help to ensure that existing MFIs are stronger, are able to offer services on a sustainable basis to currently under-served clients in remote rural areas, have access to training and good-practice information, have improved and more reliable access to funding, operate within a conducive policy and regulatory environment, and will be able to finance a higher percentage of their lending operations from savings deposits. The index-based livestock insurance scheme would be implemented by private insurance companies in the interests of long-run sustainability; Government's role would be to underwrite a stop-loss provision only during the initial pilot phase. Once the feasibility and profitability of index-based livestock insurance had been proven, the stop-loss provision would be phased out and replaced by international reinsurance.

Local Initiatives Fund Component: The key to sustainability of the LIF is to facilitate its incorporation into the government's regular process of resource allocation, through the budgetary process, and thereby to gradually reduce its dependence on external funding. This is a medium term goal and one that will not be achieved in the first phase of the program. However, it will be necessary to pilot initiatives and build a solid foundation on the basis of which the fiscal decentralization process can be mainstreamed in the second and third phases of the program. The pilot fiscal management initiative, to be implemented through action-research in the last two years of the project, will assist in accomplishing this goal. MoFE is the government body responsible for fiscal affairs, the budget process and allocation of government budget, and in the interests of sustainability will take the lead in the Working Group for the LIF component and on the fiscal management initiative directly.

8. Lessons learned from past operations in the country/sector

Detailed lessons have been learned from experience under NPAP and the IDA-financed Poverty Alleviation for Vulnerable Groups Project (PAVGP), through a joint evaluation conducted by Government, UNDP and World Bank in late 1999 in conjunction with identification of the proposed program, and through the intensive learning ICR conducted for PAVGP. Overall, NPAP was found to have been a timely response to the economic and social problems of the vulnerable poor during Mongolia's transition to a market economy. Its success under extremely difficult conditions during a period of economic transition can be attributed to:

a highly committed and dedicated implementing agency at national level

(PAPO);
the use of an existing network of local government institutions at aimag and sum levels as a delivery mechanism, which allowed the project to work efficiently in spite of severe constraints such as low population density, scattered settlement, seasonal population movements, harsh winter conditions, and poorly-developed transportation and communication networks;
the introduction of a bottom-up approach to project identification and implementation;
the trust placed in local government's capacity to identify, contract, supervise and report on public works schemes and basic education and rural health projects; and
the emphasis on making certain that funding was in place for O&M of whatever structures and services were rehabilitated by the project.

NPAP's most successful component was the Local Development Fund (LDF), which financed small projects in support of basic education, rural health and public works. The rural health and basic education sub-components achieved their objectives of reducing maternal mortality and school dropouts. The creation or rehabilitation of local infrastructure had a quick and direct impact on income earning opportunities and standards of living. However, the temporary employment created by public works programs was too brief to have had a significant impact on the livelihoods of the poor.

The key to the success of the LDF was its bottom-up, decentralized approach and its reliance on a well-developed network of cross-sectoral Poverty Alleviation Councils (PACs) at aimag/ duureg and sum/ khoroo levels. Local administrations were empowered to identify and implement projects, contract-in services, and account for expenditure. The LDF constituted practically the only capital budget at the discretion of the decentralized administration. Operation and maintenance was ensured by requiring that local governments allocate the recurrent budget prior to and as a condition for project approval. Works were useful and were greatly appreciated by communities. Beneficiary communities also demonstrated their commitment by contributing to the operation and maintenance of the works.

The main areas identified in which LDF could be improved were: (a) greater beneficiary participation; (b) stronger integration with the existing public administration and budgetary process; and (c) increased capacity of local government to continue the Fund's operation beyond the end of NPAP.

The income-generating credit schemes were the weakest aspect of NPAP and the Bank-financed PAVGP. The main cause was poor design. In 1995, in the absence of an operational bank with a branch structure, or a specialist micro-finance company serving rural areas, a decision was made to develop a government-administered credit scheme that operated through local government PACs at aimag/duureg and sum/khoroo levels. There were three main credit programs: (a) Vulnerable Group Organization (VGO) scheme, which operated under LDF; (b) Income Generation Fund (IGF) and (c) Women's Development Fund (WDF). In addition, loan repayments from the other three schemes were channeled into a series of sum and khoroo level Revolving Loan Funds (RLFs) under the direct control of sum and khoroo PACs. Of the four schemes, the most interesting and successful experience - and the only one with the potential to become self-sustaining - has been that of the RLFs.

The main lessons from NPAP are:

Poverty alleviation programs - no matter how sound in concept and principles - are unlikely to reduce poverty significantly unless they are supported by broad-based, people-oriented, and labor-intensive growth strategies. In the absence of supportive economic policies and pro-poor expenditure allocation, the gains of targeted poverty alleviation programs are likely to be offset by growing unemployment and economic deterioration. Poverty reduction is not sustainable if - for every person raised above the poverty line - another person falls into poverty to take his or her place.

Since poverty reduction is an issue that transcends sectoral boundaries, the proper location for a poverty program management unit is either under the Prime Minister's Office or in a cross-sectoral ministry such as Finance, Planning, or Local Government. A social sector ministry was a poor initial choice.

The establishment of a cross-sectoral implementing agency (such as PAPO) facilitates poverty project implementation but creates conflicts and uncertainty. Lack of clarity about PAPO's autonomy from MoSWL was a source of continual institutional conflict throughout the life of the project.

Decentralization of project management responsibility can be an effective way of overcoming institutional blockages at national level. Although controversy over PAPO's autonomy hindered implementation at central level, it was not a serious problem at aimag level and below.

Open public meetings at grassroots level facilitate successful implementation of a bottom-up, demand-driven approach. The restocking component achieved broad-based and inclusive community participation in beneficiary selection because it worked through the lowest unit of local government - the bag khural (assembly).

The creation or rehabilitation of local infrastructure can have a quick and direct impact on income earning opportunities and standards of living. However, the temporary employment created by public works programs is too short to have a significant impact on the livelihoods of the poor.

Sustainable access to credit for the poor requires the creation of a rural finance system. Local government bodies can help channel funds to the target group but constitute an inappropriate institutional base for micro banking.

Herder restocking is not sustainable in the absence of parallel support for pastoral risk management.

9. Program of Targeted Intervention (PTI) Y

10. Environment Aspects (including any public consultation)

Issues : Consistent with the World Bank's Operational Policy OP4.01, Environmental Assessment (EA) for the proposed SLP is regarded as an ongoing process that began around the time of project identification. Environmental assessment has been considered as part of several steps in the process of project identification and design: a national-level public consultation meeting in December 1999, conducted as part of project identification; an analysis of land policy and land tenure arrangements in Mongolia; a Participatory Living Standards Assessment (PLSA), conducted by National Statistical Office of Mongolia with World Bank support between March and September 2000; and an Intensive-Learning Implementation Completion

Report (ILI), documenting lessons learned under the World Bank-supported Poverty Alleviation for Vulnerable Groups Project (PAVGP). In July-August 2001, an environmental assessment scoping study of the pastoral risk management component was carried out, culminating in a dedicated environmental and social assessment over August-October 2001.

The dedicated environmental assessment was carried out over three stages by an independent team of specialists. First the EA carried out scoping of impacts and desk-based review of literature. This included the analysis of project preparation reports describing proposed project components and activities, and review of the report of the pastoral risk management scoping study. Second, in-depth stakeholder consultation was carried out over three weeks in Mongolia in September 2001. This included a series of interviews and workshops with secondary and primary stakeholders and key informants in Ulaanbaatar and rural Mongolia (in three aimags, Dundgobi, Omnogobi, and Ovorkhangai). In Ulaanbaatar, the EA team worked in close cooperation with the project preparation support team from FAO. Consultation on the EA's initial conclusions was facilitated by the use of an aide memoire distributed to MoFA, PAPO and MoNE. A draft of the EA report was prepared, and detailed comments from the World Bank, the project preparation team, and GoM were incorporated to produce a final report which was submitted in December 2001.

The full EA report covers the policy, legal and administrative framework; the methodology of the assessment; the baseline situation; the significant environmental impacts; the analysis of alternatives; and the proposed environmental management plan; complemented by a number of annexes providing detailed additional information.
Justification /rationale for category rating. The proposed project is B-rated, consistent with regional practice under other CDD-type projects and those with significant involvement in the livestock sector. Most environmental impacts resulting from the project are expected to be beneficial. No incremental livestock will be produced under the proposed project, and improved herd and grassland management practices will be supported, which will be conducive to environmental sustainability.
Overall environmental impact. According to the EA, the proposed project has the potential to deliver a significant overall positive environmental impact through its contribution to reduced land degradation, because community-level grazing management is proposed as a key part of the project's integrated approach to pastoral risk management. The EA field observations and discussions with herders indicated that the empowerment of herders or herder associations to manage their pasture has good potential for reducing land degradation, both in times of drought and dzud, and at all other times. Current pasture management patterns in Mongolia are accelerating land degradation due to concentration of herds around sum and aimag centers, partly as a result of the impact of dzud and drought, and partly due to the breakdown of existing wells, resulting in localized patterns of excessive livestock and consequent pasture over-use that have adverse effects on the pasture productivity and sustainability. Successful actions to reduce herders' vulnerability through sustainable pasture management offer a significant opportunity to reduce the extent and severity of land degradation.

11. Contact Point:

Task Manager

Robin Mearns
The World Bank
1818 H Street, NW
Washington D.C. 20433
Telephone: 202 458 4010
Fax: 202 477 2733

12. For information on other project related documents contact:

The InfoShop
The World Bank
1818 H Street, NW
Washington, D.C. 20433
Telephone: (202) 458-5454
Fax: (202) 522-1500
Web: http:// www.worldbank.org/infoshop

Note: This is information on an evolving project. Certain components may not be necessarily included in the final project.

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