Document of
The World Bank

Report No: 24155-MOG

PROJECT APPRAISAL DOCUMENT

ON A

PROPOSED CREDIT

IN THE AMOUNT OF SDR 15.00 MILLION (US$18.73 MILLION EQUIVALENT)

TO

MONGOLIA

FOR A

SUSTAINABLE LIVELIHOODS PROJECT

IN SUPPORT OF THE FIRST PHASE OF THE
SUSTAINABLE LIVELIHOODS PROGRAM

May 15, 2002

Rural Development and Natural Resources Sector Unit
East Asia and Pacific Region

CURRENCY EQUIVALENTS

(Exchange Rate Effective February 1, 2002)

Currency Unit = Mongolian Tögrög (MNT)
MNT 1,000 = US$0.91
US$1.00 = MNT 1,102

FISCAL YEAR

Government: January 1 - December 31 -- World Bank: July 1 - June 30

ABBREVIATIONS AND ACRONYMS

AEZ	Agro-Ecological Zone
BoM	Bank of Mongolia (central bank)
CAS	Country Assistance Strategy
CGAP	Consultative Group to Assist the Poorest
DCA	Development Credit Agreement
EA	Environmental Assessment
GoM	Government of Mongolia
HLSC	Household Livelihoods Support Council
HLCSP	Household Livelihoods Capacity Support Program
HLSPO	Household Livelihoods Support Program Office
ICR	Implementation Completion Report
I-PRSP	Interim Poverty Reduction Strategy Paper
LDF	Local Development Fund
LIF	Local Initiatives Fund
LSMS	Living Standards Measurement Survey
MDB	Micro-Finance Development Board
MDF	Micro-Finance Development Fund
MFI	Micro-Finance Institution
MFO	Micro-Finance Outreach
MIS	Management Information System
MMO	Micro-Finance Management Office
MoFA	Ministry of Food and Agriculture
MoFE	Ministry of Finance and Economy
MoH	Ministry of Health
MoI	Ministry of Infrastructure
MoNE	Ministry of Nature and Environment
MoSTEC	Ministry of Science, Technology, Education and Culture
MoSWL	Ministry of Social Welfare and Labour
NBFIs	Non-Bank Financial Institutions
NCHLCSP	National Committee for the HLCSP
NDVI	Normalized Differentiated Vegetation Index
NPAC	National Poverty Alleviation Committee
NPAP	National Poverty Alleviation Program
PAC	Poverty Alleviation Council
PAD	Project Appraisal Document
PAPO	Poverty Alleviation Program Office
PAVGP	Poverty Alleviation for Vulnerable Groups Project (Cr. 2760-MN)
PIM	Project Implementation Manual
PLSA	Participatory Living Standards Assessment
PM&E	Participatory Monitoring and Evaluation
PRM	Pastoral Risk Management
PRSP	Poverty Reduction Strategy Paper
RLF	Revolving Loan Fund
SCC	Savings and Credit Cooperative
SLA	Subsidiary Loan Agreement

Vice President:	Jemal-ud-din Kassum, EAPVP
Country Director:	Ian C. Porter, EACSM
Sector Director:	Mark D. Wilson, EASRD
Task Team Leader:	Robin Mearns, EASRD

MONGOLIA
SUSTAINABLE LIVELIHOODS PROJECT

CONTENTS

MONGOLIA
Sustainable Livelihoods Project

Project Appraisal Document

East Asia and Pacific Region
EASRD

Date: May 15, 2002	**Team Leader:** Robin Mearns
Country Director: Ian C. Porter	**Sector Director:** Mark D. Wilson
Project ID: P067770	**Sector(s):** AL - Livestock, BD - Decentralization, SY - Other Social Protection
Lending Instrument: Adaptable Program Loan (APL)	**Theme(s):** Rural Development; Social Protection; Poverty Reduction
	Poverty Targeted Intervention: Y

Program Financing Data

APL	Indicative Financing Plan				Estimated Implementation Period (Bank FY)		Borrower
	IDA US$ m	%	Others US$ m	Total US$ m	Commitment Date	Closing Date	
APL 1 Loan/ Credit	18.73	84.7	3.39	22.12	07/01/2002	12/31/2006	Mongolia
APL 2 Loan/ Credit	21.80	58.4	15.50	37.30			
APL 3 Loan/ Credit	19.30	40.5	28.40	47.70			
APL 4 Loan/ Credit	NA		NA				
Total	59.83		47.29	107.12			

[ ] Loan [X] Credit [ ] Grant [ ] Guarantee [ ] Other:

For Loans/Credits/Others:

Amount (US$m): SDR15 million (US$18.73 million equivalent)

Proposed Terms (IDA): Standard Credit

Grace period (years): 10 **Years to maturity:** 40

Commitment fee: 0.5% **Service charge:** 0.75%

Financing Plan (US$m): Source	Local	Foreign	Total
BORROWER	3.39	0.00	3.39
IDA	17.22	1.51	18.73
Total:	20.61	1.51	22.12

Borrower: MONGOLIA
Responsible agency: 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

Estimated Disbursements (Bank FY/US$m):								
FY	2003	2004	2005	2006				
Annual	3.69	5.11	5.37	4.56				
Cumulative	3.69	8.80	14.17	18.73				

Project implementation period: 4 years
Expected effectiveness date: 07/01/2002 **Expected closing date:** 12/31/2006

OCS APL PAD Form: Rev March, 2000

A. Program Purpose and Project Development Objective

1. Program purpose and program phasing:

The overall **program purpose** (see Annex 1) is: "*vulnerability reduced and secure and sustainable livelihoods achieved by targeted poor and vulnerable near-poor households and individuals nationwide*". The Sustainable Livelihoods Program is intended to support the shift in Mongolia's national anti-poverty strategy away from welfarist measures towards those that promote secure and sustainable livelihoods for all (see Annex 11 for a summary of program vision and approach, and Government's Letter of Development Program).

The **program development objective** (see Annex 1) is: "*target groups and individuals adopt improved livelihood strategies that build and maintain human, social, financial, physical and natural capital while reducing vulnerability to shocks*". This would be achieved through investments in four components: pastoral risk management; micro-finance outreach; local initiatives fund; and program management and policy support. The program would be divided into three phases, the build-up of which would be determined by the performance of program components and the pace of institutional reform and capacity-building at all administrative levels (see Attachments 1 and 2 to Annex 1):

- **Phase I**, of four years' duration (the Project), would continue to support during a transitional period nation-wide certain initiatives started under the National Poverty Alleviation Program (NPAP), while piloting new investment and capacity-building initiatives in eight core *aimags* (provinces). The implementation of individual activities would be flexible in pace and phased according to the particularities of each *aimag* and success in achieving targets;

- **Phase II** (next four years), within an appropriate legal and policy framework, would scale up and 'scale out' the tried and tested institutional innovations to national level. It would also extend successful initiatives that were limited in scope during Phase I due to inadequate institutional capacity; and

- **Phase III** (final four years), based on lessons learned from the first two phases, would focus on fine-tuning the technical and institutional innovations for long-term sustainability. The proposed program would therefore progressively combine horizontal (geographical) expansion with vertical deepening of policy and institutional reforms.

2. Project development objective: (see Annex 1)

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 to targeted poor and vulnerable non-poor households and individuals in rural areas of selected *aimags* achieved, including micro-finance credit and a index-based livestock insurance scheme;

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 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. Key performance indicators: (see Annex 1)

End-of-program impact indicators at **goal** level (12-year impact) would include:

- poverty incidence reduced from 36% to 14% (consistent with Government of Mongolia (GoM) targets);
- share of target groups and individuals able to withstand external shocks increased by 100%;
- *dzud*-related animal deaths reduced by half and number of households losing all animals reduced by 60%;
- 78% of school-aged children graduated at least from 'non-full' secondary school; and
- infant mortality reduced from 32 to 29 per 1000 live births (consistent with GoM targets).

The key indicators at the level of **program purpose** concern target groups and individuals' adoption of improved strategies relating to pastoral risk management; livelihood security and diversification; and the construction, rehabilitation and maintenance of demand-driven local and community infrastructure. Outcomes for each phase of the program are as follows (for detailed indicators developed by participants at the Second National Stakeholder Consultation Workshop on the Sustainable Livelihoods Program, July 29-August 2, 2001, see Annex 1):

Phase III: Nation-wide, targeted poor and vulnerable near-poor people are *using* improved and effective *sustainable livelihood strategies* to improve long term outcomes at household and community levels; assets have been created and are being maintained; strategies that reduce vulnerability to shocks and stresses have been implemented; and supporting public and private sector policies and strategies are being implemented.

Phase II: Phase I program *scaled-up nation-wide;* public supporting institutions being gradually institutionalized; and targeted poor using improved, effective and sustainable livelihood strategies to improve long term outcomes at household and community levels (winter preparation and improved pasture management adopted by 50% of herder households in target areas; 20% of target group have access to micro-finance services; and access to functioning basic education and rural health facilities increased by 20%).

Phase I: Effective approach to promoting secure and sustainable livelihood strategies developed, demonstrated, and validated in eight core *aimags* and one pilot *duureg* (urban district of Ulaanbaatar), and ready for scaling-up under Phase II; institutional capacity for implementing the approach developed in core *aimags* and existing capacity maintained outside core *aimags*.

Key performance indicators of progress towards the achievement of **project (Phase I) development objectives** are:

A. Improved pastoral risk management strategies adopted in core *aimags*:

- proportion of herding households making adequate winter preparations increased by 33% in project areas by comparison with start of project and/or non-project areas representing similar ecological zones;
- *dzud*-related animal losses reduced by 33% by comparison with start of project and/or non-project areas representing similar ecological zones;
- at least 50% of grazing land area under improved management in project areas by comparison with start of project; and
- discernible, positive impact on range-vegetation condition in project areas by comparison with non-project areas representing similar ecological zones and precipitation conditions, and as measured using a normalized differentiated vegetation index (NDVI, data obtained from remote sensing) or similar indicator.

B. Micro-finance services accessible to and used by poor households to build assets and smooth consumption on a financially and institutionally sustainable basis in remote rural areas of target *sums*:

- 10% of target beneficiaries in selected *aimags* use financial services;
- quantitatively and qualitatively measurable improvement in livelihood security of target beneficiaries (precise indicators to be selected in design of baseline survey);
- less than 10% of total loan portfolio of selected revolving loan funds (RLFs) past due;
- selected RLFs achieve 50% operational self-sufficiency;
- 50% of RLFs receiving additional funding privatized; and
- index-based livestock insurance scheme developed and operational.

C. Basic district- and community-level infrastructure improved and well-maintained in core *aimags*:

- 75% of target community members satisfied with the procedure for the identification, selection, and implementation of sub-projects;
- 85% of target beneficiaries of sub-projects satisfied with infrastructure activities implemented; and
- options identified for integrating needs-driven public expenditure allocation with regular local government budgeting.

B. Strategic Context

1. Sector-related Country Assistance Strategy (CAS) goal supported by the project: (see Annex 1)
Document number: 17604-MOG**Date of latest CAS discussion:** 04/01/98

CAS Goal: equitable development and poverty alleviation

The primary goal of the Mongolia CAS is to support the Government in completing the transition to a market-led economy, to improve living standards and reduce poverty. It adopts a four-pronged approach to help the Government create an environment conducive to private sector-led growth, to tackle transitional and structural poverty, and to manage the country's resources strategically to improve long-term growth. Institutional capacity building and environment protection measures are integrated into this approach. The four CAS goals are: (a) to support macroeconomic stabilization; (b) to facilitate private sector development and associated employment and income-generation opportunities; (c) to develop infrastructure to support private sector growth and market development; and (d) to promote equity in development through direct poverty alleviation assistance to ensure continued support for the most vulnerable groups. The project

directly supports the fourth of these CAS goals – to promote equitable development through direct poverty alleviation assistance to ensure continued support for vulnerable groups.

2. Main sector issues and Government strategy:

Increasing poverty and inequality

Following the exceptionally difficult years of the early 1990s, and despite of 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. The 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 or MoSWL) 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 a 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 the 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 heads.

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 public 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 reached 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, and the draft Mongolia Public Expenditure Review. Overall, sub-national and local governments account for less than a third of total public expenditure and, on average, 65% of their revenues come from central government transfers. Local governments can levy only marginal user fees,

mainly on the use of natural resources. Virtually all of the already small fraction of total public spending that sub-national and local governments control goes to meet recurrent expenditures. There is therefore a 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, priorities, 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 traits, as summarized in 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 FACs. 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) XACBank which has rapidly achieved financial and institutional sustainability 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.

3. Sector issues to be addressed by the project and strategic choices:

The project aims to address these **sector issues** in the following ways:

Increasing poverty and inequality. Poverty will be addressed primarily by increasing the capacity of poor and vulnerable households in rural areas and smaller urban settlements to better manage risk and build up income-generating assets, and by facilitating investment in community-level infrastructure in the same areas. This would be achieved through a shift from a welfare-oriented approach to poverty alleviation to one that aims to promote secure and sustainable livelihoods, linked to macro-economic policy and pro-poor public expenditure allocation.

Ambiguous institutional structure. The new Government is fully aware of the ambiguity under the existing Government Law that assigns MoSWL the lead role in anti-poverty efforts. Recent work in developing the PRSP has seen the Ministry of Finance and Economy (MoFE) take a much more important and proactive role in this area. Government has decided to retain an inter-ministerial committee as an oversight body for the proposed project and related operational programs, and the newly reconstituted National Committee for the Household Livelihoods Capacity Support Program (NCHLCSP), which replaces NPAC, assigns a much more significant role to MoFE. If necessary, consideration may also be given to amending the Government Law in due course.

Inadequate capacity building. This issue would be addressed through efforts to build institutional capacity as an integral part of each of the components, and program-wide investments in improved management, monitoring and evaluation capacity. Lessons learned under PAVGP suggest that: (a) capacity building

essential to a project cannot be left to parallel financing – it must be costed and included as an integral part of the project; (b) capacity building at the *sum/khoroo* and community (*bag* and below) levels should be a major area of concentration; and (c) provision needs to be made for ongoing training/ re-training in view of staff turnover.

Weakness in pastoral risk management. A major new component of the program/project, compared with NPAP, would be the development of a pastoral risk management strategy adapted to *aimag*-specific conditions in order to reduce the losses of poor herding households due to drought, *dzud* and other episodic shocks. Ministry of Food and Agriculture (MoFA) also has an enhanced role in the NCHLCSP, in recognition of the need for public action in and promoting secure and sustainable livelihoods among the rural poor.

Inadequate community participation, sustainability, and decentralization. The project would improve community participation and sustainability through a decentralized and demand-driven approach to identifying, co-financing and executing investments in basic infrastructure under the local initiatives fund. This would help to lay the foundation for future fiscal decentralization by enhancing district and community-level capacity in sub-project selection, implementation, monitoring and evaluation; and by identifying fiscal decentralization options and mechanisms.

Underdevelopment of financial system, particularly in rural areas. The micro-finance outreach component would support the development of Mongolia's small and fragile financial sector by expanding the range and outreach of micro-finance services targeted to poor households and especially the rural poor, including both insurance and micro-credit.

Based on lessons from experience under NPAP, the following **strategic choices** have been incorporated in program design:

First, the program is based on the recognition that the *livestock sector* in Mongolia has played an extremely important, though under-recognized, role as an economy-wide safety-net throughout the period of economic transition to date, and that it would continue to do so over the medium- to long-term. The multiplier effects of livestock production are even wider than its direct contribution of around a third of GDP suggests, given the importance of non-monetary, inter-household (rural to urban) transfers of livestock products in assuring domestic food security. Mongolia has been highly successful in maintaining an environmentally sustainable livestock sector, notwithstanding recent pressures that have led to a decline in pastoral mobility and a rise in localized congestion, overgrazing, and conflict over pasture. The national-level legislative and policy framework broadly facilitates and underscores the importance of pastoral mobility, and includes constitutional protection of pasture land as public land to be held and managed by communities as common property.

The pastoral risk management component addresses some of the recent pressures directly. However, it is recognized that the pastoral livestock sector cannot continue directly to support as many herding households as at present, and that many of the 'new' herders would rather pursue alternative livelihoods if they had the opportunity to do so. Project design therefore incorporates the strategic choice that support for livestock-based livelihoods be enhanced through initiatives in risk management; while parallel support for 'exit strategies' and livelihood diversification for those who would prefer to make a living by means other than pastoral livestock production also be provided, through micro-finance outreach and associated technical assistance, and support for community-level investments in the infrastructure needed for private-sector led growth. Other donor-supported programs also aim to contribute to livelihood diversification through vocational training.

Second, the program addresses both *public and private goods* aspects of a strategy to achieve secure and sustainable livelihoods for all. The pastoral risk management component supports the provision of public goods conducive to creating an environment for private-sector livestock production and associated processing enterprises, at various levels from small groups of herding households through all levels of public administration. The micro-finance outreach component aims to increase access by poor and vulnerable individuals and households to micro-finance services as private goods, but provides public goods by ensuring adequate outreach in remote rural areas and through the provision of technical assistance that the private sector would not provide unaided. The Local Initiatives Fund is aimed at providing public goods in the form of basic infrastructure for *sum/ bag* communities through a community-based prioritization and selection methodology. These activities will not only improve essential services to the targeted households, but also create an environment conducive to market development and further facilitate the activities of the private sector.

Third, it is recognized that the three main project components – pastoral risk management, micro-finance outreach and local initiatives fund – while all contributing essential elements to a strategy for promoting secure and sustainable livelihoods, necessitate somewhat different management/ organizational structures for their successful implementation. *Project management* arrangements must reflect this, for example, by constituting distinct technical steering committees for each component and at different levels of administration, while also facilitating the intended synergies among project components.

Fourth, the project as originally identified foresaw a broad range of pilot initiatives in pursuit of sustainable livelihoods in a limited area of the country that could be scaled up in the subsequent two phases of the program. However, Government clearly regards the proposed project/program as a follow-on and in some respects a continuation of NPAP, which was a nation-wide program supporting investments in both rural and peri-urban areas, and was unwilling to be seen to be 'scaling back' its direct, poverty-targeted interventions. A strategic choice has therefore been made regarding the *geographical scope* of the project to continue some of the most successful elements of NPAP nation-wide under the proposed project, with certain modifications, while also piloting institutional innovations in selected *aimags*.

Fifth, significant *capacity-building* activities are an integral feature of program design (see Annex 13 for a summary). This does not imply large inputs of international consulting services, however. Based on past experience, Government has expressed a strong desire that local capacity in technical assistance be strengthened to permit better targeting, better use of development finance, and more sustainable outcomes. Therefore, many of the technical assistance activities envisaged for project financing would take the form of local 'action-research' contracts in order to build on and make effective use of existing local capacity, and particularly to build on the experience, successes and management capacity of NPAP. While the broad scope and multi-faceted nature of proposed program activities is warranted in seeking to support secure and sustainable livelihoods, it also poses risks for implementation arrangements. Most importantly, it will not be possible to pursue all the proposed capacity-building activities in all project areas at the same time. Strategic choices will be made among project components to determine the most appropriate sequence of interventions according to prevailing conditions, needs and performance of each selected *sum* and *aimag*.

Sixth, *exploiting institutional and regional diversity* is a hallmark of program design. Program design must be consistent with local specificities rather than following the traditional "one-size-fits-all" approach. This also applies to resource allocation and targeting of benefits: rather than distributing resources equally to sub-national governments and to individual beneficiaries, the project would pilot mechanisms that provide efficiency incentives to reward better-performing local governments, communities, and individual borrowers, while maintaining poverty targeting. Given Mongolia's high regional and ecological diversity,

the weight of emphasis among and within the various components of the project would vary from *aimag* to *aimag*. Pastoral risk management would assume higher priority in areas most prone to *dzud* risk, while areas closer to markets offer greater potential for pilot-testing institutional innovations in micro-finance service delivery. Similarly, the precise character and impact of *dzud* and other weather-related hazards varies according to local ecological conditions, and the mix of elements in an appropriate risk management strategy would therefore differ from region to region (e.g. fodder production/conservation versus marketing). In short, the project would not attempt to do everything, everywhere, but would use geographical diversity as an opportunity to learn-by-doing through alternative combinations or sequences of project interventions.

4. Program description and performance triggers for subsequent loans:

Intended **end-of-program outcomes** for each component are as follows (see also Annex 11 for a synopsis of program vision and approach):

- A nation-wide **pastoral risk management system** adapted to the specificities of each *aimag* would be in place and functioning well, offering locally relevant options to enable herder households to reduce their vulnerability to drought, *dzud* (winter disasters), and other episodic shocks that undermine their livelihoods;
- A diverse range of **micro-finance services** would be available nation-wide on an institutionally and financially sustainable basis, to enable poor households and individuals to better manage risk, smooth consumption over time, diversify income sources, invest in productive activities, and accumulate livelihood assets;
- A **Local Initiatives Fund (LIF)** would be in place and functioning well throughout the country to facilitate community-level prioritization, selection, co-financing, execution, and maintenance of investments in basic infrastructure and social services. This LIF would have been fully integrated into the government budget; a needs-driven system of inter-governmental transfers would be in place that gives local government and targeted communities more discretion over capital expenditure; and a high level of fiscal decentralization would have been achieved; and
- The decision-making processes and structures developed during the execution of the program would have been refined, consolidated and integrated into the regular functioning of local and central government, and the policy/legislative framework would provide an effective enabling environment for sustainable livelihood programs.

For the program as a whole, agreed **performance triggers** between phases are summarized below (see attachment to Annex 1 for detailed phasing and triggers by each component). Performance triggers would be assessed well in advance of the end of each phase of the program (successive IDA credits), prior to the appraisal of the subsequent phase.

Triggers from Phase I to Phase II:

- legal and regulatory basis established, in the form of appropriate legislative and policy reforms at national and sub-national levels, for pastoral risk management, fiscal decentralization, and micro-finance sectoral development;
- project management framework has demonstrated institutional and financial sustainability (e.g. physical targets met, demonstrated financial management capacity achieved, LIF sub-project identification in the hands of communities, effective system for participatory monitoring and evaluation in place and functioning); and

- substantial improvement of output indicators (e.g. increased coverage of micro-finance services, higher proportion of small infrastructure construction identified, built and maintained by community); and evidence, in pilot *sums*, of substantial improvement in outcome indicators.

Experience under NPAP suggests that it would be important not to require unduly onerous national-level policy or legislative reforms as triggers for Phase II, since this may preclude the option of continuing support for local-level initiatives even in the absence of national reforms. Progress towards fiscal decentralization, however, is likely to be critical to program success, and should be regarded as a 'killer' trigger for moving to Phase II.

Triggers from Phase II to Phase III:

- institutional innovations with demonstrated success would have been introduced nation-wide;
- legislative and policy reforms adopted and implemented (e.g. attainment of targets for transparent, formula-driven fiscal transfers to local government and communities, revenue-sharing between local government and communities); and
- program evaluated and issues to be addressed have been identified.

Further conditions would be investigated in detail and agreed during preparation of Phase II.

C. Program and Project Description Summary

1. Project components (see Annex 2 for a detailed description and Annex 3 for a detailed cost breakdown):

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, supporting community-based pasture management, including mapping and re-instituting seasonal pasture rotation (including specific actions in cases of 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:

(A) 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 (through 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 Operational Manual (the Operational Manual) acceptable to IDA. 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 (subsidiary 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 (Mongolian 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 sustainable micro-finance institutions. **As conditions for the disbursement of IDA funds allocated to this sub-component for the micro-finance sub-loans (Category 5, for a total equivalent to about US$3 million), the Borrower would: (a) establish a MIS adequate to monitor micro-finance portfolio quality (in accordance with CGAP guidelines); (b) adopt an Operational Manual acceptable to IDA for the implementation of the sub-component; (c) establish and maintain during project implementation the Micro-Finance Development Fund (including the Board and the Management Office) under terms and conditions satisfactory to IDA; and (d) accredit MFIs 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 Operational Manual.**

(B) 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 financial resources to help selected RLFs approve new sub-loans to project beneficiaries, in accordance with their business plans, and contributing to improve their portfolio quality and their financial situation; and (vi) eventual privatization of the best-performing RLFs. **As conditions for the disbursement of IDA funds allocated to the provision of sub-loans by the selected RLFs (Category 6, for a total equivalent to around US$ 500,000), the Borrower would: (a) establish a MIS adequate to monitor micro-finance portfolio quality (in accordance with CGAP guidelines); and (b) prepare a detailed Action Plan for the use of these funds, acceptable to IDA, with the objective of strengthening the selected RLFs.** 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 funds for sub-loans, the purposes and uses of the sub-loans, as well as the steps to be taken towards the eventual privatization of these RLFs.

(C) Development of an index-based livestock insurance scheme. A risk index would be developed during the first year of the project with technical assistance support, on the basis of which eligible, participating private insurance companies would offer livestock insurance to individual herders, herding households, or other juridical persons owning livestock to cover covariant risk arising from dzud, drought, or other weather-related events. The index, based on objective, third-party verifiable indicators such as weather data, livestock mortality rates, and/or indices of range vegetation condition, would differentiate relative risk at an appropriate level (most likely at *sum* level) based on historical data. Indemnities under the scheme would be triggered once the index exceeded a given threshold level specific to that *sum*. Insurance cover would be for productive activities including: the replacement value of livestock; the value of goods or services to support risk preparedness and/or enhance livestock productivity, such as hay and fodder production or purchase, acquisition of veterinary drugs and services, construction of livestock shelters, and breeding services; and/or the value of goods and services to allow policy-holders to engage in alternative or supplementary livelihood strategies. Payments to participating insurance companies, on claims paid to policy-holders against covered risks and for such productive activities, would be made when the aggregated amount of these claims exceeds the agreed level of liability of the insurance company, as specified in a stop-loss agreement between the Government and the participating insurance company. The project would also finance training workshops for participating insurance companies and public officials involved, and a nationwide information campaign to publicize the scheme and attract policy-holders. 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. The role of Government during the start-up phase of the scheme (project years 2 to 4), would be to assume liability beyond the level agreed with participating insurance companies by undertaking to finance the stop-loss payments from the proceeds of the IDA credit. This stop-loss provision would take the place of international reinsurance, which would be unlikely to be attracted until commercial viability of the scheme could be demonstrated. **Conditions of disbursement of IDA funds to finance the stop-loss amounts (Category 7, for a total equivalent to US$ 1,000,000) would be the provision of evidence to IDA that the index-based livestock insurance scheme has been established, that stop-loss agreements have been concluded between Government and any participating insurance company, that insurance policies have been issued, that one of the covered risks has occurred, and that claims under these policies have been filed.** 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 a Government-financed 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 government grants based on clear and transparent criteria for inter-governmental budget transfers. The project would target all members of *sum* and *bag* communities in the core *aimags*. Principal effort will be placed in establishing effective mechanisms by which all members of these target communities can come together to identify their key infrastructure development needs and prioritize them for potential sub-project financing. Sub-projects would be selected from an open menu, with a negative list that would preclude, for example, investment for private goods, in environmentally damaging activities, and for religious purposes. Financial ceilings have been established to guide the initial allocation of these resources to all participating *sums*. Subsequent annual allocations would be made based on criteria

such as overall sub-project implementation performance, financial management, and poverty levels. Three sub-components would deliver this output: (i) there will be 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) that will provide for decentralized sub-project approval at the *sum/bag* -level ($8,000 ceiling per *sum*; $15,000 ceiling in the pilot *duureg*); and, in modified form, the Local Development Fund (LDF) which was initiated nationwide under NPAP, in the 13 other *aimags* and 8 other *duuregs* in the country where sub-project decision making could remain at the *aimag*-level ($4,000 ceiling per *sum*; $15,000 ceiling per *duureg*); (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 operational costs associated with the HLSPO, including vehicles, equipment, recurrent costs, and incremental staff hired as long-term consultants on fixed-term contracts at central, *aimag* and *sum* levels; (ii) technical assistance to develop institutional capacity to generate inputs for policy and legislative reforms; (iii) information dissemination and communications; (iv) project orientation workshops and training; (vi) monitoring and evaluation; and (vii) auditing.

Component	Sector	Indicative Costs (US$M)	% of Total	Bank-financing (US$M)	% of Bank-financing
Pastoral Risk Management	Livestock	5.70	25.8	4.13	22.1
Micro-Finance Outreach	Other Finance	6.01	27.2	5.00	26.7
Local Initiatives Fund	Community Action Program	9.16	41.4	8.52	45.5
Management and Policy Support	Institutional Development	1.25	5.7	1.08	5.8
Total Project Costs		22.12	100.0	18.73	100.0
Total Financing Required		22.12	100.0	18.73	100.0

2. Key policy and institutional reforms supported by the project:

Policy and institutional reforms in four principal areas are relevant to the proposed project: fiscal decentralization, livestock insurance, land law, and micro-finance regulation.

Little progress has so far been made by Government on the issue of **fiscal decentralization**. The proposed Public Sector Finance and Management Law would initiate certain related reforms concerning the accountability of public institutions including sub-national governments, inter-governmental transfers, and civil service reform. MoFE is the lead Government agency in this regard. The project would support MoFE's efforts to explore and pilot-test through an 'action-research' approach in the latter two years of the project, options for fiscal decentralization in relation to inter-governmental transfers; and transparency, accountability, and priority-setting in co-financing of public infrastructure activities with targeted communities. The pilot initiatives would test different strategies and administrative modalities for the progressive transfer of control over local capital expenditure from central to local governments. It is envisaged that promising options be implemented on a wider scale under Phase II of the program, and be further refined and deepened under Phase III. A possible trigger for each phase would be an agreed action plan for scaling-up these fiscal decentralization pilots on an operational scale.

GoM has been developing a law to make **livestock insurance** compulsory, in response to the catastrophic *dzud* losses of 1999-2001. An earlier draft was rejected by Ikh Khural (national parliament) in spring 2001, and the Government working group (made up of senior staff of MoFE and MoFA) is seeking assistance through the project in developing a feasible approach to livestock insurance under local conditions. The feasibility of the conventional approach to livestock insurance, which attempts to indemnify animal losses at the individual household level, has been seriously questioned by international insurance specialists. It is unlikely to be financially profitable or sustainable; it promotes the wrong incentives in livestock management ('moral hazard'); it would incur high costs in loss adjustment (verifying household-level losses); and it is highly unlikely to attract international reinsurance for these reasons. GoM would therefore risk incurring high costs to the public budget in bailing out insurance companies under the currently proposed law, and its likely failure could undermine public confidence in future efforts to develop even well-founded insurance schemes. On the basis of a feasibility study conducted as part of project preparation, it is proposed under the project to develop and implement an alternative, index-based approach to livestock insurance, using weather data, indicators of range vegetation condition, and/or livestock mortality data as the basis for a locally varying index. Insurance payments would be made to all holders of insurance certificates in a given area once a given threshold is triggered in the relevant index. Under this alternative approach, herders would face strong incentives to take management actions to prepare for risk events and to reduce their expected losses (i.e. the moral hazard problem is significantly reduced or eliminated).

Significant amendments to the 1994 **land law** are due for debate in the spring 2002 session of Ikh Khural. In part influenced by Bank-supported analytical and advisory work on land-reform options during 2000, many of the proposed reforms concern an expansion of the ways in 'possession' rights over certain types of land (chiefly urban and arable) may be transferred, including transfer by sale which would open up a free land market in Mongolia for the first time. For a variety of reasons, it is not thought appropriate for pasture land to be subject to transferable possession rights, although this is currently under debate. It may be appropriate, however, for groups of herders to hold non-transferable possession rights over pasture land in order to enhance their security of tenure and prospects for sustainable management, subject to resolving questions of group size, corporate identity, and membership; and negotiation of reciprocal rights of access by other groups during times of drought or *dzud*. Recognizing that the current law provides, in principle, a supportive framework for such operational experiments, the project will support approaches to

community-based pasture land tenure and management under the pastoral risk management component, and will support required policy reforms. As recent work suggests, however, improving consistency and transparency in implementation of the land law are more important than new legislation. The project will support certain institutional reforms in this direction, including promoting public access to information concerning land law implementation, the preparation of manuals and implementation guidelines for use by local governors, and mechanisms to resolve disputes over pasture land tenure.

The fourth area for institutional development and policy reform to be supported under the project concerns the **legal and regulatory framework for non-banking financial institutions** (NBFIs). Under the existing legislation, NBFIs are not regulated by the BoM and cannot receive financial assistance from it. However, the parliament is currently considering legislation to regulate the NBFIs. The aspects of most concern to the project and the micro-finance outreach component are the NBFIs' ability to operate effectively as MFIs and their ability to promote savings mobilization. The project would provide technical assistance to support the adoption of a legal and regulatory framework, as well as the adequate prudential requirements, that would allow NBFIs to take client deposits and to offer diversified financial products, thus becoming viable and financially sustainable intermediaries providing an important service for the target population under the project.

3. Benefits and target population:

Target Population

The program targets the "able-bodied poor" and "low-income households near the poverty line who are at risk of falling into poverty as a consequence of external shocks." The former category – "able bodied poor" – corresponds roughly to the total households below the poverty line minus those who are unable to respond to livelihood-based opportunities because they are either elderly, or physically or mentally unable to become self-supporting. The elderly and disabled are provided with material and financial assistance from the State as stipulated by the Constitution of Mongolia (Article 13, sub-article 5). The latter category "low-income, vulnerable non-poor" corresponds roughly to the 28% of the population whose per capita consumption is between the poverty line and 1.5 times the poverty line. The share of the population in the latter category is relatively large because income distribution is rather flat and there are a large number of households at or near the poverty line. Hence, in Mongolia, the total number and proportion of poor is particularly sensitive to the placement of the poverty line; a small increase in the poverty line could lead to a large increase in numbers and percentage of poor. In fact, if a less conservative yardstick of poverty were used (such as US$1 per capita per day), the low-income non-poor would qualify as poor.

The eight core *aimags* have a total population of around 155,000 households or 650,000 people, living in an area of 740,000 sq. km. with an average density of one person per sq. km. Together they account for 47% of Mongolia's land area, 27% of its population, and 45% of its rural population. Some 72% of the total population is rural, ranging from a high of 84% in Ovorkhangai and Tov to a low of 45% in Dornod. Average household size is 4.3 persons. Other major characteristics of the eight core *aimags* are summarized in the following table:

Parameter	Bayan Olgii	Uvs	Bayan khongor	Ovor khangai	Omno gov'	Dund gov'	Tov	Dornod
Region	West	West	West	Center	Center	Center	Center	East
AEZ	Altai	Altai	Altai	Khangai	Desert	Steppe	Steppe	Steppe
Mean annual precipitation	115mm	138mm	199mm	245mm	127mm	173mm	273mm	248mm
July temperature	16.3 oC	19.0 oC	18.3oC	15.3oC	21.1oC	23 oC	15.6oC	19.8 oC
Jan temperature	-17.2 oC	-32.3 oC	-16.2 oC	-14.7 oC	-14.9 oC	-26 oC	-20.4 oC	-20.5oC
Dzud risk category	H	M	M	H	H	H	M	L
Poverty incidence	3rd	6th	8th	9th	18th	22nd	20th	5th
Poverty headcount	7th	5th	10th	4th	19th	20th	13th	9th
Market accessibility	Poor	Poor	Poor	Moderate	Poor	Moderate	Good	Moderate
Herder % of all HHs	48%	53%	79%	72%	59%	67%	42%	28%
Ethnicity	Kazakh	Turkic	Khalkh	Khalkh	Khalkh	Khalkh	Khalkh	Buryat

Of the total Mongolian population of 550,000 households, the target population (able-bodied poor) comprise around 120,000 households. In addition there are some 150,000 low-income/ vulnerable non-poor households, making up a national target population of 270,000 households (1.3 million people). In the eight core *aimags,* the project's target population comprises around 80,000 able-bodied poor and vulnerable low-income households near the poverty line (355,000 people).

Although the priority target groups are the able-bodied poor and the low-income, vulnerable non-poor, this does not mean that the project would benefit these groups alone. The LIF component needs to work with the entire community (including the non-poor and the non-able bodied poor) to identify local priorities and to mobilize the 10% local contribution in cash and kind, and the pastoral risk management component needs to work with the entire herder community because the non-poor own the majority of animals. Moreover, in selecting community-based schemes for LIF financing, priority would be given to projects having the broadest possible benefits to the poor. Likewise the PRM component would ensure that herder groups include the poor and that their grazing rights are safeguarded.

One distinct target-group, falling within the overall categories of 'able-bodied poor' and 'low-income, vulnerable non-poor', are the 'newcomers' to herding. This group, most of whom lost public sector jobs following decollectivization and the restructuring or closure of other state-owned enterprises, typically acquired animals under privatization and took up livestock production in the absence of alternative livelihood opportunities. The number of herding households in the country more than doubled between 1990 and 2000 from 74,710 to 191,526. Compared with those who had been herding livestock prior to 1990, many of the newcomers tended to be younger, less skilled and experienced in herding, more urban-oriented, less well connected with other herders and often excluded from gaining secure access to winter-spring grazing and, as a result of these factors, less likely to move base camp as often as would be required for sustainable pasture land management. Many of them would also much rather pursue a livelihood through some means other than livestock production, if they had the opportunity to do so. The project aims explicitly to offer this group an 'exit strategy' from livestock production, primarily through access to micro-finance services that would assist in substituting alternative assets and income sources for livestock.

Beneficiaries

Under the LIF component, all *sums* and *khoroos* in the country are expected to benefit from *sum*-level infrastructure projects, as occurred under NPAP, since they would benefit from funding from either LIF or LDF. Therefore, the entire Mongolian population (550,000 households) would benefit, of which

approximately 60% are poor or near poor. In addition, an estimated 70,000 households in the core *aimags* (50% of the total population) would benefit from the LIF.

Pastoral risk management activities at national level such as improved drought and *dzud* forecasting and contingency planning would potentially benefit all herder households in the country (190,000 households of which 86,000 in the core *aimags*). Pilot activities in the eight core *aimags* are expected to build up gradually from 16 to 143 *sums* with a target population of around 50,000 herding households. Around 5,000-8,000 herding households would benefit directly from activities supported through herder self-help groups.

Under the micro-finance outreach component, RLF strengthening would benefit an estimated 18,000 clients (12,000 existing clients plus 6,000 new borrowers). The number of clients (sub-borrowers) of the selected MFIs that would receive loans from the MDF in the eight core *aimags* are estimated to be around 10,000 households. Total direct beneficiaries (excluding double-counting) are expected to be around 20,000-25,000 households.

Benefits

The principal benefits of supporting **pastoral risk management** would be reduction in *dzud*-related animal losses (both adult and newborn animals). The project is expected to reduce losses in pilot *sums* of core *aimags* by 33% by comparison with the start of the project and/or non-project *sums* in similar ecological zones. No assumptions have been made about improvement in other parameters such as age at first parturition, calving/kidding rates, and milk production per lactation, off-take of live animals or wool or cashmere production. Herd models illustrating typical build-up of animal numbers have not been prepared because of their limited applicability to situations in which there are wide and unpredictable annual changes in productivity parameters as a result of the presence/absence and sequencing of drought and *dzud*.

The main benefit from **micro-finance outreach** would be increased availability of financial resources to members of poor communities for income generation and asset/ wealth creation. The household-level benefits would be a fall in unemployment and an increase in the number of micro-enterprises in the communities with access to micro-finance. Institutionally, there would be an increase in the number of self-reliant RLFs, successful independent MFIs, and a proliferation of a new range of poverty tailored micro-finance products and services available to poor households. The increased availability of micro-finance products tailored to the needs of poorer and vulnerable groups would also facilitate an 'exit strategy' for the many new herding households who would prefer to pursue alternative, less risky livelihoods, and would thereby help to improve the prospects both for livelihood security and sustainability for this specific group, as well as for sustainability of livestock production and pasture land management within the extensive livestock sector as a whole. It is unlikely that the livestock sector could continue to support the number of herding households that it currently supports, even with the measures to restore levels of pastoral mobility and pastoral livelihood security envisaged under the pastoral risk management component.

The main benefits from the **Local Initiatives Fund**, and continuation of the existing LDF, would be improved access of rural and peri-urban households to basic infrastructure as well as greater availability of financial resources to local government – specifically *sums* and *duuregs* – for rural and peri-urban infrastructure that responds to the needs and priorities of poor communities. Specific benefits include: (a) a new community-responsive and local government-managed funding mechanism (LIF), piloted and extended to *sums/ duuregs* in about one third of the country; (b) funding for the LDF made available to allow it to continue to provide funding nationwide for *sum*-level projects; (c) capacity at *bag*, *sum*, *aimag* and central

level for managing such funding mechanisms increased and the associated operating procedures developed, piloted and mainstreamed; and (e) the advantages, disadvantages and repercussions of bringing the LIF into the regular government budgetary process, and with it allocating to the *sums/duuregs* financial resources over which they have discretionary powers, would be ascertained and an action plan developed for how to manage such a process in the Phase II of the program.

4. Institutional and implementation arrangements:

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 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)); and representative civil society institutions.

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 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 143 *sums* of the eight core *aimags* selected for pilot activities would be considerably strengthened. At *aimag* level, a technical working group for the PRM component, analogous to the national-level Working Group, will be constituted from the relevant line departments to advise on 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*; see Map 1), 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 Operational Manual (the Operational Manual) acceptable to the Bank. The main sections of the Operational 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 Operational 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, these options will have to be discussed in the context of the preparation of the Phase II of this APL, and the specific actions to implement the recommendations arising from this privatization study would be included in the design of this Phase II.

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 subsidiary loans by MFIs (including principal, interest and fees) 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, micro-enterprises, and juridical persons) 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 are estimated to average 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 subsidiary loans to MFIs would not exceed the equivalent of US$1 million for any individual MFI during the period of implementation, or such revised ceiling as specified, with IDA's prior concurrence, in the Operational Manual.

On-lending Arrangements. The proceeds of the IDA credit allocated to this sub-component (Category 5, amounting to around $3 million) would be made available directly from the Special Account to support sub-loans approved by accredited MFIs. The Project's HLSPO would disburse and transfer (in local currency), through MDF, the amounts required to cover those sub-loans approved, in accordance to the terms of the subsidiary loan agreements (SLAs) signed with accredited MFIs. The subsidiary loan agreements to MFIs will be provided 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 Operational Manual, in a manner acceptable to IDA. 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 IDA on: (i)

the interest rates on subsidiary loans to participating MFIs; and (ii) on the level of interest rates charged by MFIs on sub-loans to final sub-borrowers. This would be done twice a year, not later than March 31 and September 30 each year, commencing on March 31, 2003.

Project Implementation Manual (PIM). Detailed implementation guidelines for all aspects of the project are provided in the Project Implementation Manual (PIM). This includes separate sections dealing with: pastoral risk management, local initiatives fund, local development fund, micro-finance operational manual, revolving loan funds, environmental management plan, resettlement policy framework, ethnic minorities participation framework, financial management and reporting (including format of FMRs as an appendix), procurement (including sample documents as appendices), and monitoring and evaluation. **It is a condition of effectiveness that the PIM has been finalized and adopted in a form acceptable to IDA, and that staff of the HLSPO and of the HLSCs in all *aimags* and *duuregs*, and in the 16 *sums* selected to participate in the project for the first year of activities, have completed a training course satisfactory to IDA on the provisions of the PIM.**

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.

The range and periodicity of monitoring and evaluation reports to be provided to IDA shall include (see also Annex 1): (i) quarterly Financial Monitoring Reports (FMRs), including updates of physical progress as measured using output indicators; (ii) semi-annual progress reports, on or about July 31 and January 31 each year, beginning on January 31, 2003, describing progress towards meeting the project's objectives during the preceding calendar semester as measured using output indicators, and incorporating the respective FMR for the preceding calendar quarter; (iii) annual performance monitoring reports, on or about July 31 each year, commencing in 2003, on progress towards meeting the project's objectives based on outcome and impact indicators during the preceding calendar year; (iv) a comprehensive evaluation report as an input to the Mid-Term Review (MTR), on or about July 31, 2004, in respect of the period June 30, 2002 to June 30, 2004, based on outcome and impact indicators; and (v) a project completion report not later than six months prior to Credit closing. A baseline survey shall be conducted by no later than March 31, 2003, in order to provide benchmarks against which project progress can be assessed, for all agreed performance indicators not readily available from secondary sources.

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.

D. Project Rationale

1. Project alternatives considered and reasons for rejection:

Project alternatives considered include: alternative lending instruments, alternative components, alternative geographic scope, alternative design features, and alternative implementation arrangements.

Alternative Lending Instruments: The two alternative lending instruments considered for the proposed project were: an Adaptable Program Loan (APL), with triggers to move to subsequent phases; and a Specific Investment Loan (SIL). The choice of an APL was made based on the strong rationale for the proposed long-term, phased approach to institutional innovation, capacity building, and decentralization, with a long-term vision underpinning the program approach (this is summarized in Annex 11, along with the Government's Letter of Development Program). The program calls for flexibility in implementation, for which an APL is well suited. Triggers for the subsequent phases of the APL would give a strong incentive to the government in moving reforms forward. Many of the components also have a strong 'learning by doing' character, for which an APL is particularly apt. Participatory monitoring and evaluation would be an important design feature in all components. It was also important to signal to Government that the Bank would be prepared to make a long-term commitment to supporting the proposed program, consistent with the CAS and in the wider context of the PRSP.

The alternative lending instrument considered was a SIL. There are several reasons why a SIL might be thought more desirable, on grounds of limited Borrower capacity: (i) limited capacity within the public sector; (ii) problematic current administrative and fiscal relations between central and local governments, which present complications in identifying clear lines of accountability; and (iii) the complexity arising from combining vertical deepening and horizontal expansion aspects in an APL approach. While the demands on the Borrower may be lower with a SIL, this alternative lending instrument was rejected on the grounds that strengthening of borrower capacity is itself a necessary and explicit aim, within a long-term and phased program of institutional innovation.

Alternative Project Components: The proposed project needed to address major constraints on the achievement of secure and sustainable livelihoods in Mongolia while not duplicating efforts being supported by other donors and multilateral agencies (see Annex 12 for a summary of relevant donor-supported activities). There is also a need to have a degree of synergy between the proposed components, so that the contribution of the project was more than simply the sum of its parts. Several areas of possible intervention were ruled out on these grounds. For example, support for formal safety nets and restructuring of the welfare system (state pensions, allowances, health insurance, etc) are being addressed under an ADB-financed Social Security Sector Development Program. USAID is providing ongoing support for public/private partnerships in several *aimags* of the Gobi region through the Gobi Regional Economic Growth Initiative, although this program is not specifically poverty targeted. Business advisory services, vocational training, and support for a poverty research unit are being addressed under a UNDP/ SIDA-financed project for which identification was conducted in a joint exercise with identification of the proposed Sustainable Livelihoods Program/Project. Other ongoing and planned donor-supported initiatives

are also complementary, and have been designed explicitly to pilot-test approaches for implementation under the proposed Sustainable Livelihoods Project (notably the FAO-financed TCP project on Pastoral Risk Management, and the UNDP/Center for Policy Research action-research project on herder organization and pasture land management). In summary, the proposed components (pastoral risk management, micro-finance outreach, local initiatives fund, and project management support) are judged to offer the best prospects for addressing the main livelihood problems of poor herders and informal sector households in *sum* and *aimag* centers and *ger* districts of Ulaanbaatar, while complementing and building on NPAP and other government- and donor-supported initiatives, and acting in concert to contribute to the overall objective of poverty reduction.

Alternative Geographic Scope. During program identification, it was proposed that the Bank support pilot activities in 6-8 *aimags* during Phase I (the project) with the intention of scaling-up successful pilots nationwide in Phase II. However, since the proposed program was designed as a follow-on to the nation-wide NPAP, it proved to be politically unacceptable to move from a national-level program to one limited in scale to pilots in selected *aimags* alone. The agreed solution was for the proposed program/project to continue support nation-wide for the Local Development Fund (LDF) and the Revolving Loan Funds (RLFs), while in parallel piloting new approaches in eight selected *aimags*, with the aim of extending them to other *aimags* in the second phase once they have been proven successful and replicable. Under the original proposed project design, the PRM and LIF components were to be piloted on a more limited scale in the eight core *aimags*, in the case of PRM covering only 32 *sums* by end of project (Phase I). The alternative design now proposed for these components involves scaling-up project activities more rapidly to cover all 143 *sums* in the eight core *aimags*, based on pilot activities to be implemented in 16 *sums* during the first year of the project.

Alternative Micro-Finance Designs. In response to the joint Government/ UNDP/ World Bank evaluation of NPAP, which was highly critical of the local government-administered credit scheme, project identification considered withdrawing support altogether from the existing RLFs and starting afresh to build a sustainable rural micro-finance system in partnership with existing commercial banks and NBFIs. During project preparation, limited support for strengthening the existing RLFs without privatization was considered, but this proposal drew criticism from local NBFIs. A dilemma arose because the *sum*-level RLFs were the only credit program currently serving the rural poor and considerable effort has gone into building local capacity to manage them. The micro-finance outreach component design overcomes this dilemma by providing limited, time-bound support to the existing RLFs to enable these local government-administered funds to become independent micro-finance providers.

Second, from the earliest stages of identification, it was also envisaged that the project would support the development of new approaches to achieving institutionally and financially sustainable micro-finance service outreach in remote rural areas, consistent with international good practice in micro-finance. Following project preparation, it was proposed to create a new apex institution - a "Micro-Finance Outreach Foundation" - to act as wholesale lender to existing MFIs, to offer technical assistance to MFIs in conducting market research and in developing new micro-finance products accessible to the poor, and in building business management skills among potential clients. The Foundation was to have been created over the first two years of the project, and to have begun wholesale lending by project year 3. At appraisal, a modified design was proposed and developed for this sub-component, in response to concerns from Government and from private-sector MFIs that there was little current demand for a new apex institution, and that the delayed start of wholesale lending activities in project year 3 would be unacceptable given the pressing need for micro-finance outreach. The modified design proposes that the central bank (Bank of Mongolia) instead act as the wholesale lender under the project, through a small fund-management unit to be financed in part from the interest-rate spread from on-lending to selected MFIs, and that wholesale

lending to selected MFIs would begin from the start of the project. It is envisaged that this fund-management unit will function independently of Bank of Mongolia under Phase II of the program, when it would assume a similar institutional form to the originally-proposed Micro-Finance Foundation.

Third, it was envisaged from project identification that the project would support the development of micro-finance services designed specifically for herders. During project preparation, this was included as a sub-component of the PRM component. At pre-appraisal, it was decided to include this sub-component under the MFO component, given that private financial institutions would be the major actors in developing new micro-finance products for herders as well as for other socio-economic groups. The clearest identified need, other than for productive sub-loans for herders during the late-winter/ early-spring season (peak demand for credit is around the lunar New Year, *Tsaagan sar*, while income from livestock products such as raw cashmere does not flow until later in the spring) was to develop feasible approaches to livestock insurance. Following project preparation, it was proposed that the project would support the development of an index-based approach to livestock insurance on a pilot basis only, focusing on a small number of *sums* in the eight core *aimags*. At appraisal, it was agreed with Government that more substantial resources should be made available through the project to develop the proposed index-based livestock insurance scheme during the first year of the project, with a view to its being fully operational at the national level by the end of project.

Alternative Pastoral Risk Management Designs. The alternative of supporting the entire GoM program for protection of livestock from drought and *dzud* (Resolution No. 47) was considered but rejected because the GoM program embraces a number of activities only loosely connected with risk management, including livestock extension, veterinary services, and breed upgrading. Since the technical means for upgrading livestock production are well known in Mongolia, while pastoral risk management under market economic conditions remains at a more experimental level, a conscious choice was made for the project to concentrate on pastoral risk management, leaving support for livestock production more generally to donors such as ADB and IFAD. A conscious decision was also made to concentrate the bulk of project investments on the early stages of the risk cycle (risk avoidance and risk preparedness), in recognition of the fact that considerable donor resources are already available to GoM for emergency response and post-*dzud* recovery.

Finally, concern is mounting within both Government and the donor community about the advisability of the current, state-directed approach to restocking, which it was originally proposed would be supported under the project in cases of emergencies, following the procedures developed under PAVGP. Owing to the likely disincentive effects of restocking for pastoral risk management and micro-finance outreach, it was agreed at appraisal that a direct approach to restocking would not be financed under the project. The conventional, direct approach to restocking is likely to conflict with the primary objective of improving risk preparedness, and involves public officials or community leaders in making difficult judgements concerning the viability of particular individual households to continue to be involved in herding activities. The alternative component project design agreed at appraisal foresees the implementation of pastoral risk management on a wider scale than was originally envisaged; and through synergies with other project components would also support alternative, commercially-based, and demand-driven approaches to restocking and livelihood diversification. Restocking would be an eligible activity for sub-loans under the micro-finance outreach component, for example, if herders chose to borrow for this purpose; and herder self-help groups may wish to support the restocking of poorer member households from their own revolving funds, although restocking would not be an eligible activity for their initial matching loans. The LIF would also be an important potential source of financing for community-driven investments in agriculture- and livestock-related infrastructure, such as the rehabilitation of irrigation systems to support fodder and vegetable production by poorer households wishing to leave the livestock sector.

2. Major related projects financed by the Bank and/or other development agencies (completed, ongoing and planned). See Map 3 for a comparison of the geographical coverage of related donor-supported projects in agriculture and rural development, and Annex 12 for a description of related donor-supported activities and their complementarities with the proposed project.

Sector Issue	Project	Latest Supervision (PSR) Ratings (Bank-financed projects only)	
		Implementation Progress (IP)	Development Objective (DO)
Bank-financed			
Poverty Reduction	Poverty Alleviation for Vulnerable Groups Credit (completed)	S	S
Urban Development	Ulaanbaatar Services Improvement Project	S	S
Financial Sector	Financial Sector Adjustment Credit	S	S
	Banking, Enterprise & Legal TA Credit	S	S
	Fiscal TA Project	U	U
Transport	Transport Development Project	S	S
Other development agencies			
Poverty Reduction	Arkhangai and Khuvsgul Rural Poverty Alleviation Projects and extensions in Bulgan and Khentii aimags (IFAD)		
	Poverty Research and Employment Facilitation for Policy Development (UNDP/ SIDA)		
Micro-finance	Rural Finance Project (ADB)		
	Enterprise Development Innovation Fund (DFID)		
	Credit-Mongol (EU-TACIS)		
Regional/ Private Sector Development	Gobi Regional Economic Growth Initiative (USAID)		
Agriculture	Agriculture Sector Development Program (ADB)		
Pastoral Risk Management	Pastoral Risk Management TCP Project (FAO)		
	Developing and Piloting a Sustainable Development Model for the Extensive Livestock Industry (UNDP/CPR)		
Governance/ Decentralization	Human Rights, Local Development and Democracy at		

	the Bag Level in Mongolia Project (UNESCO/DANIDA)		
Social Protection	Social Security Sector Development Program (ADB)		
Rural Development	Rural Development Program (planned) (EU-TACIS)		

IP/DO Ratings: HS (Highly Satisfactory), S (Satisfactory), U (Unsatisfactory), HU (Highly Unsatisfactory)

3. Lessons learned and reflected in the project design:

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 operation and maintenance (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 short-lived 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 source of 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 O&M 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 aspects 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 institution 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) the Vulnerable Group Organization (VGO) scheme, which operated under LDF; (b) the Income Generation Fund (IGF); and (c) the Women's Development Fund (WDF). Loan repayments from the 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. 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-lived to have a significant or lasting 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.

4. Indications of borrower commitment and ownership:

GoM's Action Plan 2000-2004 puts poverty reduction high on the agenda. Its I-PRSP - recently approved by the Boards of the World Bank and IMF, including GoM's endorsement of international poverty targets and a road-map for completion of the full PRSP - shows clear evidence that Government is committed to implementing a comprehensive Poverty Reduction Strategy. Cabinet endorsement of Resolution 108 of March 2001, which established the National Household Livelihood Capacity Support Program, bears testimony to GoM's convictions concerning a livelihoods-based approach to poverty reduction. Resolution 47 (2001) demonstrates GoM's strong commitment to improving pastoral risk management. GoM's draft Regional Development Policy gives strong indication of its concern to reduce regional and rural/urban disparities. Government's Letter of Development Program (see Annex 11) articulates its long-term vision in these and other areas relevant to the proposed program.

GoM has also demonstrated strong and tangible commitment to the proposed program through its hosting of and active participation in four national-level stakeholder consultation workshops on program and project identification and design. The Economic Advisor to the Prime Minister has been appointed as the Director of the HLSPO, underscoring the importance attached to the proposed program at the highest levels of Government. During the bridging period between the end of NPAP in December 2000 and the anticipated launch of the proposed project in mid-2002, GoM has absorbed the recurrent costs of the institutional set-up created under NPAP including fixed-term staff costs, and operating costs of HLSPO and the local-level network of HLSC secretaries. GoM's allocation of US$0.8 million for continuation of LDF in 2002 is evidence of its commitment to continue to support the bottom-up approaches to local and community level infrastructure launched under NPAP.

Beneficiary commitment and ownership is demonstrated by the findings of participatory evaluations undertaken in 17 *aimags*, 9 *duuregs*, 51 *sums*, and 20 *khoroos* with a total of 2,340 participants, during the preparation of the intensive learning ICR for the PAVGP.

5. Value added of Bank support in this project:

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 Natural Resource Management 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.

E. Summary Project Analysis (Detailed assessments are in the project file, see Annex 8)

1. Economic (see Annex 4):

○ Cost benefit NPV=US$ million; ERR = % (see Annex 4)

○ Cost effectiveness

● Other (specify)

As most of the benefits are not directly quantifiable, the conventional cost-benefit analysis approach is not applicable. However, alternative approaches and illustrative analysis for each component have been used and results are presented in the following paragraphs.

Pastoral Risk Management

The benefits of pastoral risk management are reduction in *dzud*-related animal losses, which include both direct economic costs due to animal deaths and the wider economic and social costs such as reductions in cashmere and milk production resulting from animal deaths; the cost of government relief activities; disruption of schooling and other social services; and environmental costs such as tree-felling caused by lack of animal dung for *ger* stoves. The direct benefits of reduction of animal losses were estimated by considering the value of combined losses during the 1999/2000 and the 2000/2001 *dzud* in comparison with normal years. The analysis (see Annex 4) suggests that, on average, adoption of a nationwide pastoral risk management strategy (estimated at US$10 million every four years if modelled on the Phase I proposal) could cut national livestock losses in *dzud* years (such those in 1999/2000 and 2000/2001) to those of normal years, and Mongolia would save an average of over US$100 million per year in *dzud* years. If we assume that *dzud* occurs one year in every five, the pastoral risk management component would easily pay for the whole project. If adoption of pastoral risk management strategies were to reduce losses in *dzud* years by an average of 50%, Mongolia would save US$50 million per year during *dzud* years. If *dzud* were to occur only once in 10 years, the savings would still cover entire the cost of the pastoral risk management component (nationwide cost for ten years would be around US$22 million).

Indicative business models for hay and fodder enterprises to be supported under the PRM component are presented in Annex 4, and suggest that these enterprises would be economically viable.

Micro-finance outreach

A substantial share of the costs of the MFO component would be for capacity building, for which the benefits are difficult to quantify. As for the finance under MDF line of credit, most would be used for short-term and working capital finance. It is expected that most of the loans would be for a maximum of

one year and that activities complete several cycles within this time period. The conventional NPV/IRR calculation, developed for capital budgeting of multi-year investments, is not applicable to most micro-finance activities envisaged under the project. Furthermore, cost and benefit cash flows could not be totally accounted for and the costing of resources employed is often difficult. During the project implementation, an impact assessment will be done to provide an analysis of the economic impact of the MFO component. The impact assessment will include measurement of impacts on households income and employment. The survey will collect time-series data allowing an analysis of economic impacts over time. Nevertheless, for the multi-year investment finance which would be eligible for micro-finance under the project, a few representative models have been developed based on the data available (Annex 4).

Local Initiatives Fund

Due to the demand-driven nature of this component it is not possible accurately to pre-determine the sub-projects that would be funded by the LIF or the LDF. The precise composition of infrastructure sub-projects cannot be defined ex-ante. Furthermore, given the low degree of market development in rural Mongolia, the benefits either do not have a readily accessible market price or are not easily measurable, and it would therefore prove difficult to convert these benefits into monetary terms. Given the inter-linkages among the three major components of the project, some benefits from the activities of the LIF component will be reflected in the form of better pastoral risk management and more prosperous private productive activities financed by MFIs. Against this background, an overall, ex-ante cost-benefit analysis for this component would be considered too speculative. It is also unrealistic to expect that approval of each sub-project proposal be subject to an economic analysis, given the large number and diversity of sub-projects that the component would finance. However, an illustrative cost-benefit analysis, based on a range of representative community investment activities, will be developed during the first year of the project and will used in the later three years of the project as an additional input for sub-project appraisal.

In addition, to ensure that investments for infrastructure remain within economically reasonable margins, cost ceilings will be set for selected infrastructure sub-projects, such as per student investment for school dormitory heating system rehabilitation. The cost ceilings proposed under the component would ensure that even without an economic analysis the investment would generally be economically viable. This framework for cost-benefit analysis will be applied to a sample of sub-projects, focusing on those which are larger in scale and are expected to have more direct economic impacts, in order to refine the selection criteria and the cost ceilings.

2. Financial (see Annex 4 and Annex 5):
NPV=US$ million; FRR = % (see Annex 4)

Models developed for representative activities under the PRM and MFO components indicate that these activities are financially viable, implying that private sector entrepreneurs and companies are likely to be interested in taking up these activities. Credit under the micro-finance component would be in line with CGAP principles of financial sustainability. Under the LIF, mechanisms for financial control, transparency and accountability have been defined and have been incorporated in the LIF PIM. The community scorecards will also enable beneficiaries to report cases of suspected financial mismanagement to the relevant authorities.

Fiscal Impact:

In short run, the fiscal impact of the proposed project would be neutral given that only around 10% of the total project cost would be financed by Government. In the long run, it is expected that the fiscal impact of the proposed project would be highly positive owing to the increased tax base with the rise in active

economic activity and the savings of public expenditure on *dzud* disaster relief efforts as a result of improved pastoral risk management.

The project's recurrent cost implications for the GoM central budget would be limited. Under the pastoral risk management component, the O&M cost for wells would be borne by the water-user groups. This represents cost savings for GoM insofar as well O&M prior to the economic transition was borne by central government. The O&M costs of pilot commercial hay and fodder making would be borne by the participating enterprises. The *aimag*-level emergency revolving fodder funds would sell fodder to recover the cost of their operations. The only pastoral risk management activities involving incremental recurrent costs for the central budget would be emergency forecasting, preparation of *sum*-level contingency plans, post-rehabilitation maintenance of existing inter-*aimag otor* reserves, and environmental monitoring. Insofar as the pastoral risk management component is expected to reduce *dzud*-related disasters, it would reduce the need for GoM to spend money on emergency relief.

In the case of LIF component, local authorities would cover incremental O&M of the small-scale infrastructure investment. In many cases, these are expected to be small as the majority of small civil works involve rehabilitation rather than new construction and the sub-projects will often involve improvements resulting in cost savings in operating costs (repair of school dormitory heating systems is one such case). Thus, LIF infrastructure investments are not expected to place an additional burden on public expenditure. Nevertheless, a clear commitment and O&M plan with estimated labor requirements and responsibilities by the beneficiaries would be a condition for financing of sub-project proposals.

Recurrent costs under the micro-finance outreach component would be self-financed as the Micro-Finance Development Fund is expected to become at least financially self-sustaining.

3. Technical:

Pastoral Risk Management

Pastoral risk management is a relatively new technical field in which there have been very few World Bank or other donor-financed investment projects to date (with the notable exception of the Bank-supported Kenya Arid Lands Resource Management Project). Nonetheless, the proposed pastoral risk management strategies build on a strong foundation of pilots implemented under the FAO Pastoral Risk Management TCP Project in Uvs and Tov *aimags* in 2001. The proposed risk management strategies also build on substantial analytical work done in Mongolia in connection with project preparation (e.g. concerning the proposed index-based approach to livestock insurance) and on inter-country exchanges of experiences with pastoral risk management between Mongolia, China and Kyrgyzstan sponsored by FAO. The efficacy of classifying emergency forecasts by warning stages ('normal', 'alert', 'alarm', 'emergency' and 'recovering') has been demonstrated in drought-prone areas of Kenya.

The proposed herder self-help initiatives build on the experience of the UNDP-financed, Center for Policy Research (CPR)-executed pilot project, 'Developing and Piloting a Sustainable Development Model for the Extensive Livestock Industry'. This NGO-implemented pilot project was implemented in three *sum*s of Tov, Ovorkhangai and Bayankhongor *aimags,* and demonstrated the technical viability and social and economic benefits of herder cooperation in labor-pooling, pasture management, milk marketing, and in guarding winter grazing areas against encroachment. The feasibility of registering herder organizations as NGOs and of opening joint bank accounts in the group's name was also demonstrated. The project also established a sound basis for land-use mapping by herder groups. The feasibility of using existing land law to underwrite security of pasture tenure for herders groups was also tested and proven to be workable. Herder-group managed revolving loan funds for emergency fodder purchases and breed upgrading were pilot tested by the

CPR project and the ACDI/VOCA Farmer-to-Farmer project. The feasibility of community-based well rehabilitation and management has been demonstrated internationally to be best practice.

Micro-Finance Outreach

The technical basis for micro-finance outreach is well known, but the proposed approach is new in Mongolia and implies an initial effort to establish the management structures and the operational procedures for an efficient operation of the wholesale facility. However, this approach provides several advantages: (i) it ensures a shorter start-up period and greater possibilities of disbursements of sub-loans to project beneficiaries earlier in the project implementation period; (ii) it provides equal opportunities to all potential MFIs to meet the accreditation criteria to retail project funds; (iii) there is no conflict of interest with the apex institution (BoM), since it is not a retailer of funds in the market; and (iv) it offers the possibility of transferring the Fund and its management unit outside the BoM, and transforming it into a micro-finance apex organization in the private sector, during future phases of the program. The proposed index-based livestock insurance scheme is new, but there is growing international experience with weather-based insurance in dryland agriculture (e.g. in Morocco and Nicaragua).

Local Initiatives Fund

The technical basis for LIF in Mongolia is particularly sound. GoM demonstrated its capacity to implement LDF efficiently nation-wide in all *sums* and *khoroos* under NPAP. The technical basis for the innovations to be introduced under LIF have also been proven in-country. The experience of the UNESCO/DANIDA Human Rights, Local Development and Democracy at the *Bag* Level in Mongolia Project 1997-1999, which covered 36 *bags* in 6 *aimags* (Tov, Dundgov', Sukhbaatar, Khovsgol, Khovd and Övörkhangai) demonstrated that – with appropriate capacity building – *bag* communities are capable of identifying, planning, implementing and maintaining small *bag*-level infrastructure projects. Sustainability and replicability were achieved in the communities in which projects were implemented. Concrete projects undertaken by micro-project teams at *bag* level encouraged other *bags* to use the project methodology and access resources for their communities from various sources. Proposals for capacity building at *sum* level and below are based on the experience of the World Vision Area Development Program in Bulgan *aimag*. The feasibility of direct transfer of funds to the *sum* level was demonstrated by the GoM *Sum* Development Fund, established in 1996 as a relief fund to mitigate the effects of the collapsed public services and trading networks. MoFE nationwide provided 5 million MNT to each *sum* as an interest-free loan to be repaid. The experience and success of the SDF has been variable. Lessons learned were that *sums* are capable of handling funds but they need appropriate training, accompanied by manuals, and that the *aimags* need to be fully informed about the program and must be responsible for close financial monitoring.

4. Institutional:

4.1 Executing agencies:

Project activities will be executed by sub-national and local governments, and community groups, in some cases with assistance from civil society institutions, depending on the particular component and activities in question. Within sub-national and local governments, the membership and scope of activities of the HLSCs (building on the former PACs that executed activities under NPAP) will be expanded at *aimag* and (particularly) *sum* levels, and would work in an executing or facilitatory role, depending on the activities in question. The detailed project description in Annex 2 and summary of institutional capacity-building measures in Annex 13 provide further details.

4.2 Project management:

The Household Livelihoods Support Program Office (HLSPO) will be responsible for overall project management at national level. HLSPO reports directly to the National Committee on the Household Livelihoods Capacity Support Program, a committee chaired by the Prime Minister for the purpose of overseeing anti-poverty operational programs including the proposed Sustainable Livelihoods Project/Program. Coordinators for each of the three main project/ program components will be advised by technical Working Groups made up of senior staff of the relevant Government ministries, agencies, and representatives of private sector and civil society institutions as appropriate. Appointment of the three component coordinators under terms of reference acceptable to IDA is one of the conditions for Credit effectiveness.

4.3 Procurement issues:

Due to the scattered locations and staggered implementation schedules of the three components of the project, each participating *aimag* and *sum* would undertake its own procurement for small civil works and community contracting. The HLSPO, based in Ulaanbaatar, would take responsibility for:

(a) managing procurement of works under NCB (for the rehabilitation of two irrigation schemes);
(b) managing the procurement of goods (vehicles, agricultural and weather forecasting equipment) through international shopping and small-value goods through local shopping;
(c) contracting and managing all consulting services required under the project;
(d) guiding and supervising procurement work handled at *aimag/sum* level for small civil works and community contracting;
(e) organizing training in procurement procedures for *aimag/sum* HLSC members;
(f) coordinating procurement planning and reporting; and
(g) providing other support to *aimags* and *sums* when needed.

All procurement documents subject to IDA's prior review will be sent to IDA through the HLSPO. Due to the decentralized procurement arrangements, vehicles, agricultural and weather-forecasting equipment will most likely be the only goods packaged together for bidding. Procurement plans will developed on an annual basis, given the phased approach of the program.

A detailed procurement capacity assessment was undertaken during the pre-appraisal mission in November 2001 and updated at appraisal in March 2002, and the Procurement Capacity Assessment Report is held on file. A detailed procurement plan for the first year of the project was also reviewed and found to be satisfactory; this is also held on file. The assessment concluded that a general level of procurement capacity exists in the participating *aimags, sums*, and HLSPO. However, it was determined that additional strengthening would be required. A time-bound action plan was proposed to address the weaknesses identified. The proper implementation of the action plan would minimize the potential risks. Additional details regarding procurement arrangements are provided in Annex 6.

4.4 Financial management issues:

The HLSPO will be responsible for overall project financial management including planning and budgeting, preparing consolidated financial statements, Financial Monitoring Reports, progress reports, and ensuring the smooth flow of funds to the respective project activities. The HLSPO will manage the project's Special Account and ensure its timely replenishments, including preparation of statements of expenditures (SOEs) and replenishment/reimbursement claims (in addition of maintaining the local currency account for the counterpart funds) . It will monitor and train *aimag*- and *sum*-level financial management staff in project accounting procedures and financial operations.

The HLSPO is organized in two main divisions: (1) the Program Implementation Coordination Division; and (2) the Finance, Auditing, and Evaluation Division. The minimum agreed number of staff will be 16 persons, adding an additional eight to the existing eight, including three additional staff in the Finance, Auditing, and Evaluation Division. Based on the activities envisaged under the various components, this proposed level of staffing was deemed appropriate for project implementation. Appointment of the three additional staff in the Finance, Auditing, and Evaluation Division, under terms of reference acceptable to IDA, is one of the conditions of Credit effectiveness.

Based on a financial management capacity assessment undertaken during the pre-appraisal mission in November 2001 and updated at appraisal in March 2002, the need to strengthen controls and procedures was identified so as to meet minimum Bank financial management requirements. In addition, it was also recommended that oversight and audit functions be further developed at all levels. The full Financial Management Capacity Assessment is kept in the project files, and a summary, including the time-bound action plan, is attached to Annex 6.

HLSPO will establish a financial management and accounting system to control the flow of funds at each level of project implementation. All necessary reporting and monitoring features will be built into the system to track the use of Credit proceeds implemented in the form of sub-projects by communities at *aimag* and *sum* levels and below. Such procedures will be documented in the Project Financial Management Manual.

5. Environmental: Environmental Category: B (Partial Assessment)

5.1 Summarize the steps undertaken for environmental assessment and EMP preparation (including consultation and disclosure) and the significant issues and their treatment emerging from this analysis.

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 (EA) was carried out over three stages by an independent team of specialists. First the EA carried out a 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 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*: Dundgov', Omnogov', 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, HLSPO 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 and publicly disclosed in December 2001, both in the country and at the InfoShop.

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 community-driven development 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-based 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.

5.2 What are the main features of the EMP and are they adequate?

The EA sets out an environmental management plan (EMP), with an associated environmental management system. The design of the EMP will ensure that environmental sustainability is not considered in isolation from social, economic and institutional sustainability in the wider rural space. The EMP puts strong emphasis on the formulation of *sum*-level pastoral risk management plans within the context of overall land use planning and the establishment of herder organizations and well-user groups as a means of ensuring positive environmental outcomes. It outlines the training of MoNE and MoFA staff in pastoral risk management and sustainable pasture management, and provides templates for the monitoring and reporting of possible localized negative impacts of certain activities. It also details the pre-screening of projects to be financed under the LIF and documentation of environmental impacts of micro-credit under the micro-finance outreach component.

5.3 For Category A and B projects, timeline and status of EA:
Date of receipt of final draft: December 19, 2001

An environmental screening and scoping of the pastoral risk management component was carried out in Mongolia in July-August 2001. This was followed by a five-person, dedicated EA carried out from September 3-23, 2001. A draft EA report was submitted for comment on October 9, 2001. A separate Social Assessment (SA) report was submitted for comment on November 12, 2001, based on extensive fieldwork during October 2001. The finalized versions of the EA and SA reports were submitted as a consolidated, two-volume document on December 19, 2001, and publicly disclosed in December 2001 in Mongolia and in the InfoShop.

5.4 How have stakeholders been consulted at the stage of (a) environmental screening and (b) draft EA report on the environmental impacts and proposed environment management plan? Describe mechanisms of consultation that were used and which groups were consulted?

During the initial environmental screening and scoping of the PRM component and again during the dedicated EA, consultative meetings were held with concerned government ministries (MoNE, MoFA, MoFE), international organizations, universities and research institutes, environmental NGOs, local authorities including Poverty Alleviation Councils, and environmental inspectors at *aimag* and *sum* level as well as NPAP beneficiaries and herders.

During the preparation of the EA itself, there was an intensive schedule of interviews with key stakeholders and informants, as well as joint meetings/workshops with groups of stakeholders. A typical agenda of a meeting included an introduction of participants, a brief overview of the project, views and comments of the consultees, and specific questions from the EA team regarding the details of environmental and social sensitivities, people's interaction with the environment, and potential impacts of the project. Interview and workshop techniques included time budgets and ranking exercises. Some stakeholders were interviewed on two or three occasions, in order to discuss conclusions in detail.

Key stakeholders consulted on the project included: national government agencies; local government (*aimag* and *sum* levels); herders in rural and peri-*sum* and peri-*aimag* areas; environmental/social NGOs; research institutes; private sector; and international development agencies.

5.5 What mechanisms have been established to monitor and evaluate the impact of the project on the environment? Do the indicators reflect the objectives and results of the EMP?

Provision has been made for: (a) ongoing environmental monitoring by existing environmental inspectors at *sum* level under the technical guidance and supervision of the environmental inspectors at *aimag* level; and (b) studies to document environmental effects and impacts to feed into the mid-term review and ICR. The environmental inspectors will have a role in project decision-making through their membership in the *sum* and *aimag* level HLSCs. The annual environment and social reporting by the *sum, aimag* and national SLP staffs will reflect progress of the EMP and the meeting of overall project objectives.

6. Social:

6.1 Summarize key social issues relevant to the project objectives, and specify the project's social development outcomes.

Planned social development outcomes. As a result of the project, it is expected that: (a) poor but otherwise viable herding households continue to be able to pursue livestock-based livelihoods in a sustainable manner, with secure access to adequate grazing; (b) non-livestock-related livelihood diversification in rural areas or in smaller urban settlements in *sum* or *aimag* centers would be made possible for other targeted poor households, including women-headed and single-male headed households; (c) both of these categories of households would be able to cope with and respond to a wide range of idiosyncratic and covariant risks without having to dispose of assets at low prices or borrow from moneylenders at high rates of interest; and finally, (d) inclusive and accountable mechanisms would be established through which communities would play a key role in prioritizing, selecting, co-financing, implementing and maintaining investments in small-scale infrastructure.

Anticipated social impacts. The social assessment concluded that overall social impacts are expected to be positive, with few or no adverse social costs anticipated. Drought, *dzud*, land degradation, and increased vulnerability of herders are leading to significant reductions in living standards among poor and middle-poor herder households, and the Mongolian rural economy and society centers around extensive

herding. Lower living standards in rural Mongolia are associated with rising malnutrition, increased incidence of disease, and lower school attendance. As herders lose their livestock, they are increasingly attracted to *sum* and *aimag* centers, in order to reduce their insecurity, resulting in concentrations of livestock around these centers and further decline in livestock productivity and survival rates. Herders that have lost all of their livestock are vulnerable to social breakdown in *sum* and *aimag* centers, resulting in malnutrition, depression, increased incidence of drunkenness among men, divorce, and increased incidence of domestic violence. The proposed project, through the combined actions of the pastoral risk management, LIF, and micro-finance outreach components, has the potential to deliver an overall positive social impact, by empowering herders to manage their livelihoods, and by contributing to rising living standards among poor households and herder households.

For many of the same reasons, it is anticipated that the project would have a positive impact on *gender relations*. Some of the key gender issues in contemporary Mongolia are: a much higher level of female participation in tertiary education by comparison with male participation, in part reflecting higher rates of male drop-outs from primary and secondary schools, which translates into higher and increasingly female levels of skilled workforce participation in Ulaanbaatar, particularly in the service sectors; high levels of domestic violence among poorer groups in *aimag* and *sum* centers, associated with male unemployment, depression, and alcohol abuse; high and growing levels of divorce and marital breakdown as a result of both of these trends; particular forms of vulnerability among single male- as well as single female-headed households; and relatively higher representation of women among clients of micro-credit services. To the extent that the project would support livelihood security and sustainability both within and outside the livestock sector, it may be expected to enhance opportunities for male as well as female livelihood diversification, thereby helping to reduce male drop-outs from schools both by increasing demand for skilled male labor and by reducing the need to withdraw boys from school owing to improvements in livestock productivity.

6.2 Participatory Approach: How are key stakeholders participating in the project?

Project identification and preparation has been guided by a participatory, project-cycle management approach. Four participatory, stakeholder consultation workshops have been held in connection with program and project identification and preparation to allow a wide range of stakeholder groups to express their views in an open-ended manner through 'problem and objective trees' (December 1999), leading to an initial screening of options for project components and a logical framework-based workshop to design aspects of the pastoral risk management component (April 2000). The Bank-supported Participatory Living Standards Assessment 2000 also generated a good deal of information that guided the content and approach to be taken within each of the project components. Two additional National Stakeholder Consultative Workshops were held from June 12-16, 2001 and July 30-August 12, 2001 with the support of a PHRD grant. The first workshop - the primary aim of which was to develop the logframe for the proposed program project in a participatory manner - involved local and international consultants, component advisory teams (drawn from private sector organizations, NGOs, and research institutes) and relevant implementing agency staff (around 50 people). The second workshop – whose task was to discuss the consultant team proposals and to refine the logframe – was a larger event with over 100 participants including Members of Parliament and representatives of local government in addition to the participants in the first workshop. The EA also involved a stakeholder consultation workshop.

The consultation process for project preparation was closely linked with participatory evaluation of the previous Bank-financed PAVGP under NPAP. To maximize stakeholder input into the design the new project, in connection with the Intensive Learning ICR (ILI) conducted for PAVGP, a comprehensive series of stakeholder workshops were carried out by local PACs in 17 *aimags*, 9 urban districts (*duuregs*), 51

sums, and 20 urban sub-districts (*khoroos*) with 2,340 participants. The workshops used PRA methods to assess the perceived impact of PAVGP on the livelihoods of beneficiaries and to identify strengths and weaknesses of each project component. The *sum*-level stakeholder workshops fed into *aimag*-level stakeholder workshops, attended by representatives of direct beneficiaries, *sum* officials, *aimag* level officials and NGOs. Findings from the 17 *aimags* and 9 *duuregs* were analyzed jointly by GoM and the ILI mission in a two-day participatory analysis session. The overall findings were discussed at three national level stakeholder workshops in order to draw lessons for future operations: the first with members of an 18-person Core Learning Team comprising mission members and representatives of the Borrower (MoFE) and implementing agencies; the second with key informants who played important roles in NPAP design and implementation; and a third with newly-appointed members of the cross-sectoral National Poverty Alleviation Committee. Continuity between the ILI and project preparation was facilitated by ensuring continuity in team membership, both international and local.

Key stakeholder participation in project implementation. Groups at *bag* level would be the catalyst for developing project ideas within the community for co-financing under LIF, and the *bag khural* would provide the forum in which the needs of the *bag* are debated and project ideas discussed. They would facilitate an interactive process of prioritization – assisted by the *sum* HLSCs – and ensure that the interests of the poorer members of the community, of women and single men- and single women-headed households, of elderly people, of new herders, and of other vulnerable groups are heard and reflected in the process. They would work with community groups that are interested in receiving LIF funding for a sub-project and help them develop their ideas into costed proposals. After reviewing sub-project proposals from the community groups, a short-list of priority sub-projects would be chosen and the submitting community groups would be requested to further detail the proposals.

The *bag*-level working groups would also serve as a liaison between herder organizations, hay-making groups, and community-based well-user groups to be organized and strengthened in connection with the pastoral risk management component and the *sum* HLSCs, and act as a clearing house for proposals submitted to the LIF fund by such groups. The HLSCs, with local consultant support, would assist herder groups to organize themselves and to register as NGOs or cooperatives, to open a joint bank account in the name of the group, and to mobilize a local contribution that would entitle them to establish and manage a group-level revolving fund in support of winter preparation, hay-making, veterinary care or emergency fodder purchase. The HLSC would also work closely with the *sum* RLF loan officer and any MFI branches available in the *sum,* assisting poor households wanting income-generation sub-loans to make contact with the RLF or with the branch of the MFIs.

6.3 How does the project involve consultations or collaboration with NGOs or other civil society organizations?

National NGOs such as the Women's Federation, the Youth Federation and the Union of Private Employers would continue to be represented on the National Committee on the Household Livelihoods Capacity Support Program, as they were on NPAC, as well as on the HLSCs at *aimag*/duureg and *sum*/ *khoroo* level. In addition, in pilot *sums* of the eight core *aimags*, HLSC composition would be broadened to include representatives of local MFIs as well as elected representatives of the *sum* and bag *khurals* (assemblies). The pastoral risk management component would assist herder groups to establish themselves as NGOs, cooperatives, or some other appropriate form of civil society organization.

6.4 What institutional arrangements have been provided to ensure the project achieves its social development outcomes?

Beneficiary selection and targeting criteria form an integral part of the Project Implementation Manual (PIM). HLSC members will be trained in participatory approaches. The *sum* HLSCs and will have

responsibility for grassroots capacity building and social development. Women made up the majority of *sum* PAC members under NPAP, and are also expected to dominate the HLSCs; this will facilitate dialogue with women in the communities and will ensure that their priorities will be heard and acted on. An Ethnic Minorities Participation Framework has been developed to promote the social development outcomes of the project in those few areas in which ethnic minorities form a significant proportion of the population.

6.5 How will the project monitor performance in terms of social development outcomes?

Poverty monitoring will rely on the National Statistical Office's newly revamped Household Income and Expenditure Survey (incorporating LSMS modules) and the Poverty Research Unit established under the UNDP/SIDA-financed Poverty Research and Employment Facilitation for Policy Development project. Participatory M&E as an integral aspect of the proposed project will facilitate the feeding back of beneficiary views on social outcomes into management decisions through the MIS. A baseline survey will be conducted by March 31, 2003, and re-surveyed at mid-term review and end of project. Key social development impact indicators will be tracked in the MIS, and participatory methods as used in the PLSA will be incorporated. The option of establishing a 'panel' under the baseline survey will also be explored, giving the option of tracking livelihood dynamics within a specific group of households over the life of the project/program.

7. Safeguard Policies:

7.1 Do any of the following safeguard policies apply to the project?

Policy	Applicability
Environmental Assessment (OP 4.01, BP 4.01, GP 4.01)	● Yes ○ No
Natural Habitats (OP 4.04, BP 4.04, GP 4.04)	● Yes ○ No
Forestry (OP 4.36, GP 4.36)	○ Yes ● No
Pest Management (OP 4.09)	● Yes ○ No
Cultural Property (OPN 11.03)	○ Yes ● No
Indigenous Peoples (OD 4.20)	● Yes ○ No
Involuntary Resettlement (OP/BP 4.12)	● Yes ○ No
Safety of Dams (OP 4.37, BP 4.37)	○ Yes ● No
Projects in International Waters (OP 7.50, BP 7.50, GP 7.50)	○ Yes ● No
Projects in Disputed Areas (OP 7.60, BP 7.60, GP 7.60)*	○ Yes ● No

7.2 Describe provisions made by the project to ensure compliance with applicable safeguard policies.

Environmental Assessment, Natural Habitats and Pest Management. The conduct of the environmental assessment was consistent with OP4.01. A proposal for the project to finance the drilling of new wells was rejected on the grounds that such actions would contravene OP4.04 – that is, the areas to receive new wells would be 'natural habitats' (as defined within the Policy) that might incur 'significant conversion', and that the alternative of rehabilitating broken wells was desirable and practical. Participatory community monitoring of water quality and quantity, and of vegetation changes around these wells will be conducted to inform water supply policy and future interventions. A proposal for the project to support means of controlling vole populations using chemical means was rejected on the grounds that there was inadequate safeguard that the means would be (as required by OP4.09) effective against the target species, have minimal effect on the mammal non-target species with which the vole shares the grasslands, and take into account the need to prevent the development of resistance. The project will, however, support ecologically-benign, community-based measures that will help reduce vole populations such as the enhancement of vole predators and increasing grass height to make the habitat less favorable to the voles. At an earlier stage in project preparation, concern was raised that pesticides might be used on hay fields supported under the project. In fact, pests are rarely an issue in hay-making and productivity of areas

allocated for hay can be increased simply by leaving animal dung deposited after the hay has been harvested and by using snow melt- or channel irrigation, whichever is appropriate. The Project Implementation Plan (PIP) explicitly states that the project will not finance pesticides in support of hay-making. In compliance with OP4.09, a pest management plan has been prepared covering all relevant project activities; this plan is subsumed within the overall Environmental Management Plan.

Indigenous Peoples. There are over 30 different ethnic groups in the country. They are either the descendants of Mongolian nomadic tribes, or groups of Turkic origin who have become Mongolized over time. Khalkh Mongols are the national majority (90%) and also the ethnic majority in six of the eight project *aimags*. Kazakh form the majority (89%) in Bayan-Olgii *aimag*, and Buriad are in the majority in five *sums* of Dornod *aimag*. Uvs is the most ethnically diverse of the project *aimags;* Dorvod and Bayad are the main groups in the province.

Cultural differences among these ethnic groups are relatively minor. Mobile pastoralism has traditionally been practiced within Mongolia and throughout the Inner Asian region. This common nomadic way of life has fostered a relatively uniform culture over extensive areas, with large groups of people sharing similar livelihoods, having frequent contacts with speakers of other dialects, and developing related social and cultural practices over the centuries.

Ethnic distinctions among the Mongol subgroups are relatively minor, although some may have a stronger sense of their own identity than others. While language differences and their Islamic beliefs may make ethnic distinctions appear to be more marked between the Kazakh and the Mongol subgroups, Kazakh livelihoods are not significantly different from those of the Mongol subgroups. Overall, however, language or tribal differences have not become significant political or social issues in Mongolia.

The social assessment undertaken during project preparation concluded that the project will have negligible negative impacts and more significant positive impacts for all poor beneficiaries, including the ethnic minority communities. An Ethnic Minorities Participation Framework has been prepared to help ensure the participation of ethnic minorities in the Project.

Involuntary Resettlement. While no involuntary resettlement or land acquisition is anticipated, a Resettlement Policy Framework was developed during project preparation to protect people who may be negatively impacted as a result of the possible community demand for the construction and or rehabilitation of small-scale infrastructure sub-projects, such as roads, bridges, buildings, structures, water supply and sanitation facilities, and other civil works. Local officials confirmed that since rural Mongolia has a vast amount of land with low density population, land acquisition will either not be necessary or will be extremely rare. Demand for the rehabilitation of small-scale infrastructure sub-projects will only be known during project implementation.

Overall, compliance with the Bank's environmental and social safeguard policies will be addressed by an **integrated environmental and social screening process** which will check for possible negative impacts and for the necessary actions required for sub-projects to be financed under LIF and LDF. Staff will be assigned at the various levels who will provide orientation on the safeguards and on monitoring the screening process and any required action. Details have been provided in the Environmental Management Plan, and are described in the full EA/SA report.

F. Sustainability and Risks

1. 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 as control of parasites that threaten animals' winter survival, could 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 gauge 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.

2. Critical Risks (reflecting the failure of critical assumptions found in the fourth column of Annex 1):

Risk	Risk Rating	Risk Mitigation Measure
From Outputs to Objective		
No dzud: actions to reduce dzud could not be pilot tested; pastoral risk management might lose priority.	M	Pilots planned for all AEZs; dzud probability was a criterion in aimag selection.
Severe dzud in Year 1 or 2: A large-scale dzud could cause severe losses and overwhelm capacity while pastoral risk management strategy is being established.	M	Index-based livestock insurance scheme would help ease the financial losses.
Several continuos dzud years: financial viability of models for emergency fodder reserves, pilot hay-making enterprises, and feed concentrate enterprises would be difficult to test.	N	Since pilot activities will be undertaken in several aimags in different regions and AEZs, there will always be some project sites that are not affected by dzud.
Private insurance companies not willing to accept risk of piloting index-based livestock insurance.	M	Government stop-loss provision envisaged, to be financed under project.
Sector ministries opposed to transferring part of the budgetary resources currently under their control at central level to local government at sum level (i.e. moving from 'tied' funds under LDF to an 'open menu' under LIF).	S	Government expected to maintain current commitment to promoting decentralized fiscal management.
Government may change its current policy of promoting decentralized fiscal management and may not facilitate greater availability of budgetary resources at the disposal of the sums/duuregs for investment in basic infrastructure.	S	Government has expressed its strong commitment to this policy in the context of the I-PRSP and proposed Public Sector Finance and Management Law (see Annex 11).

From Components to Outputs		
Poor synergy between PRM sub-components due to complex design and limited implementation capacity.	M	Full-time PRM coordinator within HLSPO will coordinate activities under the guidance of technical Working Groups at central and aimag levels.
GoM continues to confuse PRM with pastoral livestock development or sustainable pasture management.	M	Staff training on PRM to be provided to MoFA & MoNE.
Limited interest on part of existing MFIs to work with the MDF or to service the rural poor.	N	Demand from potential partner institutions was ascertained during project preparation and appraisal.
The demands involved in making LIF truly community-responsive are too great and the sum and aimag HLSCs are unable to manage the process on the scale envisaged, with the result that there are major delays in sub-project processing and/or the prioritization/selection process is compromised.	M	Considerable effort and resources allocated to training stakeholders at bag, sum and aimag levels in the principles, processes and dynamics of participatory, community-based planning and prioritization. Detailed procedures and criteria have been developed and reproduced in the LIF PIM that will be regularly updated through participatory user feedback. The procedures and processing will be kept as simple as possible.
Mismanagement of the LIF at sum level due to lack of commitment and inability to create an effective implementing capacity.	M	Resources are earmarked under the project to enable the sum HLSC to manage funds and account for expenditure in a professional manner. It will be necessary for the sum governors and khurals to make a commitment to support the HLSC and to make physical and financial resources available to help them do a professional and accountable job. Indications from all sum level officials interviewed were that there is substantial support and enthusiasm for the LIF and for the processes involved in its execution.
Overall Risk Rating	S	A substantial level of risk is appropriate since Phase I aims to pilot institutional innovations in each component that need to act in concert for the overall project development objectives to be realized.

Risk Rating - H (High Risk), S (Substantial Risk), M (Modest Risk), N(Negligible or Low Risk)

In analyzing and determining the critical risks, it is understood that there are risks associated with both the project and the overall program. Moreover, at both of these levels, there will be risks associated with the policy framework, with institutions, and lastly in the creation of assets and their sustainability.

The main risks associated with the PRM component relate to: (a) the timing, frequency and severity of *dzud;* and (b) poor understanding of the PRM concept. The risks faced by the MFO component are: (a) slower than anticipated uptake of on-lending to the intended client groups; (b) lower than anticipated demand from MFIs for the technical assistance services offered under the project; (c) collapse or liquidation of RLFs before they can be strengthened; and (d) possible unwillingness of private insurance companies to pilot index-based livestock insurance. The risks faced by the LIF component include: (a) weak *sum*-level management capacity; (b) possible mismanagement of funds; (c) opposition by sectoral ministries to transfer of resources formerly under their control to local government's discretion; and (d) possible risk that GoM might change its fiscal decentralization policies.

3. Possible Controversial Aspects:

Continued support for the local government-administered micro-credit scheme established under NPAP is less controversial than it appears. Under the micro-finance outreach component, limited and time-bound support would be provided only to the best-performing of the existing RLFs with the aim of removing them from government control and transforming them into independent, autonomous, and sustainable managed micro-finance institutions. The justification for supporting the RLFs is that these are the only micro-finance institutions currently serving the poor in remote rural areas; they were established in part with Bank support and considerable (scarce) local capacity has been built that would be lost if all support were to be withdrawn. Limited, time-bound support for the existing RLFs would be a transitional activity under Phase I only.

G. Main Credit Conditions

1. Effectiveness Conditions

a) The Household Livelihoods Support Program Office (HLSPO) has appointed the following six core staff members under terms of reference acceptable to IDA: a coordinator for each of the three main components of the project (pastoral risk management, micro-finance outreach, and local initiatives fund), a procurement officer, a disbursement officer, and an accountant [DCA, Article VI, Section 6.01(a), and Schedule 4, paragraph 1(b); PAD, Sections E.4.2 and E.4.4, and Annex 6, paragraph 4(a) and attached Financial Management Action Plan].

b) HLSPO's financial reporting system is upgraded to produce Financial Monitoring Reports (FMRs) in a format acceptable to IDA; the financial accounting system, including computer hardware and software, is improved to a standard acceptable to IDA; and HLSPO accountants and participating *aimag*, *duureg* and *sum* HLSC secretaries have been trained in financial management [DCA, Article VI, Sections 6.01(b) and 6.01(c); PAD, Section E.4.4, and Annex 6, Financial Management Action Plan].

c) The Project Implementation Manual (PIM) has been adopted in a form acceptable to IDA, including separate sections dealing with: pastoral risk management, local initiatives fund, local development fund, micro-finance operational manual, revolving loan funds, environmental management plan, resettlement policy framework, ethnic minorities participation framework, financial management and reporting (including format of FMRs as an appendix), procurement (including sample documents as appendices), and monitoring and evaluation; and staff of the HLSPO and of the HLSCs in all *aimags* and *duuregs*, and in the 16 *sums* selected to participate in the project for the first year of activities, have completed a training course satisfactory to IDA on the provisions of the PIM [DCA, Article VI, Sections 6.01(d) and 6.01(e), and Schedule 4, paragraph 3; PAD, Section C.4, Project Implementation Manual, and Annex 2, Project Management component].

2. Other [classify according to covenant types used in the Legal Agreements.]

Disbursement Conditions:

Sub-loans under the Micro-Finance Development Fund (Category 5, for around US$3 million equivalent). No disbursement shall be made from this category until:

a) An adequate management information system (MIS) has been established to enable the Borrower to monitor micro-finance activities and assess micro-credit portfolio quality, acceptable to IDA and consistent with CGAP guidelines [DCA, Schedule 1, paragraph 3(b), and Schedule 4, paragraph 17; PAD, Section C.1 and Annex 2, Sub-components 2.1 and 2.2].

b) The Borrower has established the Micro-Finance Development Fund (MDF) with full legal power to enter into Subsidiary Loan Agreements (SLAs) acceptable to IDA with selected MFIs, the Micro-Finance Development Board (MDB) has been appointed with a composition acceptable to IDA, the Micro-Finance Management Office has been created with staffing acceptable to IDA, and the Micro-Finance Operational Manual has been adopted by the MDB [DCA, Schedule 1, paragraph 3(c), and Schedule 4, paragraphs 3(a)(iii) and 9; PAD, Section C.1 and Annex 2, Sub-component 2.1].

c) A qualified MFI, selected under the provisions of the micro-finance operational manual, has entered into a valid and enforceable SLA with the MDF, acceptable to IDA, to on-lend the proceeds of the Credit to project beneficiaries [DCA, Schedule 1, paragraph 3(c)(ii), and Schedule 4, paragraph 11; PAD, Section C.1 and Annex 2, Sub-component 2.1].

Sub-loans under the Strengthening of Revolving Loan Funds (RLFs) (Category 6, for around US$500,000 equivalent)

d) No disbursements shall be made under this category until a detailed action plan has been prepared and agreed with IDA, including: review of current operations and financial status, selection criteria for RLFs, business plans for their strengthening, institutional responsibilities and on-lending terms and conditions for additional funding under the project, flow and use of funds, and privatization strategy [DCA, Schedule 1, paragraph 3(d), and Schedule 4, paragraph 13; PAD, Section C.1 and Annex 2, Sub-component 2.2].

Insurance claims for the development of an index-based livestock insurance scheme (Category 7, for around US$1 million equivalent)

e) No disbursement will be made in respect of the stop-loss amounts under eligible claims made against any eligible insurance company until IDA has been provided with satisfactory evidence that the Borrower has established an index-based livestock insurance program, the Borrower has executed a stop-loss agreement with an insurance company, the participating insurance company has issued livestock insurance policies to policy-holders, and one of the covered risks has occurred and eligible claims have been filed [DCA, Schedule 1, paragraph 3(e), and Schedule 4, paragraphs 14(b) and 15; PAD, Section C.1 and Annex 2, Sub-component 2.3].

Other Conditions

Project management:

f) The Borrower will maintain, throughout the life of the project, levels of qualified and capable staff acceptable to IDA in the HLSPO, and in HLSCs in all participating *aimags* and *sums* [DCA, Schedule 4, paragraphs 1(b) and 1(d); PAD, Section C.4, Sections E.4.1 and E.4.2, and Annex 2, Component 4].

g) The Borrower will maintain, throughout the life of the project, separate technical working groups at national level with compositions acceptable to IDA to oversee and advise on implementation of the pastoral risk management and local initiatives fund components and ensure consistency with national sectoral policies [DCA, Schedule 4, paragraph 1(c); PAD, Section C.4, Section E.4.2, Annex 2, Component 4, and Annex 13].

h) An MIS acceptable to IDA is operational throughout the life of the project [DCA, Schedule 4, paragraph 17; PAD, Section C.4, Section E.6.5, and Annex 6, Financial Management].

Implementation:

i) A communications and public awareness strategy acceptable to IDA shall be prepared by December 31, 2002 and it shall be implemented thereafter [DCA, Schedule 4, paragraph 7; PAD, Sections C.1 and C.4].

j) A baseline survey shall be conducted, under terms of reference acceptable to IDA, to collect data to support the monitoring of the outcome and impact of project activities, and shall provide the results of such baseline survey to IDA not later than March 31, 2003 [DCA, Schedule 4, paragraph 18(b); PAD, Section E.6.5 and Annex 1].

Financial:

k) A multi-year contract with an independent auditor, selected under procedures acceptable to IDA, will be concluded by December 31, 2002 for the auditing of all project accounts and financial statements [DCA, Article IV, Section 4.01(b), and Schedule 4, paragraph 2; PAD, Section E.4.4, and Annex 6, Financial Management].

l) HLSPO shall submit, by June 30 each year, annual audited project accounts and financial statements for all components, the first of which is due by June 30, 2003 [DCA, Article IV, Section 4.01(b)(ii); PAD, Section E.4.4 and Annex 6, Financial Management].

m) HLSPO shall submit to IDA quarterly FMRs in a format acceptable to IDA, each due within 45 days of the end of the preceding calendar quarter, and the first due within 45 days of the end of the first quarter after Credit effectiveness [DCA, Article IV, Section 4.02; PAD, Section E.4.4 and Annex 6, Financial Management].

Procurement:

n) Procurement plans for each calendar year of the project shall be submitted to IDA for review by June 30 of each preceding year, commencing in 2003; the procurement plan prepared at appraisal for the first year of project implementation shall be updated by December 31, 2002 to cover the whole of calendar year 2003 [DCA, Schedule 4, paragraph 8; PAD, Section E.4.3 and Annex 6, Financial Management attachment].

Environmental and Social:

o) All project activities shall be carried out in accordance with the Environmental Management Plan dated December 20, 2001; the Ethnic Minority Participation Framework dated December 16, 2001, and updated on May 2, 2002; and the Resettlement Policy Framework dated December 20, 2001 [DCA, Schedule 4, paragraphs 3(a)(v), 4, 5, and 6; PAD, Sections E.5.2, E.6.4, and E.7, and Annex 14].

Reporting and Monitoring:

p) An annual work plan and budget for each component, covering the next calendar year, should be submitted to IDA for review by June 30 each year; the annual work plan and budget prepared for calendar 2003 shall be updated by December 31, 2002 [DCA, Schedule 4, paragraph 8; PAD, Section C.4].

q) HLSPO shall submit for IDA review, on or about January 31 and July 31 of each year, beginning in January 31, 2003, semi-annual progress reports of works and activities carried out following the format agreed in the adopted PIM, every second such report to incorporate the respective FMR for the preceding calendar quarter [DCA, Schedule 4, paragraph 19; PAD, Section C.4 and Annex 1].

r) The outcome and impact of the project will be monitored using selected performance indicators, agreed with IDA, as presented in the adopted PIM. HLSPO will submit for IDA review, on or about July 31 each year, starting on July 31, 2003, an annual monitoring report on progress towards meeting the project development objective. A comprehensive project impact evaluation report would be prepared and provided to IDA on or about July 31, 2004 as an input to the mid-term review (MTR). Agreement shall be reached between the Borrower and the Bank at MTR on an action plan detailing any required changes in program design or implementation arrangements [DCA, Schedule 4, paragraph 19; PAD, Section C.4 and Annex 1].

s) In accordance with OP13.55 the Borrower will prepare a project completion report not later than six months prior to Credit closing and provide assistance to IDA for the preparation of an Implementation Completion Report [DCA, Article III, Section 3.03; PAD, Section C.4 and Annex 1].

Micro-Finance Development Fund (MDF):

t) Proceeds accrued from the repayment of loans to MFIs (principal, interest and fees) would be used to establish and maintain the MDF as a revolving fund for on-lending for the same purposes and under the same terms and conditions as those for under the original IDA credit, and as specified in the Operational Manual. [DCA, Schedule 4, paragraphs 10(a) and 10(b); PAD, Section C.1 and Annex 2, Sub-component 2.1].

u) By no later than March 31 and September 30 of each year, commencing on March 31, 2003, or such other interval as the Borrower and IDA may agree, the Borrower would exchange views with IDA on the level of interest rates charged on Subsidiary Loans to MFIs, and on sub-loans to final sub-borrowers, to determine if such rates are positive in real terms and above the weighted average deposit rates prevailing in the market at the time of the review and, with the prior concurrence of IDA, revise such rates, if required [DCA, Schedule 4, paragraph 11(d); PAD, Section C.1 and Annex 2, Sub-component 2.1].

(v) No later than June 30, 2004, the Borrower shall carry out a comprehensive assessment of the performance of the MDF, under terms of reference satisfactory to IDA, to provide options for the future development of micro-finance in Mongolia and viable alternatives for the management and operation of the MDF [DCA, Schedule 4, paragraph 9(c); and PAD, Annex 2, Sub-component 2.1].

w) No later than June 30, 2004, the Borrower shall provide to IDA the action plan mentioned in Section G, paragraph (d) above, for the use of the credit proceeds to strengthen selected RLFs with a view to their privatization, and thereafter implement such action plan giving due consideration to IDA's views [DCA, Schedule 4, paragraph 13].

H. Readiness for Implementation

☐ 1. a) The engineering design documents for the first year's activities are complete and ready for the start of project implementation.
☒ 1. b) Not applicable.

☒ 2. The procurement documents for the first year's activities are complete and ready for the start of project implementation.
☒ 3. The Project Implementation Plan has been appraised and found to be realistic and of satisfactory quality.
☐ 4. The following items are lacking and are discussed under loan conditions (Section G):

I. Compliance with Bank Policies

☒ 1. This project complies with all applicable Bank policies.
☐ 2. The following exceptions to Bank policies are recommended for approval. The project complies with all other applicable Bank policies.

Robin Mearns **Team Leader**	Mark D. Wilson **Sector Director**	Ian C. Porter **Country Director**

Annex 1: Project Design Summary

MONGOLIA: Sustainable Livelihoods Project

Hierarchy of Objectives	Key Performance Indicators	Data Collection Strategy	Critical Assumptions
Sector-related CAS Goal: Equitable development & poverty alleviation: Vulnerability reduced and sustainable livelihoods achieved by targeted poor. Targeted poor defined as able-bodied poor and near-poor households vulnerable to impoverishment in rural and peri-urban areas.	**Sector Indicators:** Goal Impact: (end of 12-year program (EOP)) 1.Poverty incidence reduced from 35% to 13% by EOP. 2.Percentage of target beneficiaries able to withstand external shocks increased by 100% by EOP. 3.*Dzud* related animal deaths decreased by half by EOP and HHs losing all animals reduced by 60% 4.Percentage of herder HHs owning durable goods (as specified in NSO Statistical Yearbook, table 10.17 - motorbike, tractor, TV, car, electric generators) increased from 15% to 25% by EOP. 5. 78% school-aged children graduated at least from non-full secondary school by EOP. 6.Infant mortality reduced from 32% to 29% by EOP.	**Sector/ country reports:** NSO Household Income and Expenditure Survey (HIES) with LSMS modules Project PM&E system MoFA's Information, M&E Dept MoFA NSO MoSTEC MoH	**(from Goal to Bank Mission)** HIES conducted to coincide with EOP
Program Purpose: Targeted poor implement improved sustainable livelihood strategies that reduce vulnerability and create and maintain human, social, physical, institutional, financial assets	**End-of-Program Indicators:** **Phase III** Nation-wide, the targeted poor are *using* improved and effective *sustainable livelihood strategies* to improve long term outcomes at HH and community levels: e.g. 1. Targeted beneficiaries build and maintain assets: ▪Human assets: keep children in school, seek training, information; use health services; ▪Social assets: form associations and participate in decision making; ▪Physical assets: invest in new equipment & technologies, achieve viable herds, diversify crops and income generating assets; improve and maintain basic local infrastructure; ▪Natural assets: manage pastures and other renewable natural resources in a sustainable manner; ▪Financial assets: invest, save, establish new businesses; 2. Implement mechanisms and *strategies that reduce vulnerability/risks* due to shocks: ▪% of herder HHs in pilot *sums* adopting at least 3 improved PRM strategies (using emergency forecasts as a basis for rapid response; joining herder organizations; preparing hay and winter fodder; improving winter shelters; controlling animal parasites); ▪At least 8,000 HHs in MF pilot *sums* using micro-finance facilities by EOP (ex-RLFs + MOF partners);	**Program reports:** Intensive Learning ICR with end-of-Program stakeholder workshops to evaluate Phase impact. Advisory group, component working groups, project staff at all levels, Bank and other donor staff, and beneficiary representatives to participate. Independently commissioned impact evaluation.	**(from Purpose to Goal)** Pastoral risk management systems operate independently of state intervention. Other government programs in health, education, and social protection are implemented as projected.

	3. Supporting public & private sector strategies implemented (policies adopted; programs, systems, services and fiscal decentralization institutionalized in public structures and systems on a sustainable basis by EOP).		
	Phase II Phase I programme *scaled-up nation-wide*, public supporting institutions being gradually institutionalized & targeted poor using improved and effective sustainable livelihood strategies to improve long term outcomes at HH and community levels. ▪winter preparation and improved pasture management adopted by 50% of direct beneficiaries among herder HHs; ▪20% of target group have access to microfinance services; ▪access to functioning basic education and rural health facilities increased by 20%.	Intensive Learning ICR with end-of-Phase stakeholder workshops to evaluate Phase impact and assess performance against triggers for advancing to next Phase. Advisory group, component working groups, project staff at all levels, Bank and other donor staff, and beneficiary representatives to participate; results of independent evaluation as input.	Harmonization of approaches of donor programs overlapping in the same *aimags* is feasible
	Phase I Effective approach to promoting improved and sustainable livelihood strategies developed, demonstrated and validated in pilot *sums* of core *aimags* + 1 duureg and ready for scaling up in Phase II; project capacity for implementing the approach developed in core *aimags* and existing capacity maintained outside core *aimags*.	As for Phase II	*Dzud* occurs at least once in project *aimags* to permit PRM piloting

Hierarchy of Objectives	Key Performance Indicators	Data Collection Strategy	Critical Assumptions
Project Development Objective:	**Outcome / Impact Indicators:**	**Project reports:**	**(from Objective to Purpose)**
Effective approach to promoting improved and sustainable livelihood strategies developed, demonstrated and validated and capacity created so that these strategies can be replicated and scaled up in Phase II of the Program.	<u>Project Outcomes</u>: (end of Phase I) **1.1 Improved PRM strategies adopted in 143 *sums* of 8 core *aimags:*** ▪proportion of HHs making adequate winter preparations increased by 33% in project areas by comparison with start of project and/or non-project areas representing similar ecological zones ▪*dzud*-related animal losses reduced by 33% by comparison with start of project and/or non-project areas representing similar ecological zones ▪at least 50% of pasture land under improved management in project areas by comparison with start of project ▪discernible, positive impact on range-vegetation condition by comparison with start of project and/or non-project areas representing similar ecological zones and precipitation conditions, and as measured by NDVI (data obtained from NOAA satellite imagery) or similar indicator;	Intensive Learning Implementation Completion Report (ICR) Project Evaluation Report Mid-Term Review (MTR) (Each to involve: project staff at all levels, beneficiaries, advisory group, component working groups, Bank staff and other donors, and civil society institutions) Annual performance monitoring reports	A large-scale *dzud* does not overwhelm institutional capacity to cope while pastoral risk management strategy is being established.
	1.2 Microfinance services available and used by poor households to build assets and smooth consumption on a financially & institutionally sustainable basis in selected *aimags*: ▪10% of target beneficiaries in selected *aimags* use financial services ▪quantitatively and qualitatively measurable improvement in livelihood security of target beneficiaries (precise indicators to be selected in design of baseline survey) ▪less than 10% of total loan portfolio of selected RLFs past due ▪selected RLFs achieve 50% operational self-sufficiency ▪ 50% of selected RLFs receiving additional funding privatized ▪index-based livestock insurance scheme developed and operational;		Stable domestic economic, political, and social environment with growth rate of >3% p.a. and inflation <10% p a.
	1.3 Infrastructure improved and well-maintained with community participation ▪75% of target community members satisfied with the procedure for the identification, selection, and implementation of sub-projects ▪85% of target beneficaries of sub-projects satisfied with infrastructure activities implemented ▪options identified for integrating needs-driven public expenditure allocation with regular local government budgeting.		GoM will institutionalize LIF scheme in budgetary process.

Output from each Component:	Output Indicators:	Project reports:	(from Outputs to Objective)
1. An integrated strategy developed, piloted, and adopted in 8 selected *aimags* for managing covariant risk in pastoral livestock production, with a primary emphasis on risk preparedness.	**Sub Component 1.1 – Risk forecasting and contingency planning strengthened** 1.1.1 Capacity of hydro-meteorological stations to generate weather forecasting data increased in 16 *sums* of 8 core *aimags* 1.1.2 Semi-annual (April & August) Early Warning System Bulletins provide meaningful messages for risk management and are received and used as input to contingency planning by local authorities and herders in at least the 8 *aimags* 1.1.3 Risk-management and contingency plans developed and operational in 143 *sums* of 8 core *aimags* to facilitate rapid response and local action when required **Sub-component 1.2 – Grazing and pasture management improved** 1.2.1 Community-based grazing management systems revitalized, grazing discipline improved, and pasture conflict effectively managed in 143 *sums* 1.2.2 Emergency grazing reserves rehabilitated, used and effectively managed (2 inter-*aimag* reserves rehabilitated including 6 wells rehabilitated & 2 management plans; inter-*sum* grazing reserves established in 4 *aimags* without access to inter-*aimag* reserves including 16 wells rehabilitated) 1.2.3 Around 430 wells rehabilitated in under-used grazing areas and effectively managed by herder groups/ communities, allowing pastures to be brought back into use and local grazing intensity to be reduced **Sub-component 1.3 – Herder self-help groups established and able to mobilize resources for risk management and livestock productivity improvement** 1.3.1 Herder self-help groups established and members trained in organizational and business skills, and effective group behaviors demonstrated (e.g. mentoring of less experienced by more experienced herders), facilitating collective action where appropriate in livestock production, processing and marketing (430 groups in 8 *aimags*) 1.3.2 Multi-purpose revolving funds successfully managed by herder self-help groups for risk-management and livestock productivity-enhancing activities including nucleus herd breeding, purchase of veterinary drugs and services, bulk hay and fodder purchase, dairy processing, cashmere sorting and grading, joint livestock	Annual performance monitoring reports Semi-annual progress reports Semi-annual Bank staff supervision site visits Quarterly FMRs	A large-scale *dzud* does not overwhelm institutional capacity to cope while pastoral risk management strategy is being established Adequate capacity building for project staff at all levels UNDP/Govt of Netherlands, ADB, and IFAD-supported projects are implemented as scheduled and their interventions complement the SL project. Agricultural and/or environmental officers participate effectively as HLSC members and mobilize herder groups

	marleting, group-based animal theft/ predator control (192 groups, or around 45% of those initially established) **Sub-component 1.4 – Commercial viability of hay and fodder enterprises demonstrated in *dzud* and non-*dzud* years** 1.4.1 Mechanized hay-making piloted and commercial business model (including marketing) successfully demonstrated (2 irrigated, 3 rain-fed) 1.4.2 Hay-making with animal drawn equipment piloted and commercial business model (including marketing) successfully demonstrated (60 HHs) 1.4.3 Commercial concentrate feed making piloted and commercial business model (including marketing) successfully demonstrated (4 companies) 1.4.4 *Aimag*- and *sum*-level emergency fodder reserves managed on sustainable basis (8 *aimags*)		*Dzud* occurs in at least one year in some pilot areas of 8 core *aimags* to allow business models to be tested
2. Outreach of institutionally and financially sustainable micro-finance services to targeted poor and near-poor vulnerable households achieved in selected *aimags*.	**Sub-component 2.1 – Enabling environment for micro-finance outreach to poor established** 2.1.1 Micro-finance Development Fund established and subsidiary loan agreements concluded with selected MFIs for on-lending in 8 core *aimags* 2.1.2 Micro-finance products tailored to the needs of the able-bodied poor and vulnerable near-poor developed and being taken up in 8 core *aimags* 2.1.3 Policy and legal framework for MF outreach established	Annual performance monitoring reports Semi-annual progress reports Semi-annual Bank staff supervision site visits Quarterly FMRs	Sufficient number of MFIs meet qualifying criteria to obtain subsidiary loans from MDF
	Sub-Component 2.2 – RLF strengthening & privatisation 2.2.1 RLFs with >80% repayment rate upgraded 2.2.2 RLFs with <80% repayment rate restructured 2.2.3 Privatisation of RLFs piloted in core *aimags*		MFI law does not require RLFs to shut down before their privatization
	Sub-component 2.3 – Commercially viable approach to livestock insurance developed and operational nation-wide 2.3.1 Weather-based and/or livestock mortality-based index developed for all *sums* nation-wide 2.3.2 Herders take up index-based insurance in sufficient numbers that scheme is profitable by end of project 2.3.3 Participation of private insurance companies is sufficient to meet demand for insurance nation-wide 2.3.4 At least one insurance company offering index-based insurance obtains international reinsurance by end of project.		Weather-based and/or livestock mortality-based index accurately reflects underlying risks and data remain free from manipulation by local officials Government-offered livestock insurance stop-loss provision is sufficient to limit losses for private insurance companies while scheme is developed
3. Efficient, socially inclusive, and transparent community- driven mechanisms identified and established in selected *aimags* to execute investments in local	**Sub component 3.1 – Investments made in community-identified sub-projects nation-wide through local investment funds (LIF and LDF)**	Annual performance monitoring reports Semi-annual progress reports Semi-annual Bank staff supervision site	Wider governance and civil-service reforms implemented as planned Line ministries do not resist community-driven, cross-sectoral

infrastructure and social services, and future plans agreed for integrating them with regular inter-governmental budget transfers.	3.1.1 LIF has financed community-identified and -prioritized *bag*- and *sum*-level sub-projects in 143 *sums* of the 8 core *aimags* and 1 *duureg* 3.1.2 LDF has financed community-identified and -prioritized *sum*-level sub-projects in 13 non-core *aimags* and 8*duuregs* 3.1.3 Combined community/ local government contribution amounted to 10% of total cost of sub-projects under LIF.	visits Quarterly FMRs	financing mechanisms Communities able to mobilize resources to make own 10% contributions
	Sub component 3.2 – Training and capacity-building completed 3.2.1 HLSPO staff are familiar with operational modalities of LIF/LDF and team built 3.2.2 Key national-level stakeholders (NCHLCSP members, Ikh Khural members and Standing Committee chairs, *aimag* governors and *khural* members, senior line ministry officials, civil society representatives) have clear understanding of LIF/ LDF and support project activities 3.2.3 *Aimag* and *sum* HLSC members (including HLSC coordinators, *sum* governors and *khural* members, *aimag* and *sum* line-department officers, NGO representatives) in 143 *sums* of 8 core *aimags* and 1 *duureg* have clear understanding of LIF operational modalities and are able effectively to mobilize communities in developing proposals for sub-projects 3.2.4 *Aimag* and *sum* HLSC members in 13 non-core *aimags* and 8 *duuregs* have clear understanding of modified LDF operational modalities and are able effectively to mobilize proposals for sub-projects 3.2.5 Community mobilization and leadership skills at *bag* level developed, enabling *bag* governors and other community leaders to play lead role in mobilizing community participation and eliciting proposals for LIF sub-projects.		Change of national or local governments does not lead to loss of institutional capacity built at all levels
	Sub component 3.3 – Options for fiscal decentralization successfully demonstrated for wide implementation under Phase II 3.3.1 Best practices for fiscal management agreed and an issues and options paper prepared 3.3.2 Fiscal management pilot programs completed in 8 *sums* in the 8 core *aimags* in PY3 and PY4 3.3.3 Impact and implications of programs established and action plan agreed for the extension of fiscal decentralization initiatives to other areas.		Key policy reforms relating to fiscal decentralization/ inter-governmental transfers identified by end of Phase I and ready for adoption during Phase II
4. Project management system operational and policy framework for promoting sustainable	**Sub component 4.1 – Project management system established and operational**		Change of national or local governments does not lead to loss of institutional capacity built at all levels

livelihoods improved.	4.1.1 HLSPO fully staffed (16 staff members), team built, office equipped, and operational at central level 4.1.2 Project management and coordination system functioning at *aimag* and *sum* levels (HLSCs) 4.1.3 Project implementation manual used and regularly updated in light of operational experience 4.1.4 Financial management and procurement system established and operational 4.1.5 Lessons learned from Phase I and incorporated into Phase II design. **Sub component 4.2 – Policy and legislative support provided** 4.2.1 100 people concerned with policy/legislative initiatives concerning sustainable livelihoods have better understanding of the options and opportunities for improving the policy framework for sustainable livelihood after participating in cross-sectoral workshops 4.2.2 40 level decision makers better able to formulate policies and legislation after participating in project policy/legislative briefing sessions 4.2.3 200 representatives at *bag* and *sum* levels present priority concerns affecting formulation and implementation of sustainable livelihoods strategies in annual workshops **Sub-component 4.3 – Communications strategy developed and program- relevant information disseminated** 4 3.1 Communications strategy prepared, implications for radio broadcasts and publications decided, and strategy operational 4.3.2 Regular radio broadcasts, as proposed in the communications strategy, reach target beneficiaries 4.3.3 Newsletters published and disseminated as recommended in communications strategy 4.3.4 400 people participated in orientation workshops held in the 8 core *aimags*, 1 pilot *duureg*, 13 non-core *aimags* and 8 *duuregs* on project operations 4.3.5 160 people including *sum* governors, *khural* chairs, *bag* governors, *sum* HLSCs, NGOs, etc participated in orientation workshops held in the 8 core *aimags* and 1 pilot *duureg* **Sub-component 4.4 – Monitoring and evaluation system and MIS developed and operational** 4.4.1 Integrated MIS and participatory M&E operational and used for effective management and decision-making 4.4.2 Training-of-trainers courses conducted in participatory M&E approaches and implementation modalities		Sufficient, qualified and experienced technical assistance locally available

	4.4.3 MIS data including PM&E findings used as inputs for Mid-Term Review and EOP Evaluation Report		
Project Components / Sub-components:	**Inputs: (budget for each component)**	**Project reports:**	**(from Components to Outputs)**
1. Pastoral risk management **1.1 Risk forecasting and contingency planning** 1.1.1 Equipment procured for 16 *sum* level hydro-meteorological stations (8 automated weather stations, 16 wind speed/direction meters, 16 power generators, 16 electronic scales for measuring pasture yield) 1.1.2 Consulting services to assist in developing strategy for broadening inputs to Early Warning System bulletins, data acquired, bulletins produced and distributed (new data to include. long-range weather forecasting data, NDVI for pasture yield calculated using NOAA satellite imagery, market information, livelihood well-being indicators; 12,570 bulletins produced over life of project) 1 1.3 Consulting services to assist local governments in 16 pilot *sums* to develop risk-management and contingency plans in PY1, and development of training strategy and delivery of training to assist remaining 127 *sums* of the 8 core *aimags* to develop same by EOP **1.2 Grazing and pasture management** 1.2.1 Preparation of land-use maps and community-based grazing-management plans in 16 pilot *sums* during PY1, and training strategy and delivery of training to assist local authorities to develop same for remaining 127 *sums* in 8 core *aimags* by EOP, with attention paid to seasonal pasture rotation, conflict management, group-based pasture tenure, ecological approaches to rodent control, etc (42 person/ months consulting services & direct costs) 1.2.2 Two fodder storage facilities constructed for 2 inter-*aimag* grazing reserves, 8 engineered wells rehabilitated, and management plans prepared with consultant support; and 16 wells rehabilitated in inter-*sum* grazing reserves in 4 *aimags* 1.2.3 430 wells rehabilitated on under-utilized pastures in 8 core *aimags*, executed by herder groups/ communities **1.3 Herder self-help groups** 1.3.1 48 person/months consulting services (12 each year) to deliver training/ capacity-building support for around 430 herder self-help groups in 143 *sums* of 8 core *aimags* (training of leaders and members, assist in opening bank accounts and legal registration) 1.3.2 Time-bound, matching loans made available to 192 herder self-help	US$ 5.70 million total cost for component 1 US$ 223,030 cost for sub-component 1.1 1.1.1 US$ 80,552 1.1.2 US$ 71,596 1.1.3 US$ 70,882 US$ 1,645,330 cost for sub-component 1.2 1.2.1 US$ 241,681 1.2.2 US$ 115,677 1.2.3 US$ 1,287,973 US$ 1,999,742 cost for sub-component 1.3 1.3.1 US$ 79,742	Monthly site visits by *aimag* HLSC staff with *aimag*-level PRM Working Group members Monthly review and quarterly monitoring meetings with national-level PRM Working Group Quarterly FMRs Semi-annual progress reports to the Bank Semi-annual Bank staff supervision visits Annual audited financial reports Annual work plan and budget review meeting with PRM national-level Working Group (forward-looking)	Competent technical assistance locally available PRM Working Group members devote adequate time to oversight of component implementation, and are able and willing to ensure good coordination between activities.

groups for eligible activities as specified in PIM (loans to cover 50% of total cost of sub-projects of an average size of US$10,000)	1.3.2 US$ 1,920,000		
1.4 Hay and fodder enterprise development 1.4.1 Equipment procured for hay-making and feed concentrate production enterprises (9 tractors, 6 tractor-drawn rakes, 3 balers, 24 animal-drawn mowers, 24 animal-drawn rakes, 1 feed grinder, 1 feed mixer) and made available to pilot enterprises on lease or hire-purchase basis; 2 irrigation systems rehabilitated; 1 building renovated	US$ 1,295,393 cost for sub-component 1.4 1.4.1 US$ 666,657		
1.4 2 Storage facilities for 8 *aimag* -level and 16 *sum*-level fodder banks constructured or rehabilitated (cost of fodder met separately from Government budget under existing inter-governmental loans scheme)			
1.4.3 40 person/months of consulting services for the development of management plans for revolving fodder banks and for business management services to pilot hay-making and fodder enterprises	1.4.2 US$ 562,284		
Component Management and Implementation Proportionate share of HLSC vehicle and equipment costs, incremental staffing, and recurrent costs (vehicle O&M, office peripherals, field allowances, honoraria for working group members).	1.4.3 US$ 66,452		
Training events and workshops (8 *aimag* and 16 *sum*-level orientation workshops; technical training for local officials and herders in 16 *sums*; and training of trainers workshops.	US$ 364,228		
	US$ 170,872		
2. Rural micro finance **Sub-component 2.1 - Establishment of Micro-finance Development Fund**	US$ 6.01 m total cost for component 2	Monthly review and quarterly monitoring meetings of MDF Board	RLFs continue to operate during the transition period
- Office start-up costs; international study tour; consulting services for market research, strategy development and new products design; training	2.1a US$ 205,164	Quarterly FMRs Semi-annual progress reports to the Bank	MDF is able to find partner MFIs interested in profitably servicing the poor
- Total cost of micro-finance sub-loans (financed @75% from creditline to selected MFIs)	2.1b US$ 4,000,000	Semi-annual Bank staff supervision visits	
Sub-component 2.2 - Strengthening of Revolving Loan Funds - Consulting services in training and upgrading RLF performance; assistance to RLFs qualifying for top-up funds		Annual audited financial reports	
- Top-up funds for qualifying RLFs	2.2a US$ 108,012		
Sub-component 2.3 - Index-based Livestock Insurance Scheme - Consulting services for design of index, training workshops, information campaign	2.2b US$ 500,000		
- Stop-loss provision			
Component Management and Implementation Incremental staffing of MDF office in	2.3a US$ 124,325		

Bank of Mongolia, office equipment, and recurrent costs (office peripherals and equipment O&M, honoraria for MDF Board members, field allowances for HLSC staff in supervising RLFs).	2.3b US$ 1,000,000 US$ 75,828		
3. Local Initiatives Fund **Sub component 3.1 – LIF/LDF Activity Implementation** - pilot LIF activities in 2 *sums* from each of the 8 core *aimags* and one *duureg* during the first year - begin implementation of LIF in all sums in eight core aimags - financing of LDF operations in 13 non-core aimags and 8 duuregs **Sub-component 3.2 – Training & Capacity Building** - NGO/research institution contracted to work with HLSPO in design & implementation of training program Training programs implemented: - workshop for HLSPO staff - national workshop for key stakeholders - orientation workshop on LIF for 8 core *aimags* and one *duureg* - orientation workshops on LDF for 13 non-core *aimags* - *aimag* HLSC training of trainers - *sum/aimag* training on community mobilization, administration, and facilitation - *sum/aimag* reorientation on new operations of LDF - *bag/sum* training sessions on leadership, community mobilization and development, and participation - technical training on demand Impact assessment of training and capacity building activities completed after 1st year of implementation, for subsequent modification of training program based on experience from 1st year **Sub-component 3.3 – Pilot Fiscal Management Initiative** – Request for proposals for fiscal management initiative – Research contract prepared by HLSPO – Draft workplan for fiscal management initiative prepared, discussed & workplan finalized – Pilot initiative implemented in 1 *sum* in one of 8 core *aimags* in PY3 and PY4 – Initial pilot activities evaluated & training material prepared for extension into 7 more *sums* (1 per *aimag*) **Component Management and Implementation** Proportionate share of HLSC vehicle and equipment costs, incremental staffing, and recurrent costs (vehicle O&M, office peripherals, field allowances for incremental staff and technical backstopping, honoraria for	US$ 9.16 million total cost of component 3 3.1a US$ 3,962,000 total cost of LIF sub-projects 3.1b US$ 3,504,000 total cost of LDF sub-projects 3.2 US$ 249,452 3.3 US$ 105,925 US$ 1,341,836	Monthly site visits by *aimag* HLSC staff with *aimag*-level LIF Working Group members Monthly review and quarterly monitoring meetings with national-level LIF Working Group Quarterly FMRs Semi-annual progress reports to the Bank Semi-annual Bank staff supervision visits Annual audited financial reports Annual work plan and budget review meeting with LIF national-level Working Group (forward-looking)	Timely disbursements and liquidity of Agriculture Bank, and continued good performance and management once privatized Competent technical assistance locally available for participatory training methodology

LIF Working Group members).			
4. Management and Policy Support **Sub-component 4.1 - HLSPO** 1 x 4WD Vehicle, 17 computers, MIS development, office furniture, 16 staff members (long-term consultants on fixed-term contracts), and vehicle/ office equipment O&M costs **Sub-component 4.2 - Policy & Legislative Support** Cross-sectoral technical workshops, High-level policy-makers briefing sessions, *sum/bag* demand-focused policy workshops, studies and surveys (including baseline survey) **Sub-component 4.3 - Information Dissemination and Communications** Development of communications strategy, radio program development & broadcasts, preparation & distribution of newsletters **Sub-component 4.4 - Project Orientation and Training** Orientation workshops for 8 core *aimags* & 1 pilot *duureg*, 13 non-core *aimags* & 8 *duuregs* **Sub-component 4.4 - Monitoring and Evaluation** Design & testing of M&E system, training of trainers in participatory M&E, mid-term review, end of Phase I evaluation, auditing.	US$ 1.25 million total cost for component 4 US$ 684,408 US$ 93,032 US$ 180,049 US$ 20,565 US$ 270,113	Quarterly FMRs Semi-annual progress reports to the Bank Semi-annual Bank staff supervision visits Annual audited financial reports	Government pre-finances start-up costs of HLSPO, making use of retroactive financing if desired

Attachment 1: THE THREE PHASES OF THE PROGRAM

	Phase I	Phase II	Phase III
Component I Pastoral Risk Management	4 sub-components: Risk forecasting & contingency planning Grazing & pasture management Herder self-help initiatives Hay & fodder enterprise development	Successful activities from Phase I extended nationwide; New components added: - Livestock marketing (opportunistic pre-winter culling/"strategic destocking)" - Livestock production systems intensification & diversification (peri-urban)	PRM program fine-tuned for sustainability, and institutionalized in regular GoM activities; Herder groups prepared for phase-out of donor support; Marketing expanded nationwide; Differentiation/intensification of production systems: coexistence of extensive, semi-intensive and intensive production;
	US$ 5.70 million total cost IDA share US$ 4.13m	US$ 13.0 million base cost IDA share US$ 8.0m	US$ 18.0 million base cost IDA share US$ 8.0m
Component II: Micro-Finance Outreach	Establish Microfinance Development Fund (MDF); New financial products piloted by MFIs	MDF becomes financially and institutionally self-sustaining; New products extended by MFIs	MDF programme continues nationwide; New products consolidated nationwide
	Upgrade local government-administered Revolving Loan Funds (RLFs)	Privatised RLFs in 8 core *aimags* become financially self-sustaining	
	RLF restructuring/privatisation in 143 *sums* of core *aimags*	RLF privatisation in non-core *aimags*	Privatised RLFs in non-core *aimags* financially self-sustaining
	Index-based livestock insurance scheme developed and operated by private insurance companies, backed by Government stop-loss provision	Index-based livestock insurance scheme operated by private insurance companies on full commercial basis with international reinsurance and no need for public stop-loss provision	
	10% of targeted poor in core *aimags* have access to micro-finance	20% of targeted poor have access to micro-finance	50% of target poor have access to micro-finance
	US$ 6.01 million total cost IDA share US$ 5.00m	US$ 6.2 million base cost IDA share US$ 4.2m	US$ 12.1 million base cost IDA share US$ 6.1m
Component III: Local Initiatives Fund	LIF operations for sum and bag-level projects piloted for 1 year in 2 sums of the 8 core *aimags*	LIF extends nation-wide (340 *sums*)	2-window LIF operational nationwide fine-tuned for sustainability beyond EOP
	Full LIF operations from PY2 in 143 *sums* of 8 core *aimags*		
	LDF: 1-window facility for *sum* level projects operates in all *sums* of 13 non-core *aimags*	LDF ceases to operate, having been supplanted by LIF	
	Pilot fiscal decentralization initiative begins in 2 *sums* of the 8 core *aimags* in PY3 and PY4.	LIF brought into budget in core *aimags*	LIF brought into GoM budget nationwide
	Budget share: 10% from community/government and 90% from IDA	Budget share: 40% from government; 10% from community; and 50% from IDA	Budget share: 70% from government; 10% from community; and 20% from IDA
	US$9.16 million total cost IDA share US$ 8.52m	US$ 15.1 million base cost IDA share US$ 7.6m	US$ 14.6 million base cost IDA share US$ 3.2m
Component IV: Management & Policy Support	Includes establishment of HLSPO capacity building for pilot activities in 143 *sums* in core *aimags*, plus policy initiatives	Includes capacity building for nationwide program extension to 340 *aimags* + national policy initiatives	Includes fine-tuning and consolidation of activities in 340 *aimags*; full integration in GoM budget and programs

	US$ 1.25 million total cost IDA share US$ 1.08m	US$3.0 million base cost IDA share US$ 2.0m	US$ 3.0 million base cost IDA share US$ 2.0m
Total Program	US$ 22.12 million total cost IDA share US$ 18.73m	US$37.3 million base cost IDA share US$ 21.8m	US$47.7 million base cost IDA share US$ 19.3m

Attachment 2: Performance triggers for successive credits, by component:

Pastoral Risk Management

Triggers from **Phase I to Phase II**:

- institutional framework for PRM established and functioning at national level and in core *aimags*;
- integrated *sum*-level contingency and grazing management plans formulated and under implementation in all *sums* of the selected *aimags*;
- socially inclusive herder organizations established and well functioning in over half of *sums* in the selected *aimags*;
- group-based approach to well rehabilitation and management successfully pilot-tested;
- PRM strategies developed and successfully tested for at least two AEZs; and
- at least three of the following activities proven successful and ready for scaling-up in Phase II: herder group self-help initiatives, commercial hay making (with mechanized or animal-drawn equipment) and feed concentrate production, or *aimag*- and *sum*-level emergency fodder reserves.

Triggers from **Phase II to Phase III** would include:

- institutional framework for PRM in place and functioning nationwide on all levels (national, *aimag*, *sum*, *bag*, herder groups);
- PRM strategies developed and successfully tested for all AEZs/herding systems;
- mechanisms to support opportunistic pre-winter marketing of cull animals by herder groups successfully piloted; and
- evidence of GoM commitment to institutionalize PRM in its regular programs.

Micro-Finance Outreach

Triggers from **Phase I to Phase II**:

- Micro-Finance Development Fund established and operational;
- micro-finance products tailored to the poor developed and successfully piloted in core *aimags*;
- less than 10% of total loan portfolio of selected RLFs past due
- selected RLFs achieve 50% operational self-sufficiency
- 50% of selected RLFs receiving additional funding privatized; and
- index-based livestock insurance scheme developed and operational and, ideally, at least one participating insurance company has secured international reinsurance.

Triggers from **Phase II to Phase III** would include:

- Micro-Finance Development Fund achieves financial and institutional self-sufficiency;
- substantial improvement in micro-finance outreach to the poor in rural areas (20% of population in selected *aimags* have access to micro-finance services);

- at least 50% of ex-RLFs privatized under Phase I achieve financial viability by the end of Phase II; and
- RLF credit operations in additional *aimags* successfully privatized.

Local Initiative Fund

Triggers from **Phase I to Phase II**:

- management capacity at *sum* level created/strengthened and operating effectively in the implementation of LIF;
- the process of identifying and selecting projects carried out so that community priorities are fairly and accurately reflected including the priorities of women and youth;
- the management and flow of funds are competently handled with no misappropriation of funds and with minimum delays, as reflected in clean audit opinions;
- a commitment has been made by government to make available to the *sums* discretionary funds for local investment as identified through the LIF and the necessary legal and policy instruments have been put in place to allow the LIF to be incorporated into the regular government budgetary process;
- the output indicators stipulated in the component logframe have been met or exceeded; and
- a participatory monitoring and evaluation system is in place and operating effectively.

Triggers from **Phase II to Phase III** would include:

- agreed levels of revenue generation by *sum* governments have been attained;
- legislative and policy reforms have been adopted and implemented nationwide; and
- fiscal management capacity created and procedures to ensure accountability are in place in all *sums* and *duuregs* that will participate in phase 3 LIF operations.

Annex 2: Detailed Project Description
MONGOLIA: Sustainable Livelihoods Project

Overview

The project development objective 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". Four investment components aim to deliver the outputs that in combination would achieve this development objective over the first four years (Phase I) of the three-phase, 12-year program:

1. The Pastoral Risk Management (PRM) component: 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 aims to reduce the vulnerability of herders and enhance their resilience to drought, *dzud* and other shocks through testing and developing approaches in support of risk forecasting and contingency planning; grazing and pasture management; herder self-help initiatives; and hay and fodder enterprise development;

2. The Micro-Finance Outreach (MFO) component aims to improve the access of the poor to financial services by creating a micro-finance apex facility for wholesale lending to MFIs; strengthening existing revolving loan fund operations in *sums* and *khoroos* (rural and urban districts) and facilitating their conversion into viable private sector entities; and developing a commercially viable, index-based approach to livestock insurance;

3. The Local Initiatives Fund (LIF) component would improve the access of the poor in rural and peri-urban areas to basic infrastructure by supporting local investment funds including the creation of a new community-responsive financing window (the LIF) and the funding of a modified Local Development Fund (LDF), providing training and capacity-building support, and undertaking an action-research initiative to identify options for fiscal decentralization; and

4. The Project Management and Policy Support component would establish a decentralized management system for the project, which would also be responsible for support to formulation of policy reforms, communications, monitoring and evaluation, and fiduciary oversight including external auditing.

By Component:

Project Component 1 - US$5.70 million

Pastoral Risk Management

Guiding principles:

- Base component activities on participatory decision-making processes with broad stakeholder involvement, and strengthen the capacity of herders and local authorities to play active roles.
- Apply flexible programming based on a guided, learning-by-doing implementation strategy.
- Build on what already exists, and in particular on related programs supported by MoFA.

Approach:

The PRM component primarily concerns measures to improve risk preparedness by herders and local authorities. It supports the implementation of Government Resolution 47 on measures to protect against losses from drought and *dzud*, but does not attempt to deal with all aspects of this Government program. Support for risk preparedness should also be viewed in the context of other stages in a notional risk 'cycle', as follows:

- Risk Avoidance and Preparedness: It is important to distinguish between: (i) long-term *strategies for risk reduction and avoidance*, which prepare the herding economy and authorities on an on-going basis for stress periods, such as winter, and for unexpected shocks; and (ii) *annual (short-term) planning for risk,* which includes activities that prepare the herding households for regular (foreseeable) stress periods such as occur during the winter months.
- Responding to Risk: The response to risk arising once a risk turns into an acute threat and then hardship and damage dictates immediate action. It is more likely that successful action can be taken if good planning and preparatory steps have been taken by all stakeholders involved. Actions piloted by the project would pursue immediate and integrated solutions.
- Recovering from Damage: Recovery from damage is vital to livelihood security and sustainability. Until the household economy has recovered, it remains vulnerable to new risks. Any recovery process in the context of risk management should be understood as a new step towards renewed preparedness. The level of damage/loss and the support needed at this stage are determined, on the one hand, by the gravity of the calamity and, on the other hand, by the quality, quantity and coordination of actions during the previous stages.

To achieve this integrated approach, the PRM component would: test and consolidate economically viable, region-specific, risk management strategies for improved disaster preparedness; build up technical capacities for the implementation of these strategies; and put in place the necessary organizational mechanisms at each administrative level.

Description of investment required:

The PRM component consists of four sub-components: (i) risk forecasting and contingency planning; (ii) grazing and pasture management; (iii) support for herder self-help groups; and (iv) hay and fodder enterprise development. Capacity-building measures are incorporated into each sub-component. Activities would vary by AEZ and herding system in response to herder demand. Micro-finance services for herders - notably development of an index-based livestock insurance scheme - also support the overall goals of the PRM component and are considered under the Micro-Finance Outreach component description below.

1. Risk Forecasting and Contingency Planning: This sub-component would support the improvement of the emergency forecasting system (improving weather forecasting, incorporating additional information in the emergency forecasting system, improving the dissemination of forecast information to herders, and improving the use of forecasting information for rapid response) and the development of *sum*-level risk management or contingency plans in all *sums* of the eight core *aimags*. Three activities are envisaged:

(i) *strengthening of* sum-*level hydro-meteorological services to improve coverage of weather forecasting information* - the project would finance central procurement by HLSPO of equipment for *sum*-level meteorological stations, including: wind direction/speed meters, power generators, and electronic scales for assessing pasture yield for 16 *sums* in the 8 core *aimags*, and automated weather stations for 8 *sums*;

(ii) *development and dissemination of Early Warning System Bulletins* - the project would finance consulting services to assist MoFA's Information, Monitoring and Evaluation Department and the Institute of Hydro-Meteorology in broadening the range of data used in EWS bulletins published in April and August each year to include: long-range weather forecasting data; NDVI remote-sensing data for range vegetation monitoring; market information; and livelihood well-being indicators. Information dissemination would be in hard copy from central to *aimag* levels, and from there via the existing network of short-wave transceivers to *sum* and *bag* levels. Financial support would also be given for data acquisition and for the development and dissemination costs involved in producing the EWS bulletins; and

(iii) *development of* sum-*level contingency plans* - drawing on the EWS bulletins and locally gathered indicators, various stages of alert would be defined (normal, alert, alarm, emergency), each of which would trigger a series of pre-planned actions at *sum* level with clearly defined institutional responsibilities. Local consulting services would assist in developing such contingency plans for 16 *sums*, and in developing training materials and conducting training activities to enable technical staff in the 8 core *aimags* to develop similar plans for the 127 remaining *sums* in the 8 core *aimags* over the next two to three years.

2. Grazing and Pasture Management: Three activities are envisaged in support of this sub-component:

(i) *community-based pasture management* - the project would finance local consulting services to assist herder groups and *sum/bag* officials in the development of pasture management plans for 16 pilot *sums* in the first year of the project, and to develop training materials and a training strategy to enable the 8 core *aimags* to develop similar plans for the remaining 127 *sums* in the 8 core *aimags* over the next two years. Preparation and application of the pasture management plans would involve require some or all of the following steps being carried out with herding communities: identification and mapping of seasonal grazing areas; scheduling of pasture rotation; the application of appropriate group-based pasture tenure options under the land law (e.g. possession contracts); making arrangements for negotiating reciprocal rights of access with other communities or herder groups during risk episodes; establishing and adopting procedures for conflict management; developing ecological approaches to rodent control; and participatory monitoring of range vegetation condition;

(ii) *emergency grazing reserve rehabilitation and management* - the project would finance the rehabilitation of two inter-*aimag* grazing reserves (known as *otor* reserves) in Kherlenbayanulaan (bordering Khentii and Tov *aimags*) and Argalant (bordering Gov'Altai and Bayankhongor *aimags*), including: the rehabilitation or construction of fodder storage sheds, the rehabilitation of around 8 existing engineered wells in these reserves, and consulting services to support the development of management plans for these facilities. Fodder stocks should comprise primarily high-quality, long-life fodder (only a small proportion of hay), to be financed under an existing Government program, with management costs involved in the turnover of fodder stocks to be defrayed from the sales of fodder to the users of the emergency grazing reserves. In addition, the project would support the re-establishment of inter-*sum otor* reserves in 4 of the 8 core *aimags* without access to inter-*aimag* reserves by financing the rehabilitation of around 16 existing engineered wells in these grazing reserves; and

(iii) *group-based well rehabilitation and management* - the project would finance the rehabilitation of an estimated 430 existing engineered wells in areas of high-quality yet currently under-utilized pasture in the 8 core *aimags*, beginning with an average of two wells in each of the 16 pilot *sums* selected for the first year of the project. The selection of wells for rehabilitation would be made by herder groups in a participatory manner, and on the basis of the community-based pasture management plans to be developed under the project. Clearly identified herder/ well-user groups would be responsible for operation and maintenance (O&M), and would contribute around 10% of the cost of sub-projects in the form of labor, materials, and

O&M responsibilities. Procurement would follow similar procedures as under the LIF component (small works or community-contracting).

3. Herder Self-Help Groups: Strong herder groups are regarded as the key to successful pastoral risk management at community level. This sub-component would therefore focus on establishing and strengthening herder self-help groups above the *khot ail* (social herder unit) level, based on existing patterns of cooperation between herder households; and on supporting their initial development through time-bound, matching loans:

(i) *Organizational strengthening* - the project would finance local consulting services to facilitate the creation of herder self-groups and provide training for eligible new and existing herder self-help groups in 16 pilot *sums* in business and organizational skills, including assistance in legal registration and opening of a group bank account, and in developing proposals for activities eligible for matching loan support. The consultants would also develop training materials and a training strategy for scaling-up this approach beyond the initial 16 pilot *sums*, to cover all 143 *sums* in the 8 core *aimags*. Eligible groups would include existing residence-based groups and *khorshoo* (cooperatives). Groups may register as *khorshoo* or NGOs under existing law. It is anticipated that an average of around three such groups in each *sum* would receive such support (i.e. a total of around 430 groups); and

(ii) *Time-bound, matching loans* - on a clearly time-bound basis (e.g. 1-2 years), eligible herder groups would be able to access 50:50 matching loans via their local HLSC (with repayment terms specified in the PIM, but initially based on those adopted for the RLFs under the Micro-Finance Outreach component, i.e. interest payable 10% per annum, with a maximum loan term of one year) for eligible sub-project activities, based on an initial mobilization of savings from the group's own resources. Eligible activities would include but need not be restricted to: nucleus herd breeding, purchase of veterinary drugs and services, hay and fodder purchase and/or production, dairy and other livestock product processing, cashmere sorting and grading/ auctions, joint marketing activities, and group-based animal theft or predator control.
Cost-recovery would need to be sought within the group (e.g. for bulk-purchases of fodder or veterinary supplies) so as to preserve and build up group capital as a revolving fund. Access to progressively larger loans within the initial period would be contingent on demonstrated success in financial management and repayment of the initial loan. Beyond the period of eligibility for matching loans, herder groups would be required to seek micro-finance on a commercial basis (e.g. as developed under Micro-Finance Outreach component). Groups may also wish to use revolving funds as means to restock poorer member households as appropriate, although this would not be an eligible activity for the initial matching loans. Repayments from the matching loans would accumulate in revolving funds at the *aimag* level, managed by the *aimag* -level HLSCs/ PRM working groups, to be used for the same activities on an ongoing basis. It is anticipated that less than half of the initially supported groups would be eligible for and access time-bound, matching loans (a total of around 192 in the 8 core *aimags*).

4. Hay and Fodder Enterprise Development: This sub-component entails two activities:

(i) *testing and demonstration of business models for hay and fodder enterprise development using alternative technologies* - the project would pilot three commercial hay-making models with existing, private entrepreneurs using alternative technologies: (a) mechanized hay-making using tractor-drawn equipment under rainfed conditions (3 enterprises – 1,400 ha each); (b) mechanized haymaking under irrigated conditions (2 enterprises – 200 ha each); and (c) household-based hay-making using animal-drawn mowers (120 households – 45 ha each); and (d) the project would also pilot small-scale fodder, feed, and concentrate production to assess its commercial viability (4 companies). The objective would be to test whether the enterprises could become commercially and financially viable in both emergency and non-emergency years. The challenge for financial viability is for hay makers to sell their hay in years when there is little or no *dzud* threat.

For the mechanized models, the project would finance replacement of tractors and tractor-drawn equipment (mowers, rakes and balers) which would be contracted to selected enterprises on a hire-purchase basis, or under a lease arrangement with an option to buy at the end of project. Incremental operating costs would be borne by the enterprises. For animal-drawn production, the project would finance two pairs of draught animals (horses or yaks) plus animal-drawn mowers and rakes, which would be contracted by local government to households on a hire-purchase basis or under a lease arrangement with an option to buy at the end of project. The irrigated model would also involve the rehabilitation of two irrigation systems, for which the procurement of works under national competitive bidding would be required. This investment would be cover by the project (no cost recovery of investments from the beneficiaries), with possible water user fees to cover the cost of O&M on the part of local authorities or by water user groups. For the fodder concentrate enterprises, the project would finance the rehabilitation of buildings and replacement of equipment; and

(ii) *support for* aimag- *and* sum-*level fodder reserves* - management models for fodder reserves/ fodder banks would be tested in the 8 core *aimags* to ascertain whether they are able to recover their operating and overhead costs from fodder sales both in bad years and in good years when there is limited demand for their services. The project would finance the rehabilitation or construction of storage facilities, and local consulting services for the development of business management plans. Government would finance the fodder stocks under an existing program which provides loans to local government for hay and fodder purchase.

Although the PRM component may appear relatively complex, not all activities would be undertaken in all *sums* or even all *aimags*. In particular, activities such as hay and fodder production pilots, concentrate feed making, ecological approaches to rodent control, and inter-*aimag* emergency *otor* reserve rehabilitation would only be implemented in selected *sums* and *aimags*. Herder self-help group-based activities such as stock theft and predator control, breed upgrading, cashmere auctions, dairy production, and joint marketing would be implemented on a demand-driven basis. The expected distribution of project activities across the eight core *aimags* is described in the following table:

Regional Distribution of PRM Activities	Bayan Ulgii	Uvs	Bayan khongor	Ovor khangai	Omno gobi	Dund gobi	Tuv	Dornod
1. Risk forecasting and contingency planning								
Strengthening *sum*-level hydro-meteorological services	x	x	x	x	x	x	x	x
Development & dissemination of EWS bulletins	x	x	x	x	x	x	x	x
Development of *sum*-level contingency plans	x	x	x	x	x	x	x	x
2. Grazing and pasture management								
Community-based pasture management	x	x	x	x	x	x	x	x
Inter-*sum* emergency grazing reserves	x	x		x				x
Inter-*aimag* emergency grazing reserves			x		x	x	x	
Group-based well rehabilitation	x	x	x	x	x	x	x	x
e.g. ecological approaches to rodent control				x		x	x	
3. Herder self-help group initiatives								
Organizational strengthening	x	x	x	x	x	x	x	x
Time-bound, matching loans	x	x	x	x	x	x	x	x
Demand-driven activities (breed improvement, marketing, etc.)	x	x	x	x	x	x	x	x
e.g. group-based stock theft and predator control	x	x						x
4. Hay and fodder enterprise development								
Household-based, animal-drawn hay making	x	x	x	x			x	x
Mechanized, rainfed hay production	x	x					x	x
Mechanized, irrigated hay production		x						
Feed concentrate production				x			x	x
Local fodder reserve management	x	x	x	x	x	x	x	x

Implementation arrangements:

The project would finance a PRM component coordinator within HLSPO (long-term consultant) to take primary responsibility for overseeing component implementation, and would establish technical PRM Working Groups at central level and each of the 8 core *aimags* to advise on component implementation. The national level PRM Working Group would also help to assess the policy implications of the evolving program, and channel priorities identified at *sum*, *bag,* and herder-group levels into national policy and planning processes. The *aimag* working groups would act in an advisory capacity to their respective *aimag* -level HLSCs. Support is also provided for PRM project implementation groups at *sum* and *bag* levels, with the main emphasis placed on capacity building through training workshops at *sum, bag,* and herder-group levels.

Central level. The technical Working Group to advise on project implementation has been established at national level, with eight members. Three members represent divisions of MoFA; namely: Livestock and Water Supply Division (the Chief of which chairs the Working Group); the Policy and Planning Division; and the External Relations Division. An additional member represents MNE, drawn from either the Land Administration Authority or the Institute of Hydrology and Meteorology. Two civil society representatives, both specialists in pastoral risk management, serve as advisory members. They are drawn from among the Mongolian State University of Agriculture, a research institute or NGO, and/or a professional association such as the Mongolian Graziers Association. Two HLSPO staff members, the PRM Coordinator and the Project Coordinator, are ex-officio members of the Working Group; the PRM Coordinator serves as secretary to the Working Group.

The terms of reference of the PRM Working Group are to: ensure that GoM policies are adequately reflected in the component activities; provide technical advice to HLSPO on the content of policy and how to implement it; prepare and revise the PIM in the light of experience and in consultation with the World Bank; prepare and approve terms of reference for the required consulting services and assist in the preparation of consultant short-lists; advise on the preparation of tender/ bidding documents for the procurement of goods or works under international and local shopping and small works procedures; receive, review, and comment on progress reports on the implementation of the PRM component produced by HLSPO staff; together with HLSPO staff, conduct field site visits to evaluate and monitor performance; and support discussion and formulation of policy reforms, when suggested by project experience. The Working Group shall meet regularly on a monthly basis.

***Aimag* Level.** PRM working groups would also be established in the 8 core *aimags*, drawn from existing technical staff within the *aimag* local government structure. The *aimag* working groups would perform similar role to the central Working Group, but in an advisory capacity to their respective *aimag* HLSC. The *aimag* HLSC would play a supervision/ evaluation and technical backstopping role, although it would be directly responsible for the implementation of certain some activities (e.g. well rehabilitation in inter-*sum* grazing reserves).

***Sum* and *Bag* Levels.** The *sum* HLSC would carry the main responsibility for execution of PRM activities, and would have direct responsibility for some two thirds of the component's activities. The HLSC will include those relevant technical specialists on staff in that *sum*, whether they are primarily responsible for agriculture, livestock/ animal husbandry, or environmental inspection. Working closely with *bag* governors (also members of the HLSC) and in the context of public meetings of the *bag khural*, the HLSC would encourage interested herders to form herder groups and participate in component activities as appropriate.

Project Component 2 - US$6.01 million
Micro-Finance Outreach Component.

Sub-component 1: Micro-Finance Development Fund (MDF)

The objective of the component is to expand the outreach of financially and institutionally sustainable micro-finance services to targeted poor and vulnerable non-poor households and individuals in remote rural areas of the eight core *aimags*. This first sub-component includes the 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 Operational Manual (the Operational 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 microfinance 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 include also substantial technical assistance resources to promote the strengthening of the MFIs and to 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 IDA funds allocated to this sub-component for the micro-finance sub-loans (Category 5, for a total equivalent to around US$3 million), the Borrower would: (a) establish a MIS adequate to monitor micro-finance portfolio quality (in accordance with CGAP guidelines); (b) adopt an Operational Manual acceptable to IDA for the implementation of the sub-component; (c) establish and maintain during project implementation the Micro-Finance Development Fund (including the Board and the Management Office) under terms and conditions satisfactory to IDA; and (d) accredit MFIs 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 Operational Manual.**

Operation of the MDF. The daily management and operation of the MDF (as a commercial wholesale banking facility) would be the responsibility of MMO, which will be adequately budgeted, well equipped and with qualified staff 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 Operational Manual (the Operational Manual) acceptable to the Bank. The main sections of the Operational 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 Operational Manual was reviewed by the Appraisal Mission and found to be satisfactory. In order to ensure a full coordination and efficient use of credit resources, MMO's implementation of 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 micro-finance institutions), and academia. The Director of 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 micro-finance development fund, 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, the future of the MDF would be discussed in the context of the preparation or the Phase II of this APL, and the implementation of the agreed actions included in the design of this Phase II.

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 subsidiary loans by MFIs (including principal, interest and fees) would be used to establish and maintain the 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 (individuals, households, micro-enterprises, and other juridical persons) to finance working capital for their viable initiatives. If needed, medium-term loans (up to three years) to finance small capital investment would also be granted. Sub-loans under this sub-component would be expected to average around US$400 for individual households and around US$1,000 for micro-enterprises (employing at least two persons outside the immediate family). IDA financing under subsidiary loans to MFIs would not exceed the equivalent of US$1 million for any individual MFI during the period of implementation, unless otherwise agreed with IDA.

On-lending Arrangements. The proceeds of the IDA credit allocated to this sub-component (Category 5, amounting to around US$3 million) would be made available directly from the Special Account to support sub-loans approved by accredited MFIs. The HLSPO would disburse and transfer (in local currency), through MDF, the amounts required to cover those sub-loans approved, in accordance to the terms of SLAs signed with the MFIs. These subsidiary loans to selected MFIs will be provided 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 local currency 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 Operational 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 IDA on: (i) the interest rates on subsidiary loans to participating MFIs; and (ii) the level of interest rates charged by MFIs on sub-loans to final sub-borrowers. This would be done twice a year, not later than March 31 and September 30 each year, commencing on March 31, 2003.

Process of MFI Accreditation. In order to safeguard the MDF's financial assets and its long-term sustainability, and to ensure a successful implementation of the micro-finance sub-component, the MFIs would be selected based on agreed accreditation criteria to be detailed in the Operational Manual. The accreditation criteria ensure that the participating MFIs pass the tests of legality, solvency, liquidity, profitability, efficiency and lending performance, ownership and management capacity. Selection would involve two steps: (a) the MFI would have to meet the requirements specified in the Operational Manual, based on a thorough evaluation of its financial performance and operations, in order to receive accreditation; and (b) once the accreditation is decided, the final credit evaluation would be based on the proposal by the MFI on how to use the project's funds to provide sub-loans to the target beneficiaries in compliance with the project's overall objectives and strategy.

In principle, the following institutions would be allowed to participate: commercial banks, joint-stock urban and rural banks, cooperatives, credit-granting NGOs, and any other financial institution interested in micro-finance activities that meets the related accreditation criteria and is legally authorized to provide loans under the existing legal framework.

Accreditation Criteria. The main criteria include the following elements:

(a) BoM Regulations. MFIs would comply with all BoM regulations, particularly those related to the review of loan portfolio and other risk assets, definition of past due loan accounts, loan classifications, and adequate provision for expected loan losses. In the case of banks, compliance with BoM's minimum capital requirements is a necessary condition for accreditation. In the case of non-banking institutions, they would have to meet other criteria as specified in the Operational Manual and provide collateral at the discretion of the MDF.

(b) Solvency Requirements. Eligible MFIs would comply with a minimum net equity base of at least 8% of their risk assets. The net equity base would be computed applying the criteria established by the Bank for International Settlements ("Basel" or BIS), at the time of accreditation. In addition, eligible MFIs would maintain a net past due over equity of not more than 25% and a Capital Adequacy Ratio (CAR), defined as equity over risk assets, of not less than 10%. The eligible cooperatives and credit-granting NGOs would maintain a net capital (or fund balances for NGOs) ratio of at least 12% of the risk assets.

(c) Liquidity. Eligible MFIs would comply with minimum liquidity ratio (liquid assets over short-term deposits and bills payable) of not less than 30%.

(d) Profitability Requirements. Eligible MFIs would demonstrate their profitability in real terms during the life of the sub-loans, measured by the Return on Equity (ROE) of return on earning assets. If their profits obtained are positive in real terms, then it would be considered that the real profitability criteria has been met.

(e) Quality of Portfolio. The eligible MFIs would have to maintain a net overdue rate of not more than 10% of the loan portfolio (where net overdue means total overdue loans less loan provisions).

(f) Ownership, Management, and staff Quality Requirement. MFI's ownership, management, and staff quality should be satisfactory to MDF. This would include qualified management team of good reputation, presence of adequate and qualified staff, sound operation policies and procedures, compliance with all relevant laws, decrees, and regulations.

If an existing MFI does not meet the criteria, it could be selected to receive technical assistance to prepare an Institutional Development Plan (IDP) and to receive adequate training, as long as it agrees on a detailed timetable for its institutional strengthening and for achieving full compliance.

In the event that a MFI already accredited loses its accreditation status (having failed to meet one or more of the accreditation criteria), then MDF would: (i) cancel the uncommitted portion of the line of credit granted to the MFI; (ii) take the necessary actions to safeguard the committed portion extended to the said MFI; and (iii) notify IDA on actions taken.

Structure of the Micro-Finance Management Office (MMO). The institutional structure of the MDF would be established prior as a condition of disbursement for the funds allocated to the sub-component. As the unit in charge of the operation of the MDF, the MMO would be responsible for implementing the sub-component in compliance with the Operational Manual. It would handle day-to-day matters related to implementation of the micro-finance sub-component and manage the resources in available in the Fund on behalf of the GoM. The MMO shall be operationally independent from the BoM and would maintain a separate account for all project activities, which would be annually audited by private independent auditors.

The MMO would have the following five key responsibilities: (i) MFIs evaluation and accreditation; (ii) appraisal of subsidiary loan proposals presented by qualifying MFIs; (iii) monitoring and evaluation of loans and sub-loans; (iv) accounting and disbursement; and (v) environmental screening. The staff of MMO would comprise a Director and a minimum of 8 permanent staff.

Sub-component 2: Strengthening of Revolving Loan Funds (RLFs). This sub-component seeks 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 financial resources to help the selected RLFs approve new sub-loans, according to their business plans, and improve their portfolio quality and financial situation; and (vi) eventual privatization of the best-performing RLFs. Those RLFs qualifying for privatization would have four options: (a) to become a savings and credit cooperative, that is legally able to offer members savings services as well as credit services; (b) to register as a NGO, along lines similar to the network of *sum* and *aimag* level NGOs that make up the Mongolian Women's Federation; under current law, they cannot legally offer savings services to potential clients; (c) to dissolve the RLF and 'graduate' clients into existing financial institutions, such as registered banks or non-banking financial institutions (NBFIs), although recognizing that there may be a reluctance on the part of banks and NBFIs to accept any but the very 'best' clients; or (d) become a fully-fledged NBFI or an accredited branch office of an existing NBFI. Once privatized, these institutions may put themselves forward for possible selection, provided they meet the qualifying criteria, as accredited MFIs eligible for loans from the MDF. **As conditions for the disbursement of IDA funds allocated to the provision of sub-loans by the selected RLFs (Category 6, for a total equivalent to about US$ 500,000), the Borrower would: (a) establish a MIS adequate to monitor micro-finance portfolio quality; and (b) prepare a detailed Action Plan for the use of these Funds, acceptable to IDA, with the objective of strengthening the selected RLFs.** 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 financing for sub-loans, the purposes and uses of these sub-loans, as well as the steps to be taken towards the eventual privatization of these RLFs.

Sub-component 3: Development of an Index-based Livestock Insurance Scheme. During the first year of the project, international and local consulting services would be financed to assist in the development of a risk index, on the basis of which eligible, participating private insurance companies would offer livestock insurance to individual herders, herding households, or other juridical persons owning livestock to cover covariant risk arising from dzud, drought, or other weather-related events. The index, based on objective, third-party verifiable indicators such as weather data, livestock mortality rates, and/or indices of range vegetation condition (e.g. a normalized, differentiated vegetation index (NDVI) derived from processing of satellite imagery), would differentiate relative risk at an appropriate level (most likely at *sum* level) based on historical data. Indemnities under the scheme would be triggered once the index exceeded a given threshold level specific to that *sum*. Insurance cover would be for productive activities including: the replacement value of livestock; the value of goods or services to support risk preparedness and/or enhance livestock productivity, such as hay and fodder production or purchase, acquisition of veterinary drugs and services, construction of livestock shelters, and breeding services; and/or the value of goods and services to allow policy-holders to engage in alternative or supplementary livelihood strategies. Payments to participating insurance companies, for claims paid to policy-holders against covered risks and for such productive activities, would be made when the aggregate amount of those claims exceeds the agreed level of liability, as specified in a stop-loss agreement between the Government and the participating insurance company. The project would also finance training workshops for participating insurance companies and public officials involved, and a nationwide information campaign to publicize the scheme and attract policy-holders. 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. The role of Government during the start-up phase of the scheme (project years 2 to 4), would be to assume liability beyond the level agreed with participating insurance companies by undertaking to finance the stop-loss payments from the proceeds of the IDA credit. This stop-loss provision would take the place of international reinsurance, which would be unlikely to be attracted until commercial viability of the scheme could be demonstrated. **Conditions of disbursement of IDA funds to finance the stop-loss amounts (Category 7, for a total equivalent to US$ 1,000,000) would be the provision of evidence to IDA that the index-based livestock insurance scheme has been established, that stop-loss agreements have been concluded between Government and any participating insurance company, that insurance policies have been issued, that one of the covered risks has occurred, and that claims under these policies have been filed.** 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.

Project Component 3 - US$ 9.16 million
Local Initiatives Fund

Guiding principles in design of the component:

- respond to the community priorities and particularly those of the more vulnerable segments in those communities;
- provide funding for both rural and peri-urban areas, with the prime focus being rural and the selected eight core *aimags*;
- build on the experience and capacity developed under the LDF and continue to support its operations nationwide during a transitional period;move the main focus for fund management and decision making from the center and *aimag* to the *sum*;

- require a compulsory community contribution of 10% to the financing of sub-projects selected under the LIF; and
- operate through an 'open menu', but one that would be 'steered' by a negative and positive list of sub-projects, with the positive list based on sub-projects that have been proven to be successful, are economically/socially 'viable', sustainable in operating/maintenance terms, and where relevant are consistent with development policies, priorities and plans.

Approach:

Component design was guided by the need to: (i) balance between regional and national initiatives; (ii) facilitate convergence between the old LDF and the new, community-driven LIF; (iii) progressively incorporate the LIF into the government budget; (iv) harmonize community-identified project priorities with government plans and policies; (v) develop effective communication strategies to ensure transparency and accountability; (vi) ensure that the projects benefit poor and vulnerable groups; and (vii) guarantee that women are actively involved in project prioritization, selection and planning.

The LIF's target group are all members of *sums* and bags in the core *aimags*. The project will be driven by the active participation of all these communities and will invest in sub-projects that have been identified, prioritized and selected by them. They will be allowed to propose projects from an 'open menu', in practice the community mobilization/ planning process will use as a guideline a 'positive list' and a 'negative list'. The negative list comprises: predominantly private economic goods that would result in establishment or rehabilitation of private assets; activities that would benefit relatively few households; activities that could have negative environmental impacts or negative social consequences; activities that would result in the rehabilitation or construction of religious facilities; and/or activities financed from other sources.

The HLSC, particularly at the *sum* level, will expend considerable resources to ensure that the sub-project identification and selection process provides accurate representation of the target communities priorities. In deciding on the combination of sub-projects to be included, *sums* will assign priority to sub-projects that:

- respond to the priority needs of the community as these are publicly articulated;
- result in the greatest benefit to the benefiting households;
- demonstrate a positive 'gender balance';
- reach the greatest number of poor/ vulnerable households;
- benefit the maximum number of households; and
- involve rehabilitation/ repair rather than new construction; and have the minimum additional recurrent cost implications and an assured method for covering these costs.

Description of investment required:

The LIF component involves three sub-components: (i) local initiatives funds, (ii) training and capacity building, and (iii) a fiscal decentralization initiative.

(i) Local Initiatives Funds. Two separate investment funding facilities would be financed under this activity: the Local Initiatives Fund (LIF) and the Local Development Fund (LDF).

The *Local Initiatives Fund* (LIF) is a new fund that will be piloted in the eight core *aimags* and one *duureg*. Financial ceilings for all *sums* participating in the first phase of the SLP have been established as follows: $8,000 for *sums* in the core aimags and $15,000 for the pilot *duureg*. These amounts will be reviewed on an annual basis by the LIF Working Group for those *sums* in the core *aimags* and may be increased based on a number of criteria such as poverty levels, implementation performance, and fund-management capacity (a detailed description of the operating guidelines is provided in the "LIF Project Implementation Manual").

Local Development Fund: The main objective of the LDF is to provide financial resources to small-scale poverty-related projects at the *sum* and *bag* level. Similar to the LIF, the key operating principle of the LDF will be to ensure community participation at the *sum, khoroo* and *bag* level in the identification of priorities and the formulation and implementation of projects. The key difference between the LDF and the LIF will be that the appraisal and approval of all LDF sub-projects will be undertaken at the *aimag* level for *sum*-level projects, and at Ulaanbaatar level, for the *duureg*-level projects. The review and approval of these sub-projects would come from the *aimag* and Ulaanbaatar Household Livelihood Support Councils. In addition, all *sums* participating in the LDF will have a financial ceiling of $4000. The policies and procedures used under the NPAP for implementation of the LDF will continue to be used for the SLP. A detailed description of the implementation guidelines is provided in the "LDF Project Implementation Manual".

The activities of the LIF component will be divided into three **phases** with durations of four years each, over the 12-year duration of the SL Program:

- ***Phase 1***: The LIF and LDF operate independently of each other during the first phase. The LDF will carry out its activities only in the 13 non-core *aimags* and eight *duuregs* while the LIF will operate only in the 8 core *aimags* and one *duureg*. In addition, during this phase a contract will be provided to a research institute to consider options for integrating the LIF into fiscal government budgets;
- ***Phase 2***: The LDF will cease to operate and its activities will be fully merged into the LIF. During this phase, pilot-testing of approaches to fiscal decentralization will begin. A decision would need to be reached prior to appraisal of Phase 2 on the proposed geographical coverage of LIF under Phase 2, but it would be intended to extend beyond the 8 core aimags, perhaps to national level; and
- ***Phase 3***: Phase 3 would see full integration of an LIF-type mechanism with regular government budgeting and planning process for activities at the *sum* and *bag* level nationwide.

Within Phase 1 of the program (i.e. the project), the LIF would be implemented in two distinct **stages**:

- ***1st Stage***: The principal objective of this first stage is to pilot the basic operations, procedures and processing involved in implementing and managing the identification, prioritization, selection, and implementation of *sum* and *bag*-level projects in two *sums* of each of the eight core *aimags*. During this period, various procedures will be tested, refined, and modified, if necessary, before full implementation of the LIF in all *sums* of the eight core *aimags*.
- ***2nd Stage***: Provided the results of the first two stages are successful, the LIF will begin to provide financing for *bag*-level, inter-*bag*, and *sum*-level projects in all 143 *sums* within the 8 core project *aimags* starting in the project's second year.

Summary of LIF Component Implementation Strategy By Phase

	PHASE I		PHASE II (4 years)	PHASE III (4 years)
	Stage 1 (1st year)	Stage 2 (3 years)		
LIF	pilot process and implementation in 2 sums from each of the 8 core *aimags and* 1 *duureg*	143 sums from 8 core aimags & 1 duureg	nationwide (LDF merges into LIF)	nationwide
LDF	13 non-core aimags and 8 *duuregs*	13 non-core aimags and 8 *duuregs*	merge with LIF & halt operations	cease to exist
Fiscal Decentralization	identify research institute/NGO to conduct action-research	begin research in 2nd year and thereafter begin action-research activities in PY3 and PY4	begin limited fiscal decentralization	integration of LIF with government budgeting

Under Phase I of the project, the LDF will continue to operate as it did under NPAP with regard to methodology and implementation in all *aimags/duuregs,* other than the 8 core *aimags* and one *duureg* in which the LIF will be piloted during Phase 1.

The project will implement the LIF in parallel with the normal budgetary process, much in the same way as the LDF operated under the NPAP. However, during the first phase of the program a number of processes will be initiated which will facilitate its transformation into a community-based funding mechanism to provide local government with discretionary funds to meet high-priority capital expenditures in the *sums* and *bags*. This will involve the following: demonstration that the *sums* can manage the identification, planning and implementation of local investment projects (through the 'parallel' LIF program), creating an enabling policy and legislative framework to permit the transfer of resources from central to local level, creating the financial capacity at *sum* level to efficiently manage and be accountable for the funds (LIF), and piloting in a few selected *sums* the operation and management of the LIF under a reformed budget procedure.

(ii) Training and Capacity Building. Because of the importance of community participation, the complexity of managing such processes successfully, and the need to build up institutional and implementing capacity of the *sums* (and *duureg*), a substantial provision has been included under this component for training and capacity building. At the beginning of the project, a training needs assessment will be carried out to provide a strategic framework for managing the component's training program. It will focus particularly on the eight core *aimags*, but will also take account of the requirements for modifying the LDF. Following its completion, a contract will be provided to assist the HLSPO in the preparation of training materials to form a LIF training manual. There will be two main sources for the drafting of this material: in the first instance, the training material currently in use for the LDF and, subsequently, experience derived during PY1 from the planning and piloting of LIF interventions in the first 16 pilot *sums* will be used to revise the manual.

Funding would be provided for workshops and capacity building on all administrative levels but with the main focus at *sum* level and below. These activities will primarily be for orientation, skills development in administration and management, study tours and exchanges, refresher training, and for the development of appropriate training material.

(iii) Fiscal Decentralization Initiative. The funds to be provided by LIF – like those provided by LDF – will represent a supplementary source of funding to local government and specifically to the *sums* and *duuregs*. The little revenue generated within the *sums/duuregs* (from fees collected and taxes levied) goes towards meeting recurrent expenditures, and at that covers on average less than one quarter of these expenditures. The rest is provided through central government transfers. In order for the project to be successful, it must demonstrate that making available discretionary funds to the *sum* level local government is an efficient and responsive way of meeting part of the demand for rural/peri-urban infrastructure.

In order to assess the potential for incorporating the LIF into the regular government budget, the project would finance a three-year, pilot action-research program to explore the modalities and options for decentralized fiscal management of capital expenditure. Eight *sums* would be involved in the process using resources generated from: (i) an increased level of local revenues and taxes; and (ii) fund allocation from the central to the *sum* level. This combination of funds would be made available to the *sum* in a similar way that recurrent expenditures are provided and accounted for.

Implementation arrangements:

There will be a LIF Coordinator within the HLSPO that would have principal responsibility for the component and would liaise with the LIF Working Group. This Working Group would be made up of senior staff from MoFE, MoSTEC, MoH, and MoSWL; two NGOs; and two ex-officio members: namely, the HLSPO Program Coordinator and the LIF Coordinator. The LIF Working Group will assist in providing overall oversight of the operations and management units at each administrative level, the most important of which will be the *sum* HLSCs. In addition, it would contribute to promote adequate cooperation and support from all the relevant line ministries in the implementation of the LIF. The MoFE's responsibility for the budget and for management of the government's finances will be key to facilitating the implementation of the component.

Implementation Responsibilities. At the **central level**, a LIF Coordinator would be located within the HLSPO that would liaise directly with the LIF Working Group. The HLSPO would be responsible for managing the funds for LIF and LDF operations and would maintain fiduciary oversight for the units at *aimag* and *sum* levels and coordinate the training programs to be financed under the component. The proposed staffing would be similar to that of PAPO for the LDF. The *aimag* HLSC, through the person of the *aimag* HLSC Secretary, will receive the list of sub-projects approved for funding by the *sum* HLSC. It will review the proposals to ascertain whether they accord with the *aimag*'s development plan and sustainable livelihoods strategy. Once the review is completed, the *aimag* HLSC secretary will: a) certify the sub-project proposals' consistency with the *aimag* development plans and sustainable livelihoods strategies; b) enter the relevant sub-project information into the MIS, updating it in the light of ongoing reports from the *sum* HSLCs; c) provide advice and assistance to the *sum* HLSCs, including mobilizing technical advice and support from *aimag* technical staff; and d) submit a compiled financial report on sub-project activities to the HLSC.

At ***sum* level**, while the selection of LIF sub-projects would be with the communities, their approval and implementation would be handled primarily by the *sums*, except for small *bag* projects that the communities themselves would manage. In this capacity, the *sum* HLSC will: mobilize the community in

support of the project; receive all sub-project proposals from the *bags*; review and approve sub-project proposals for financing; submit approved sub-project proposals to the *aimag* HLSCs for review; and oversee and manage the contracting process, including contracting with communities and contractors.

At ***bag* level**, project activities would focus on groups that would be composed of households from within the *bag*. They would be the catalyst that would develop project ideas and initiatives within the community and provide the forum in which the needs of the *bag* are debated and project ideas discussed. They would facilitate an interactive process of prioritization and ensure that the interests of the poorer members of the community are heard and reflected in the process.

LIF Project Planning Process. The LIF sub-project planning process starts in the community. At the beginning of the process, a meeting open to all members of the community would be organized at *bag* level, based on the regular *bag khural* meetings. Participation would be promoted through facilitation techniques, active dialogue and debate encouraged and people's views actively solicited. Through a process involving three or four sessions in each *bag*, sub-projects would be identified, discussed and priorities established. This process would be a guided one in which the *sum*-level team would indicate those sub-projects that cannot be included – the negative list – and those that have been successfully implemented elsewhere – in essence a 'positive list'. During this process, the community would be informed about the priorities as presented in the *sum* development plan and, in particular, the *sum* sustainable livelihoods strategy. The community would be required to identify and prioritize *bag*-level sub-projects and/or *sum*-level sub-projects. For *bag* sub-projects, the decision of the community would be expressed through the *bag* governor or citizens' representative to the *sum* HLSC. For *sum* or inter-*bag* sub-projects, there would need to be an agreement among all the *bags* in the *sum*. Once a sub-project had been ratified, a sub-project management committee would be set up either within the *bag* or within the *sum*, depending on the nature of the sub-project, and together with the *sum* HLSC, the detailed planning and preparation would take place.

The *sum* collectively with the *bag* groups would be at liberty to decide on how to allocate the LIF money to sub-projects. The full amount available within the funding ceiling could be allocated to say one *sum* sub-project and one large *bag* sub-project, or to one *sum* sub-project and a number of smaller *bag* sub-projects. This decision would be made based on the priorities of the communities and compliance with the eligibility criteria.

After the first round of sub-project investment, the ceiling would be adjusted up or down for the subsequent year based on a number of criteria, including: the performance of the *sum* (and *bags*) and adherence to sub-project goals and implementation procedures, timely completion of the sub-projects, absence of cost overruns, absence of financial management irregularities, proof that the project-supported facilities are in use and are used by poor households and women, and a positive rating on community scorecards.

The process in the LIF pilot *duureg* would be similar to that described above but due to the close proximity of the communities in *duuregs*, communication and the organization of meetings would be considerably easier than in rural *sums*. The *khoroo* would be the focus of the participatory processes in the *duureg*. It would organize the communities and facilitate the identification, prioritization, selection, planning and implementation of the sub-projects in a similar way to the *bag* in a rural context.

Project Component 4 - US$1.25 million

Project Management and Policy Support

Guiding principles in design of the component:

- establish project management as part of the regular government structure and minimize creation of new institutional entities whenever possible;
- capitalize on the experience, skills and capacity developed under NPAP and utilize their staff whenever possible at *sum*, *aimag* and central levels;
- work within those institutions that will have the long term responsibility for management of project activities and that will oversee sustainable livelihood and poverty alleviation initiatives within the country;
- decentralize decision making and responsibility for project activities to the maximum extent possible within the capacities that can be created and sustained at those levels; and
- develop the capacity to generate inputs for policy/legislative formulation/reform from the lowest level up.

Approach:

Based on these principles, the project will not establish additional project management facilities at central, *aimag*, *sum/duureg* and *bag* level. Instead, the project will employ the existing system to implement the project and will treat capacity building of the existing system as the priority. The HLSPO would serve as central PIU and undertake overall responsibility for coordination and implementation under the guidance of the National Committee on Household Livelihood Capacity Support Program and with technical assistance from the three technical Working Groups. Local government would carry the main responsibility for implementing the project through its officers (HLSC secretaries) and structures (*aimag* and *sum* HLSCs) at *aimag*, *sum* and *bag* levels.

Description of investment required:

The component would finance: (i) the operational costs of the Household Livelihoods Support Program Office (HLSPO) under the National Committee on Household Livelihood Capacity Support Program, including vehicles, equipment, recurrent costs and consulting services; (ii) technical assistance to support activities to generate proposals of policy and legal reforms identified during implementation, (iii) information dissemination/ communication, (iv) project orientation workshops and training, (vi) monitoring and evaluation, and (vii) auditing.

Implementation arrangements:

The main features of the project management structure are:

- The National Committee on Household Livelihood Capacity Support Program (ex-NPAC) will have overall responsibility for the Sustainable Livelihoods Program.
- HLSPO, as the executing office of the National Committee, will serve as the central PIU and provide capacity building, coordination, monitoring and evaluation, information dissemination, and policy guidance to project implementation.
- Three technical Working Groups will be established to provide technical and policy assistance to the HLSPO to implement the project and will be made of members of the relevant line ministries and technical specialists. The fourth component, Management and Policy Support, will be managed directly

by the Household Livelihoods Support Program Office.

- The day-to-day responsibility for implementing project activities will be with the local government, primarily though the *sum/duureg* and *aimag* Household Livelihoods Support Councils, and where appropriate, community groups.
- Communities and households within the framework of the *bags* (and the *khoroos* in the peri-urban areas) will participate in project implementation through committees and informal groups established to assist the project in formulating, prioritizing, planning and implementing project activities.

Project Implementation Manual (PIM). Detailed implementation guidelines for all aspects of the project are provided in the Project Implementation Manual (PIM). This includes separate sections dealing with: pastoral risk management, local initiatives fund, local development fund, micro-finance operational manual, revolving loan funds, environmental management plan, resettlement policy framework, ethnic minorities participation framework, financial management and reporting (including format of FMRs as an appendix), procurement (including sample documents as appendices), and monitoring and evaluation. It is a condition of effectiveness that the PIM has been finalized and adopted in a form acceptable to IDA, and that staff of the HLSPO and of the HLSCs in all *aimags* and *duuregs*, and in the 16 *sums* selected to participate in the project for the first year of activities, have completed a training course satisfactory to IDA on the provisions of the PIM.

Annex 3: Estimated Project Costs
MONGOLIA: Sustainable Livelihoods Project

Project Cost By Component	Local US $million	Foreign US $million	Total US $million
1. Pastoral Risk Management	4.52	0.86	5.38
2. Micro-Finance Outreach	5.77	0.22	5.99
3. Local Initiatives Fund	8.85	0.15	9.00
4. Management and Policy Support	0.91	0.23	1.14
Total Baseline Cost	20.05	1.46	21.51
Physical Contingencies			0.00
Price Contingencies	0.56	0.05	0.61
Total Project Costs[1]	20.61	1.51	22.12
Total Financing Required	20.61	1.51	22.12

Project Cost By Category	Local US $million	Foreign US $million	Total US $million
Goods	0.16	0.62	0.78
Works	1.82	0.37	2.19
Vehicles	0.01	0.04	0.05
Training/Services (International)	0.00	0.29	0.29
Training/Services (Local)	1.56	0.19	1.75
Micro-finance Sub-loans	4.50	0.00	4.50
Livestock Insurance Stop-loss Provision	1.00	0.00	1.00
Herder Group Sub-projects	1.92	0.00	1.92
Community Development Sub-projects	7.46	0.00	7.46
Recurrent Costs	2.18	0.00	2.18
Total Project Costs[1]	20.61	1.51	22.12
Total Financing Required	20.61	1.51	22.12

[1] Identifiable taxes and duties are 0.11 (US$m) and the total project cost, net of taxes, is 22.01 (US$m). Therefore, the project cost sharing ratio is 85.08% of total project cost net of taxes.

Annex 4: Cost Benefit Analysis Summary
MONGOLIA: Sustainable Livelihoods Project

Pastoral Risk Management Component

Summary of benefits and costs:
The benefits of pastoral risk management are reduction in *dzud*-related animal losses, which include both direct economic costs due to animal deaths and the wider economic and social costs such as reductions in cashmere and milk production resulting from animal deaths; the cost of government relief activities; disruption of schooling and other social services; and environmental costs such as tree felling caused by lack of animal dung for *ger* stoves. Total livestock losses to *dzud* since 1950 were over 36 million animals, which at current prices would have a value of US$1.27 billion. The direct benefits of the PRM component in reducing animal losses were estimated by considering the value of combined losses during the 1999/2000 and the 2000/2001 *dzud* in comparison with normal years. The two *dzud* years resulted in the loss of 7.15 million animals (22% of the national herd) at an estimated cost of US$252 million compared with average stock losses over the past 51 years *(dzud* and non-*dzud* years combined) at an average rate of 720,000 animals with a value of around US$27 million. The average annual loss for each of the two *dzud* years was US$125.8 million. When 51-year average losses are deducted, the incremental savings are US$98.5 per annum in *dzud* years.

Table 1 Estimated Value of Livestock Losses due to *Dzud*

	Total loss 1950-2001	Avg. loss 1950-2001	*Dzud* losses 1999-2001			Average losses 1999-2001	Average loss 1999-2001 less 51-yr average loss	50% loss reduction in *dzud* years due to SLP
			1999/2000	2000/2001	Total 1999-2001			
% of national herd lost		2	8.6	13.8	22.4	11.2	9.2	4.6
Animal losses (million heads)	36.17	0.72	2.98	4.17	7.15	3.58	2.86	1.43
Avg. value/lost animal MNT	38,000	38,000	38,000	38,000	38,000			38,000
Avg. value/lost animal US$	35.19	35.19	35.19	35.19	35.19			35.19
Value of stock lost million MNT	1,374,460	27,300	113,240	158,460	271,700	135,850	108,550	54,340
Value of stock lost million US$	1,273*	25	105	147	252	125.8	98.5	50

Source: *TCP/MON/0066 Pastoral Risk Management, Discussion Note No.1 - Managing the Risk of Drought and Dzud,* ***Concepts and Issues, Aug. 2001 and*** UNDP, 2000, *Lessons Learnt from the Dzud 1999-2000*, Ulaanbaatar, 2000, pp. 5-7. UNDP and FAO figures were updated by the mission to include losses during the 2001 *dzud*. * at current prices.

This suggests that, on average, if adoption of PRM nationwide (estimated at US$10 million every four years if modelled on the Phase I proposal) could cut national losses in *dzud* years (such those in 1999/2000 and 2000/2001) to those of normal years, Mongolia would save an average of nearly US$100 million per year in *dzud* years. If we assume that *dzud* occurs one year in every five, the PRM component would easily pay for the entire project (US$20 million). If adoption of PRM were to reduce losses in *dzud* years by 50% on average, Mongolia would save around US$50 million per year during *dzud* years. If *dzud* were to occur only once in 10 years, the savings would still cover entire the cost of the PRM component (nationwide cost for ten years would be around US$22 million). The time-series data cited in Templer, Swift and Payne (' The changing significance of risk'. *Nomadic Peoples* 33: 1993) since 1944 suggest that a *dzud* was declared in one or more *aimags* of Mongolia in 26 of the 56 of years, although major losses involving many *aimags* occurred on average only once in 10 years.

Potential production of raw cashmere that was lost during the 1999/2000 *dzud* amounted to more than 130 tons, valued at about US$5 million. The poor 2001 season, on top of the poor 2000 season, means that goat

stocks were almost 2 million down on the figure that would have been reached if seasons had been normal. The loss in potential cashmere in 2001 amounted to about 240 tons, which has a value of the order of US$10 million. These estimates do not include indirect costs, which are virtually impossible to quantify. The implication of this very rough analysis is that if planned PRM can reduce the economic costs by a fairly small proportion, it is likely to be economically viable.

Table 2 Effects of Poor 2000 and 2001 Seasons on Cashmere Production

	1998	1999	2000	2001	2002 (b)
Number of Goats '000 (a)	11061.9	11033.9	10230.9	9500.0* (e)	9758.9
Breeding Females '000 (a)	4890.3	4835.2	4483.3* (e)	4163.0* (e)	4257.8
Raw Cashmere Produced (tons) (c)	3126.7	3194.8	3088.2	3005.7	2961.7
Estim. production in normal season (tons)			3219.4	3249.6	
Potential Raw Cashmere lost in Poor Season (tons) (d)			131.2	243.9	
% fall in herders' income compared to normal season (f)			-4.2%	-8.1%	

Source: Filmer, Richard J., The Mongolian Cashmere Industry, Aug. 2001 (p. 29).
Notes: * = estimation
(a) Except where indicated otherwise, figures are Census figures for December
(b) Figures for 2002 are estimated on assumption that 2002 has seasons similar to 1998-1999
(c) Raw Cashmere produced has been estimated based on the goat population in April classified by age and multiplied by yield/age ratios. The production figure includes an allowance for cashmere derived from skins.
(d) Cashmere lost has been estimated by running the goat model for 2000 and 2001 on the assumption of seasonal conditions similar to 1998-1999 and subtracting the actual cashmere produced from these implied estimates.
(e) Estimates based on discussions with Professor Zagdsuren, Mongolian Research institute of Animal Husbandry
(f) Note that herder income rose between 1999 and 2000 because of increased prices

Main assumptions:

(a) for estimated value of livestock losses, the average cost per head of livestock of MTG 38,000 (US$35.19) was obtained by dividing total value of losses reported by UNDP by total animals lost (US$1=1090 MTG).

(b) for estimated value of cashmere lost, see Filmer (above).

Sub-component 1.4: Hay and Fodder Enterprise Development

Economic Rates of Return for indicative business models for hay and fodder enterprises using alternative technologies are as follows:

Table 3. Haymaking (Tractor unit, rain-fed model, 1400 ha)
In 000' MNT

	Year1	Year2	Year3	Year4	Year5	Year6	Year7	Year8	Year9	Year10-17
Revenue	14,000	14,000	14,000	14,000	14,000	14,000	14,000	14,000	14,000	14,000
Yield	700	700	700	700	700	700	700	700	700	700
Price/kg	0.02	0.02	0.02	0.02	0.02	0.02	0.02	0.02	0.02	0.02
Other income*	1,000	1,000	1,000	1,000	1,000	1,000	1,000	1,000	1,000	1,000
Investment										
Land use fee	700	700	700	700	700	700	700	700	700	700
Tractors	36,000									
Mower	5,000									
Rake	1,500									

Baler	6,500									
Operating Costs										
Fuel	5,544	5,544	5,544	5,544	5,544	5,544	5,544	5,544	5,544	5,544
Machine maintenance	50	50	150	50	150	50	50	150	50	150
Labor**	480	480	480	480	480	480	480	480	480	480
Income	-40,774	8,226	8,126	8,226	8,126	8,226	8,226	8,126	8,226	8,126
IRR	18%									

Notes: * Tractors for transportation; ** labor valued at MNT 2000/person day.

Table 4. Haymaking (Tractor unit, 200 ha)
In 000' MNT

	Year1	Year2	Year3	Year4	Year5	Year6	Year7	Year8	Year9	Year10-17
Revenue	8,000	8,000	8,000	8,000	8,000	8,000	8,000	8,000	8,000	8,000
Yield	400	400	400	400	400	400	400	400	400	400
Price/kg	0.02	0.02	0.02	0.02	0.02	0.02	0.02	0.02	0.02	0.02
Other income*	1,000	1,000	1,000	1,000	1,000	1,000	1,000	1,000	1,000	1,000
Investment										
Land use fee	100	100	100	100	100	100	100	100	100	100
Tractors	24,000									
Mower	2,500									
Rake	1,500									
Baler	6,500									
Operating Costs										
Fuel	528	528	528	528	528	528	528	528	528	528
Machine maintenance	50	50	150	50	150	50	50	150	50	150
Labor**	120	120	120	120	120	120	120	120	120	120
Income	-26,298	8,202	8,102	8,202	8,102	8,202	8,202	8,102	8,202	8,102
IRR	30%									

Notes: * Tractors for transportation; ** labor valued at MNT 2000/person day.

Table 5. Haymaking (Horse drawn, 45 ha)
In 000' MNT

	Year1	Year2	Year3	Year4	Year5	Year6	Year7	Year8	Year9	Year10-15
Revenue	450	450	450	450	450	450	450	450	450	450
Yield	22.5	22.5	22.5	22.5	22.5	22.5	22.5	22.5	22.5	22.5
Price/kg	0.02	0.02	0.02	0.02	0.02	0.02	0.02	0.02	0.02	0.02
Investment										
Land use fee	22.5	22.5	22.5	22.5	22.5	22.5	22.5	22.5	22.5	22.5
Horses	500			200			200			
Mower	650									
Rake	350									
Operating Costs										
Machine maintenance			50			50	50			50
Labor*	60	60	60	60	60	60	60	60	60	60
Income	-1,133	367.5	317.5	167.5	367.5	317.5	117.5	367.5	367.5	317.5
IRR	22%									

Notes: * labor valued at MNT 2000/person day.

Table 6. Fodder Production (Concentrates)
In 000' MNT

	Year1	Year2	Year3	Year4	Year5	Year6	Year7	Year8	Year9	Year10
Revenue	11,700	11,700	11,700	11,700	11,700	11,700	11,700	11,700	11,700	11,700
Yield	90	90	90	90	90	90	90	90	90	90
Price/kg	0.13	0.13	0.13	0.13	0.13	0.13	0.13	0.13	0.13	0.13
Investment										
Building rehabilitation	2,500									
Grinder	8,500									
Mixer	5,000									
Operating Costs										
Wheat barn	3,960									
Straw	1,584									
Cracked wheat	1,975									
Minerals/salt	99									
Electricity	450	450	450	450	450	450	450	450	450	450
Machine Maint.		40	40	40	40	40	40	40	40	
Labor*	450	450	450	450	450	450	450	450	450	450
Income	-12,818	10,760	10,760	10,750	10,760	10,760	10,750	10,760	10,760	10,800
IRR	61%									

Notes: * labor valued at MNT 2000/person day.

Micro-Finance Outreach Component

Economic Rates of Return for some representative production activities eligible for MFO component support are as follows:

Table 7. Ger Felt Cover
In 000' MNT

	Year1	Year2	Year3	Year4	Year5	Year6	Year7	Year8	Year9	Year10
Revenue	1,000	2,000	2,000	2,000	2,000	2,000	2,000	2,000	2,000	2,000
Investment										
Equipment	1,100									
Operating Costs										
Materials	1,000	1,000	1,000	1,000	1,000	1,000	1,000	1,000	1,000	1,000
Labor*	200	200	200	200	200	200	200	200	200	200
Income**	-1,300	800	800	800	800	800	800	800	800	800
Income***	-1,500	600	600	600	600	600	600	600	600	600
IRR**	61%									
IRR***	38%									

Notes: * labor valued at MNT 1000/person day; ** before family labor; *** after family labor.

Table 8. Saddle Making
In 000' MNT

	Year1	Year2	Year3	Year4	Year5	Year6	Year7	Year8	Year9	Year10
Revenue	450	550	550	550	550	550	550	550	550	550
Investment										
Equipment	500									
Operating Costs										
Materials	200	200	200	200	200	200	200	200	200	200
Labor*	80	80	80	80	80	80	80	80	80	80
Income**	-330	270	270	270	270	270	270	270	270	270
Income***	-410	190	190	190	190	190	190	190	190	190
IRR**	81%									
IRR***	45%									

Notes: * labor valued at MNT 1000/person day; ** before family labor; *** after family labor.

Table 9. Shoe Making
In 000' MNT

	Year1	Year2	Year3	Year4	Year5	Year6	Year7	Year8	Year9	Year10
Revenue	900	1,100	1,100	1,100	1,100	1,100	1,100	1,100	1,100	1,100
Investment										
Equipment	800									
Operating Costs										
Materials	500	500	500	500	500	500	500	500	500	500
Labor*	100	100	100	100	100	100	100	100	100	100
Income**	-500	500	500	500	500	500	500	500	500	500
Income***	-600	400	400	400	400	400	400	400	400	400
IRR**	100%									
IRR***	66%									

Notes: * labor valued at MNT 1000/person day; ** before family labor; *** after family labor.

Table 10. Vegetable Preserves
In 000' MNT

	Year1	Year2	Year3	Year4	Year5	Year6	Year7	Year8	Year9	Year10
Revenue	950	1,200	1,200	1,200	1,200	1,200	1,200	1,200	1,200	1,200
Investment										
Equipment	1,800									
Operating Costs										
Materials	300	300	300	300	300	300	300	300	300	300
Labor*	80	80	80	80	80	80	80	80	80	80
Income**	-1,230	820	820	820	820	820	820	820	820	820
Income***	-1,310	740	740	740	740	740	740	740	740	740
IRR**	66%									
IRR***	55%									

Notes: * labor valued at MNT 1000/person day; ** before family labor; *** after family labor.

Annex 5: Financial Summary
MONGOLIA: Sustainable Livelihoods Project

Years Ending
2006

	IMPLEMENTATION PERIOD						
	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7
Total Financing Required							
Project Costs							
Investment Costs	4.0	5.4	5.7	4.8	0.0	0.0	0.0
Recurrent Costs	0.4	0.6	0.6	0.6	0.0	0.0	0.0
Total Project Costs	4.4	6.0	6.3	5.4	0.0	0.0	0.0
Total Financing	4.4	6.0	6.3	5.4	0.0	0.0	0.0
Financing							
IBRD/IDA	3.7	5.1	5.4	4.6	0.0	0.0	0.0
Government	0.5	0.6	0.4	0.4	0.0	0.0	0.0
Central		0.0	0.0	0.0	0.0	0.0	0.0
Provincial	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Co-financiers	0.0	0.0	0.0	0.0	0.0	0.0	0.0
User Fees/Beneficiaries	0.2	0.3	0.5	0.4	0.0	0.0	0.0
Other	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total Project Financing	4.4	6.0	6.3	5.4	0.0	0.0	0.0
Other	0.0	0.0	0.0	0.0	0.0	0.0	0.0

Main assumptions:

Annex 6: Procurement and Disbursement Arrangements
MONGOLIA: Sustainable Livelihoods Project

Procurement

1. **The Bank's Guidelines** The Bank's "Guidelines: Procurement under IBRD Loans and IDA Credits" (January 1995 revised in January, August 1996, September 1997 and January 1999) and "Guidelines: Selection and Employment of Consultants by World Bank Borrowers" (January 1997, revised September 1997 and January 1999) will govern all Bank-financed procurement.

2. **Procurement Features**

(i) **Decentralized Procurement Activities**. Due to the scattered locations and staggered implementation schedules of project activities, each participating *aimag* and *sum* HLSC would undertake its own procurement for civil works and goods except for vehicles, office equipment, and other equipment which can be packaged together for centralized procurement. The roles and functions of the Household Livelihoods Support Program Office (HLSPO) with respect to procurement management are: (a) to manage all procurement under NCB and international shopping, (b) to manage all consultant services required under each component of the project; (c) to supervise procurement work handled at *aimag* and *sum* levels; (d) to organize and provide procurement training; (e) to coordinate and update the procurement plan and prepare procurement reporting; and (f) to provide other support to *aimags* and *sums* if needed. All procurement documents subject to the Bank's prior review will be sent to the Bank through HLSPO. The procurement profile is shown in Table A.

(ii) **Annual Program Approach**. Given the phased program approach to project implementation, only the procurement plan for the first year has been prepared. The plans for other years will be prepared and submitted to the Bank for its no objection by June 30 in each subsequent year of the project. Under the Local Initiatives Fund Component, annual project activities would be selected and approved by local communities based on their priorities in accordance with the principles and methodologies agreed at appraisal and as stipulated in the PIM. While a precise plan for this component cannot be prepared in advance, a sample procurement plan for the major expected activities has been prepared and will serve as guidance for local HLSCs during project implementation.

(iii) **Procurement Documents.** The Bank's Standard Request for Proposals (SRFP) including Form of Evaluation Report (SFEP) for Selection of Consultants will be used where applicable. Other sample documents have been developed by the HLSPO with the approval of the Bank and are found as attachments to the Project Implementation Manual (PIM), including: National Competitive Bidding (NCB), International Shopping (IS), National Shopping (NS), a simple Request for Quotations for Procurement of Small Works (SW), and sample documents to guide selection according to Consultants' Qualifications (CQ) and Individual Consultants (IC). The acceptability of these sample documents will be confirmed when the final version of the PIM is reviewed and adopted prior to Credit effectiveness.

3. **Procurement Packaging**. Due to the scattered locations of project activities and phased project implementation, the majority of works and low-value equipment which are available on the local market at competitive prices would not be suitable for large packaging. They would therefore be purchased locally. Vehicles and other relatively high-value items of equipment which are not available on the local market or for which quality cannot be guaranteed would be packaged together for centralized procurement across different *sums* and different years for optimum procurement results. HLSPO was advised at appraisal that

vehicles and office equipment may be purchased directly from IAPSO, but HLSPO prefers to use international shopping for the purchase of vehicles and office equipment.

4. **Procurement Capacity Assessment**. A procurement capacity assessment was carried out during project pre-appraisal in November 2001 and updated at appraisal in March 2002. The assessment identified the following weaknesses: (1) a lack of qualified procurement staff at each level; (2) absence of a detailed procurement training plan; (3) the respective roles and functions of HLSPO and *aimag* and *sum* HLSCs are insufficiently defined; (4) the quality-control system is inadequate; and (5) the MIS requires upgrading. The above weaknesses were judged to lead to high project risk if not properly addressed prior to credit effectiveness. In order to minimize the potential risks and ensure smooth project implementation, the following action plan was proposed at pre-appraisal and agreed at appraisal:

(a) HLSPO staff will be increased from 8 to 16, and one part-time staff member in the sum-level Household Livelihoods Support Council (HLSC, formerly 'Poverty Alleviation Council') will be converted to full-time equivalent. New staff shall be recruited as early as possible before effectiveness so as to be able to train them and ensure full operational capability at effectiveness, and to assist in carrying out those actions to be completed by negotiations. All HLSPO essential staff should be recruited and the office should be operational as a condition of effectiveness. This "core" staff includes a coordinator for each of the main components, a disbursement officer, an accountant, and the procurement officer. The procurement officer should have an engineering background and at least three years work experience in procurement procedures.

(b) It has been agreed that all project staff will be recruited with levels of salaries competitive in the local market, in order to ensure that high-caliber staff can be selected to ensure accountability and to avoid the possible mismanagement of funds. All staff will be under fixed-term consulting contracts (since they are not civil servants) and their salaries would be financed from the proceeds of the IDA Credit from the consulting services category.

(c) The roles and functions of HLSPO would be: (a) to manage all procurement under NCB and international shopping procedures; (b) to manage all consultant services required under the project; (c) to guide and supervise procurement work handled at *aimag/ sum* level (national shopping, small works, community participation, and direct contracting); (d) organize various trainings; (e) prepare and update the procurement plan and procurement reporting; and (f) provide assistance and technical support in procurement aspects to *aimag* and *sum* HLSCs when needed.

(d) A procurement training workshop for staff of HLSPO and *aimag* and *sum* HLSCs will be organized immediately after project negotiations, consistent with the overall project training plan. Training will include procurement of goods, works, and consultant services. The World Bank Resident Mission in Ulaanbaatar will provide assistance the organization of the course, supported by Bank staff and consultants, if needed.

(e) Sample contract documents for NCB, CQ/IC, small civil works, and IS/NS for goods, in a form acceptable to the Bank, will be included in the Project Implementation Manual (PIM) and will serve as guidance for *aimag* and *sum* HLSCs in carrying out small civil works procurement and shopping procurement for goods, and for HLSPO staff for consultant selection and NCB procurement.

(f) For quality-control purposes, it was agreed that a technical group would be established at *aimag* level to help prepare technical specifications for works and conduct quality inspection and provide technical advice during contract implementation. This should be done by project effectiveness.

(g) Vehicles and office equipment required by HLSPO and *aimag* and *sum* HLSCs such as computers, printers, and copy machines are included in the procurement plan and would be financed from the proceeds of the IDA Credit. As agreed at appraisal, GoM may take up the option of retroactive financing for these goods up to a ceiling of $100,000, to be procured under procedures acceptable to the Bank, at any time between the start of appraisal (February 25, 2002) and the date of effectiveness.

(h) HLSPO would hire a consultant to develop the software for the project MIS. Draft TORs for this assignment should be submitted to the World Bank for review.

(i) At appraisal, HLSPO was advised that vehicles and office equipment may be directly purchased from UNDP's IAPSO, often at lower cost. However, HLSPO prefers to use international shopping to purchase vehicles and office equipment.

(k) A Procurement Plan needs to be updated periodically based on the format and activities which were agreed with the Bank for each component of the Project.

5. Procurement Arrangements

A. Procurement of Works. Civil works worth about US$ 11.32 million would be required for the project to support the rehabilitation of wells and irrigation schemes and the construction or rehabilitation of storage facilities under the Pastoral Risk Management component, and to finance public goods such as the rehabilitation of schools, health centers, repair of rural roads and bridges and other public facilities agreed under the Local Initiatives Fund/Local Development Fund component. Since all works would be geographically scattered over 143 *sums* in the eight core *aimags,* and would be spread over four years with only a very short summer construction season each year, they are not anticipated to be of interest to foreign contractors. The largest contract is not expected to exceed US$ 100,000. Therefore, no ICB is expected.

(i) National Competitive Bidding (NCB). The works for rehabilitation of irrigation schemes under the Pastoral Risk Management component, with an estimated cost of no more than US$ 100,000 equivalent per contract up to aggregate amount of about US$ 0.21 million, would be procured and awarded contract in accordance with NCB procedures acceptable to the Bank.

(ii) Small Civil Works Procurement. Works costing less than US$ 30,000 equivalent per contract up to an aggregate amount of US$ 6.95 million would be suitable for lump-sum and fixed-price contracts awarded on the basis of quotations obtained from at least three qualified and in response to a written invitation advertised locally. These include aggregate amounts of about US$1.72 million for the PRM component and around US$5.23 million under the LIF/LDF component.

(iii) Community Participation. These include small works with an estimated cost of less than US$ 5,000 per assignment up to an aggregate amount of US$ 4.16 million, which are labor-intensive and do not require professional contractors (such as the repair of school facilities or rural roads), and for which procurement would be carried out using Community Participation procedures. Under such arrangements, communities would purchase materials from local markets and mobilize the labor required to undertake the works. Following the completion of works, the technical group established at *sum* evel would conduct final inspection and certify completion to an acceptable standard. These include about US$1.92 million under the Herders Groups component, and around US$2.24 million under the LIF/LDF component.

B. Procurement of Goods. Goods worth about US$ 1.3 million would be required for the project.

(iv) International Shopping. Goods such as vehicles, office equipment, agricultural and weather forecasting equipment and other high-value items of equipment up to an aggregate amount of around US$ 750,000 ($730,000 of various goods and $19,000 for vehicles) for which estimated cost per contract is less than US$ 100,000 and which are not available on local markets, would be procured through international shopping in accordance with procedures set out in the Bank Guidelines. HLSPO will be responsible for international shopping with the participation of *aimag* and *sum* HLSCs.

(v) National Shopping. Goods such as furniture for schools, health centers, and other low-value items of equipment required under the project, including one vehicle for use by HLSPO, for which estimated cost per contract is less than US $30,000 up to an aggregate amount of US$ 69,000 (of which $28,000 are vehicles) and which are available on local markets at competitive prices, would be procured through national shopping procedures as required in the Bank Guidelines. All shopping contracts will require at least three price quotations. *Aimag* and *sum* HLSCs would organize national shopping procurement under the guidance of HLSPO; in the case of the vehicle, HLSPO would be directly responsible.

C. Consultant Services. Consultant Services and training worth a total of around US$ 3.5 million are required for carrying out research, technical assistance, project management, project monitoring and evaluation, auditing, development of the MIS, and other assignments. Training is closely linked with the consulting services and would form an integral aspect of the Terms of Reference for consultant contracts. In a number of areas, including the technical assistance and training activities envisaged under the Pastoral Risk Management component, and training in participatory learning and action methods for project monitoring and evaluation, there are sufficient numbers of qualified local firms and individuals. Under such circumstances and where contracts are small, and competition including international consultants is not justified, short-lists comprising entirely local firms or individuals would be acceptable. However, if any qualified foreign firm has expressed interest it shall not be excluded from consideration.

(vi) Quality- and Cost-Based Selection (QCBS). For larger assignments for which consultants would be hired as a firm, such as the employment of an auditing firm, and for the development of a training strategy, the "Quality- and Cost-Based Selection" (QCBS) procedure would be used. All consulting assignments over US$200,000 would be advertised in the United Nations' Development Business to seek expressions of interest.

(vii) Selection Based on Consultant's Qualifications (CQ). For those assignments for which contracts with firms are small (less than US$100,000), such as the assignments concerning the preparation of grazing management plans and application of pasture tenure instruments, conducting of training of trainers, ecological control of rodents, and other small assignments, "Selection Based on Consultant's Qualifications" (CQ) procedures would be used, for a total amount of US$ 1.18 million. Owing to the need for distinct sets of skills and experience, and for services to be delivered in widely dispersed locations and at different times, the grouping of such contracts into larger packages suitable for QCBS is impracticable.

(viii) Individual Consultants. Individual consultants for project management, supervision, and preparation of training materials, including staff of HLSPO such as accountants, financial management staff, or M&E staff, up to an aggregate of around US$ 2.03 million, would be employed in accordance with the procedures applicable to individual consultants under the Bank Guidelines.

(ix) Single-Source Selection. For those assignments which meet single-source selection criteria set out in the Bank Guidelines, single-source selection may be used with the prior approval of the Bank. It is expected that single-source selection may be used for consulting services which require continuity of contracts or for which unique skills and experience of exceptional worth are required. At appraisal the following such circumstances were foreseen: design of the index-based livestock insurance scheme under the Micro-Finance Outreach component; support for the organizational strengthening of herder self-help groups under the Pastoral Risk Management component; and training in participatory learning and action methods for project monitoring and evaluation under the Project Management and Policy Support component. All those contracts would be under US$50,000 per contract, with an aggregate amount estimated to be not more than US$150,000.

D. Micro-Finance Sub-Loans. Some US$ 4.5 million would be provided as loans to financial intermediaries, to be on-lent as sub-loans to individual clients (households and micro-enterprises) for financing small productive enterprises. The maximum size of each sub-loan would be US$ 400 to individual clients and US$ 1,000 for micro-enterprises, for which centralized procurement is not required. Procurement of goods, works, and/or services under this component would be carried out by each individual client in accordance with usual private-sector commercial practices.

E. Incremental Operating Costs. For goods required for purposes of incremental operation under the project, including vehicle operation and maintenance; small items of office equipment, consumables, and stationery; hire of meeting rooms and other direct costs associated with workshops, up to a total amount of US$ 480,000, procurement under the Borrower's usual commercial practices would be used with due observance of the principle of efficiency.

6. Bank Review. (i) Prior Review: Since most contracts under the project are small and scattered across 143 *sums*, it would not be cost effective to conduct prior review for a high percentage of contracts. However, to ensure compliance with Bank requirements, it was agreed that that all goods and works contracts above US$30,000 per contract and the first two small civil works contracts (below $30,000) for each *aimag* in the first year would be subject to the Bank's prior review. All consultant contracts over US$ 50,000 for both firms and individuals are subject to the Bank prior review. In addition, all TORs and justification for single-source selection would also be subject to Bank prior review. The total value of contracts subject to prior review is estimated to be around US$ 3.03 million. **(ii) Post Review:** All other contracts which are not subject to prior review would be subject to ex-post review by supervision missions or ex-post review missions. The sampling ratio for ex-post review would be one out of every five contracts under the project. The first ex-post review mission would be arranged at the end of the first year of project implementation. Details are provided in Table B.

7. Procurement Reporting and Supervision. A procurement filing system would be established at each level under the project MIS system. Procurement reporting will be provided to the Bank on a quarterly basis according to the format developed at appraisal. The frequency of procurement supervision missions is proposed to be one every six months including ex-post procurement review/audits.

Procurement methods (Table A)

Table A: Project Costs by Procurement Arrangements
(US$ '000)

Expenditure Category	NCB	Method Other *	Consulting Services	N.B.F.	Total Cost
1. Works	210 (189)	6,949 (6,510)		254	7,413 (6,699)
2. Goods		820 (712)			820 (712)
3. Consulting Services and Training		150 (141)	1,900 (1,817)		2,050 (1,958)
4. Community Participation (under Herder Group and LIF/LDF Sub-projects)		4,160 (3,085)			4,160 (3,085)
5. Micro-Finance Sub-loans		4,500 (3,521)			4,500 (3,521)
6. Livestock Insurance Stop-Loss Provision		1,010 (1,010)			1,010 (1,010)
7. Incremental Operating Costs		480 (380)	1,451 (1,364)	249	2,180 (1,744)
Totals	210 (189)	18,058 (15,359)	3,352 (3,181)	503	22,123 (18,729)

Note: Figures in parentheses are the amounts to be financed by the IDA credit. All costs include contingencies.

* Other Methods includes the following (in thousand dollars):

1. Works: Small civil works: $1,723 under Pastoral Risk Management component and $5,226 under LIF component
2. Goods (including vehicles): International shopping: $751; and National shopping: $69
3. Consulting services: Single source selection of consultants: $150
4. Community Participation: Herder Groups sub-projects: $1,920; and under LIF/LDF: $2,240
5. Micro-finance sub-loans: private-sector commercial practices: $4,500
6. Livestock insurance stop-loss provision: private-sector commercial practices: $1,000
7. Incremental operating costs: private-sector commercial practices $480.

Table A1: Consultant Selection Arrangements (optional)
(US$ million equivalent)

Consultant Services Expenditure Category	Selection Method							Total Cost[1]
	QCBS	QBS	SFB	LCS	CQ	Other	N.B.F.	
A. Firms	0.29 (0.28)	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)	1.18 (1.11)	0.00 (0.00)	0.00 (0.00)	1.47 (1.39)
B. Individuals	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)	2.03 (1.93)	0.00 (0.00)	2.03 (1.93)
Total	0.29 (0.28)	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)	1.18 (1.11)	2.03 (1.93)	0.00 (0.00)	3.50 (3.32)

1\ Including contingencies

Note: QCBS = Quality- and Cost-Based Selection
QBS = Quality-based Selection
SFB = Selection under a Fixed Budget
LCS = Least-Cost Selection
CQ = Selection Based on Consultants' Qualifications
Other = Selection of Individual Consultants (under Section V of Consultants Guidelines). NB. This includes an allocation of $1.4 mn for HLSPO/HLSC staff costs.
N.B.F. = Not Bank-financed
Figures in parenthesis are the amounts to be financed by the Bank Credit.

Prior review thresholds (Table B)

Table B: Thresholds for Procurement Methods and Prior Review*

Expenditure Category	Contract Value Threshold (US$ thousands)	Procurement Method	Contracts Subject to Prior Review (US$ thousands)
1. Works	<$100	NCB	>$30; All ($210)
	<$30	Small Works	>$5; 2 per *aimag* in yr 1 ($400)
	<$5	Community Participation	N.A.
2. Goods	<$100	IS	>$30; All ($750)
	<$30	NS	N.A.
3. Services	Firms: >$100	QCBS	>$100; All ($290)
	Firms: <$100	CQ/ Sole-Source	>$50 and single source; All ($1,180)
	Individual Consultants	Individual Consultants	>$50; ($200)

* Total value of contracts subject to prior review: US$ 3.03 million

Disbursement

Allocation of credit proceeds (Table C)

Disbursements from the IDA Credit would be made on the traditional system: from the Special Account with reimbursements made based on full documentation or against Statements of Expenditure (SOE) and direct payments from the Credit Account. Disbursement of the proceeds of the Credit would be made against the categories shown in Table C below.

Table C: Allocation of Credit Proceeds

Expenditure Category	Amount in US$million	Financing Percentage
1. Works	1.75	80%
2. Goods (including vehicles)	0.71	100% of foreign expenditures, 100% of local expenditures (ex-factory cost) and 87% of local expenditures for other items procured locally
3. Consulting services (including training)	3.32	94%
4. Herder group sub-projects	0.96	100% of amounts disbursed
5. Micro-finance sub-loans	3.01	100% of amounts disbursed
6. RLF sub-loans	0.51	100% of amounts disbursed
7. Livestock insurance stop-loss provision	1.01	100% of stop-loss amounts under eligible claims specified in livestock insurance policies and stop-loss agreements
8. Community development sub-projects (LIF)	3.57	100% of amounts disbursed
9. Community development sub-projects (LDF)	3.51	100% of amounts disbursed
10. Incremental Operating Costs*	0.38	73%**
Total Project Costs	18.73	
Total	18.73	

* Incremental operating costs include: office equipment and consumables, vehicle operation and maintenance, and hire of meeting rooms. ** Average over 4 years of project. Recurrent costs calculated on a declining basis as follows: 85% in Year 1, 80% in Year 2, 70% in Year 3, and 60% in Year 4.

Use of statements of expenditures (SOEs):

Disbursements would be made on the basis of Statement of Expenditures (SOEs) for: (i) incremental operating costs; (ii) actual expenditures against sub-project financing below US$ 30,000 equivalent; (iii) works contracts below US$ 30,000 equivalent; (iv) goods and equipment contracts below US$ 30,000 equivalent; and (v) consultant contracts for individuals and for local training below US$ 50,000 equivalent and for firms below US$ 100,000 equivalent.

For expenditures incurred on the basis of SOEs, all records and supporting documentation for those SOEs will be maintained by HLSPO, HLSCs and other relevant project implementation units for review by the Bank and by independent auditors. Contracts above these limits will be fully documented upon request for withdrawal.

Disbursements for works and equipment would be based on physical completion declared in the Project Implementation Manual and certified by the *aimag* and *sum* HLSCs, the contractor (where applicable) and the supervising engineer. Disbursements for equipment would be 100% of C.I.F. costs for imported items and 100% of ex-factory cost for locally purchased items. Expenditures for training and consulting services would be reimbursed at 94%, consistent with the Standard Disbursement Percentage (SDP) recently agreed for the Mongolia country program. Operating expenses other than government staff salaries would be reimbursed at 90%.

Special account:

To facilitate timely project implementation and disbursements, HLSPO, under MoFE's authority and permission, will establish and operate a Special Account at a commercial bank acceptable to the Bank, under terms and conditions acceptable to the Bank. The account would be denominated in US dollars, with an authorized allocation of US$ 1,500,000. Partial advances shall be made with an initial deposit of US$ 500,000. However, the authorized allocation shall be limited to US$ 500,000 until disbursements and outstanding commitments against the Credit equal or exceed SDR 2,000,000 (US$ 2,497,240 equivalent). The special account will be replenished monthly to ensure liquidity of funds, and all replenishment applications will be accompanied by bank statements from the depository bank showing all transactions during the month and the statement of Bank Reconciliation.

Attachment: Financial Management Assessment Summary

A review of the Financial Management System for the proposed project was carried out by Bank staff during pre-appraisal in November 2001 and updated at appraisal in March 2002. The full Financial Management Assessment Report is held on file. The assessment concluded that the project would meet minimum Bank financial management requirements subject to the following being implemented: (1) strengthening controls and procedures to cope with decentralization through designing reporting and monitoring features to track and verify the use of the project proceeds and flow of funds at each level; (2) strengthening oversight and audit functions along the line from central level through provincial and district levels; (3) upgrading the existing accounting system and software as well as equipment and staff capacity; (4) improving the reporting system to report regularly and more frequently in an agreed format that assists management in timely monitoring and decision-making; and (5) finalizing the project Financial Management Manual as part of the Project Implementation Manual (PIM) and providing training to project staff.

Country Issues. The World Bank has not to date prepared a Country Procurement Assessment Report (CPAR) for Mongolia. The Bank-financed Fiscal TA Project aims to assist Mongolia in developing an efficient and transparent public financial management system. Annual audits for several IDA credits were supported under this TA project during fiscal 2000 with a view to upgrading local capacity in auditing. The Asian Development Bank (ADB) assessed country-level financial management issues in its report, "Financial Management and Governance Issues in Mongolia", with a particular focus on accounting and auditing arrangements and practices, and governance arrangements in the country. This assessment identifies deficiencies and provides recommendations to address these deficiencies. ADB has also actively supported the improvement of accounting and auditing systems in Mongolia since 1996. The "Improving Accounting and Auditing Systems" TA project, for example, included the preparation of a training manual for accountants, an auditing manual, and a draft audit law.

Country Financial Accountability Assessment (CFAA). A draft CFAA has been prepared for Mongolia, and is in the final stage of completion. The draft identifies the following sources of risk in financial accountability at the country level: (i) budget fragmentation, including off-budget funds; (ii) settlement of

transactions primarily in cash rather than electronic transfer; (iii) insufficient control over the number of bank accounts held by budget entities; (iv) accuracy of financial reporting is poor; (v) Government auditors do not certify the financial statements of entities they have audited; (vi) there is inadequate public disclosure concerning policy matters; and (vii) private-sector accountability is also incomplete, notably in accounting and auditing standards. Overall, there is clearly a measure of fiduciary risk in the use of public resources at the country level, particularly given that the budget process is not yet transparent and public access to government financial information is limited. At the level of the Sustainable Livelihoods Project, however, funding will be on-budget, and fiduciary risk is considered to be manageable provided the actions identified in the financial management action plan (see below) are completed in a timely manner. Government has also committed to addressing some of the above country-level weakness in the context of the Public Expenditure Review (PER) that is nearing completion.

Implementing Entity. The proposed project would be implemented by the Household Livelihoods Support Program Office (HLSPO), the same implementing agency responsible for the previous IDA-financed Poverty Alleviation for Vulnerable Groups Project (Cr. 2760-MN) and the Sustainable Livelihoods Trust Fund. The HLSPO, previously named the Poverty Alleviation Program Office (PAPO), will be responsible for overall project financial management activities including planning and budgeting, preparing consolidated the financial statements and progress reports, and ensuring a smooth flow of funds to their respective project activities. It will manage the project's Special Account and maintain a local currency account and ensure their timely replenishment including preparation of statements of expenditure and reimbursement claims. It will monitor and train *aimag* and *sum* financial staff in project accounting procedures and financial operations.

HLSPO will have two divisions: (1) Program Implementation Coordination Division; and (2) Finance, Auditing, and Evaluation Division. The minimum agreed number of staff shall be 16 persons, which is twice the current staffing level, including three additional staff in the Finance, Auditing, and Evaluation Division. The proposed organizational structure of HLSPO was reviewed and was deemed to be appropriate for the needs of the project (see Annex 15).

Funds Flow. The proposed project will establish a financial management and accounting system to control the flow of funds at each level at which the project will operate. The necessary and simple reporting and monitoring features will be built into its system to track the use of project proceeds implemented by communities at the *sum* and *aimag* levels. Such procedures will be documented in the Project Financial Management Manual.

At central level, HLSPO will operate two bank accounts comprising: (1) a Special Account denominated in US dollars to receive funds from IDA; and (2) a MNT (local currency) account to receive funds from government budgetary allocations.

HLSCs at *aimag* and *sum* levels will each open two bank accounts comprising: (1) a MNT account to operate project funds, regardless of project components; and (2) another MNT account to separate the receipt of the repayment collections and maintain as a revolving fund account.

The Special Account will be opened at a commercial bank acceptable to Bank. At the time of review, the Trade and Development Bank, which is only the reliable commercial bank at this moment, would be considered an acceptable bank. At *aimag* and *sum* levels, the bank will be selected based on availability of branches, time taken in transferring funds, capability in providing monthly bank statements, and the financial health of the Bank. The available banks, at the time of review, comprise: (1) Post Bank; and (2) Agriculture Bank.

A chart summarizing the project flow of funds from the Bank, Government, and other financiers is included in the full Financial Management Assessment Report.

Staffing. Key HLSPO staff have previous experience with the Bank's disbursement and procurement procedures. However, their knowledge and experience with international accounting and financial management standards and their familiarity with the Bank's financial reporting requirements are quite limited. The Financial, Auditing and Evaluation Division currently has four accounting staff plus a driver. The division is headed by the Head of Finance. To cope with the expanded activities of the proposed project, the division will be increased to 8 staff members to assume the functions of financial management, disbursement, financial inspection, and monitoring and evaluation. This staffing level is deemed to be adequate, however the roles and job description of each position should be specified and documented. Training needs to be provided prior to project effectiveness. The organization structure, job title, responsibilities, educational background and professional experiences will be documented in the Project Financial Management Manual.

Accounting Policies and Procedures. The accounting controls at all levels are weak, and verification and documentation are inadequate. Journal and Payment vouchers are not adequately prepared and checked. Except for the Special Account, other bank transactions have never been reconciled. The filing system does not facilitate subsequent auditing. Staff at *aimag* and levels do not have adequate accounting skills. Segregation duties are impractical given staffing constraints.

To mitigate these weaknesses, HLSPO should establish controls and procedures for flow of funds, financial information, accountability, and audit in relation to *aimag* and *sums*. Such procedures will be part of the Project Financial Management Manual.

Planning and Budgeting. HLSPO will prepare budget proposals for inclusion of those expenditures that must be reflected in national and local budgets; and compilation/verification of AWPBs for each component.

External Audit. An annual audit of project accounts and financial statements would be carried out by an independent, internationally recruited auditing firm under terms of reference (TOR) acceptable to the World Bank. The annual audit report would be sent to the Bank within six months of the end of the Borrower's fiscal year, i.e. by June 30 of each year, with the first such report due by June 30, 2003.

Reporting and Monitoring. HLSPO prepared financial statements for the previous project quarterly and annually. The statements were prepared on the basis of Mongolian accounting standards which are understood to be compatible with International Accounting Standards (IAS). A sample of reports was reviewed and found to be satisfactory but some need to be adapted to be fully used as a tool of project management and monitoring. A financial management reporting system should be elaborated. The reports should be produced more frequently and systematically. A set of Financial Monitoring Reports (FMRs) was proposed and need to be modified to comply with the project cost structure. These reports will also be required to be submitted to the Bank on a quarterly basis. The draft FMR format was submitted to the Bank for review at appraisal.

The content of FMRs comprise:

1. Discussion of Project Progress
2. Sources and Uses of Funds Statement
3. Uses of Funds by Expenditure Type

4. Output Monitoring Report
5. Procurement Report

Information Systems. The accounting system is computerized; auto-generated reports from the accounting program named "Simply Accounting". It was developed locally by a Mongolian company. The capacity is limited to produce only basic books and standard reports such as trial balance, general ledger, balance sheet and income statements, and capture data only to 10 digits.

The hardware and accounting software were reviewed and found to be inadequate. New accounting software needs to be developed to meet the expanded needs of the project, to be flexible, and able to be customized to meet the specific reporting requirements of the project. Data/ reports need to be imported into a suitable spreadsheet program so as to facilitate the preparation of the Statement of Expenditure (SOE) attachment sheet to the Withdrawal Application. Below is a list of requirements for the software:

- multi-level reporting by project, sub-project or any component level;
- multi-currency support;
- capability to track/link to physical performance indicators;
- capability to track and report on procurement/ contract basis;
- capability to track and report using flexible reporting cycles (monthly, quarterly, annually, or any user-defined period);
- capability to track based on Actual, Budget, Forecast, and Life of Project;
- multiple location and consolidation facility;
- multi-level help ay screen and field levels, as well as on-line documentation; and
- drill-down feature to take user to origin of transaction from the Query screen, providing for audit trial

Project Financial Management Manual. The manual will be used as staff guidelines and as a basis for training. The manual shall describe flow of funds, authorities and delegation of responsibilities of the project staff, disbursement procedures, internal controls, financial and accounting policies and procedures, and transaction flows as well as budget preparation procedures. A draft Financial Management Manual was submitted to the Bank for review at appraisal. Detailed comments have been provided for its revision, to be finalized prior to Effectiveness.

Supervision Plan. The supervision of the project will include close monitoring of the FM related aspects and implementation of the project by the HLSPO. Quarterly FMRs are to be submitted to the Bank within 45 days from the last quarter period. Bank supervision is planned at least twice a year.

Financial Management Action Plan: The following financial management action plan has been agreed with the Borrower to improve the system so as to meet the Bank's minimum requirements:

Action:	*Responsibility:*	*Completed by:*
1. Staffing:		
▪ Three additional staff appointed to financial division of HLSPO and all job descriptions finalized.	HLSPO	Effectiveness
▪ New financial staff at central level trained in operation of project financial management system and Bank financial management requirements and procedures.	HLSPO	Effectiveness
▪ Staff training completed and workshops conducted at central, *aimag* and *sum* levels.	HLSPO	Effectiveness
2. Project Financial Management System:		
▪ Computer hardware and software procured and capable of producing FMRs acceptable to the Bank.	HLSPO	Effectiveness
3. Project Financial Management Manual:		
▪ Project financial management system clearly documented in a Financial Management Manual acceptable to the Bank, as part of the PIM.	HLSPO	Effectiveness
4. Reporting and Monitoring:		
▪ Financial reporting system upgraded to produce Financial Monitoring Reports (FMRs) in a format acceptable to the Bank. Quarterly FMRs to be submitted to the Bank within 45 days from the last quarter.	HLSPO	Effectiveness
5. External Audit:		
▪ An independent auditing firm acceptable to the Bank appointed to perform annual audits of project financial statements under TOR acceptable to the Bank, having been selected through international advertisement following the Bank's procurement guidelines for QCBS.	HLSPO	December 31, 2002

Annex 7: Project Processing Schedule
MONGOLIA: Sustainable Livelihoods Project

Project Schedule	Planned	Actual
Time taken to prepare the project (months)	26	26
First Bank mission (identification)	12/13/1999	12/13/1999
Appraisal mission departure	02/25/2002	02/25/2002
Negotiations	04/22/2002	04/29/2002
Planned Date of Effectiveness	07/01/2002	

Prepared by:

Robin Mearns, Task Team Leader

Preparation assistance:

1. UK DFID support for consultant inputs in project identification linked to the operationalization of a Sustainable Livelihoods approach;

2. Government of Japan-financed PHRD grant (TF#026251), executed by GoM, which financed international and local consultant inputs to conduct feasibility studies for the three main project components, plus a social assessment, inputs to the environmental assessment, two Project Cycle Management (LogFrame) workshops in June and August 2001, and professional auditing services;

3. Supplementary consultant inputs financed by the World Bank for the pastoral risk management component, notably to assess the feasibility of indexed livestock mortality or weather-based insurance; and to conduct a decentralization assessment (including matching funding from the Community-Based Rural Development thematic group);

4. EU-TACIS/World Bank Joint Environmental Program (JEP) grant support for the preparation of a stand-alone environmental assessment of the proposed project;

5. FAO-CP preparation support mission to assist with the completion of the Project Implementation Plan (PIP), building on the work of the PHRD-financed and other consultants; and

6. At the additional request of GoM, Irish consultant trust funds mobilized to assist with the design of the Project Management Support component, to finance consultant inputs during pre-appraisal mission and, with the support of a local consultant, to support SLPO in finalizing project management arrangements, the PIM, and the PIP.

Bank staff who worked on the project included:

Name	Speciality
Robin Mearns	Sr. Natural Resource Management Specialist, Task Team Leader
Guzman Garcia-Rivero	Sector Leader
Guo Li	Agricultural Economist
Nathan Belete	Rural Development Specialist
Anthony Whitten	Sr. Biodiversity Specialist

Behdad Nowroozi	Sr. Financial Management Specialist
Mary Judd	Sr. Anthropologist
Nipa Siribuddhamas	Financial Management Specialist
Jinan Shi	Procurement Specialist
Keith McLean	Decentralization Specialist
Hoi-Chan Nguyen	Project Lawyer
Lisa Bhansali	Project Lawyer
Rosa Muleta	Disbursement Officer
Cornelis de Haan	Peer Reviewer
Daniel Sellen	Peer Reviewer
Michael Goldberg	Peer Reviewer
Tsolmon Bat-Ochir	Operations Officer
Evelyn Bautista Laguidao	Program Assistant
Cecilia Tan	Team Assistant
Cecilia Belita	Program Assistant
Kathryn Cherrie	Program Assistant
Jeremy Swift	Consultant (identification/ pastoral risk management)
Jerry Skees	Consultant (index insurance for livestock)
John Morton	Consultant (pastoral risk management)
Dennis Sheehy	Consultant (scoping of EA for pastoral risk management)
Suvira Chaturvedi	Consultant (local initiatives fund)
Enjiang Cheng	Consultant (micro-finance)
S. Ganbold	Consultant (micro-finance)
B. Enkhbat	Consultant (local initiatives fund)
Daniel Miller	Consultant (pastoral risk management)
N. Batjargal	Consultant (pastoral risk management)
Doug Smith	Consultant (environmental assessment)
J. Byambadorj	Consultant (environmental assessment)
Olexi Kabyka	Consultant (environmental assessment)
Natasha Pairaudeau	Consultant (social assessment)
R. Gantumur	Consultant (stakeholder participation/ social assessment)
E. Tungalag	Consultant (social assessment)
Alice Carloni	Consultant (FAO/CP preparation support mission team leader)
Stephan Baas	Consultant (FAO/CP pastoral risk management)
Joe Remenyi	Consultant (FAO/CP micro-finance)
Howard Johnson	Consultant (FAO/CP local initiatives fund)
Seamus Cleary	Consultant (project management support)

Annex 8: Documents in the Project File*
MONGOLIA: Sustainable Livelihoods Project

A. Project Implementation Plan

Project Implementation Plan: Volume 1, Main Report, March, 2002 (revised).

Project Implementation Plan: Volume 2, Annexes, November 2001.

Project Implementation Plan: Volume 3, Working Paper 1 (Pastoral Risk Management Component), November 2001.

Project Implementation Plan: Volume 4, Working Paper 2 (Microfinance Component), March, 2002 (revised).

Project Implementation Plan: Volume 5, Working Paper 3 (Local Initiatives Fund Component), November 2001.

B. Bank Staff Assessments

Filmer, Richard. 2001. The Mongolian Cashmere Industry. World Bank/Applied Economic Solutions, Canberra, Australia, August 2001.

Hanstad, Tim, and Jennifer Duncan. 2001. Land Reform in Mongolia: Observations and Recommendations. RDI Reports on Foreign Aid and Development No.109. Seattle: Rural Development Institute for the World Bank.

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C. Other

Government Documents

Government of Mongolia, 2000. Action Program of the Government of Mongolia, 2000-2004.

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USAID: Gobi Business News (various issues from 1999).

*Including electronic files

Annex 9: Statement of Loans and Credits

MONGOLIA: Sustainable Livelihoods Project

02-May-2002

Project ID	FY	Purpose	Original Amount in US$ Millions IBRD	IDA	Cancel.	Undisb.	Difference between expected and actual disbursements* Orig	Frm Rev'd
P074001	2002	Mongolia Legal Reform Project	0.00	5.00	0.00	4 99	0.00	0.00
P040907	2001	ENERGY SECTOR	0.00	30.00	0 00	29.03	2 14	0.00
P056200	2001	MN-Transport Develop	0.00	34.00	0 00	28.77	10.40	0 00
P068071	2000	MN-Financial Sector Adjustment Credit	0 00	32.00	0.00	19 06	10.46	0.00
P049789	1999	MN-PRIV.SEC. DEVT CR	0.00	12.00	0.00	5.21	3 60	0 00
P051855	1998	MN-Fiscal Technical Assistance Project	0 00	5.00	0.00	3.34	3 48	0 07
P036052	1998	MN-ULAANBAATAR SERV. IMPRMVT	0.00	16.70	0 00	4.82	5 15	1 67
		Total:	0.00	134.70	0 00	95.21	35 23	1 74

MONGOLIA
STATEMENT OF IFC's
Held and Disbursed Portfolio
Jan - 2002
In Millions US Dollars

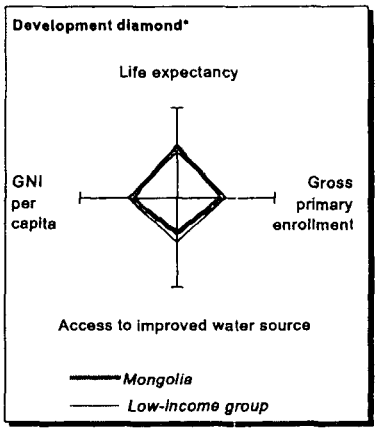
		Committed				Disbursed			
		IFC				IFC			
FY Approval	Company	Loan	Equity	Quasi	Partic	Loan	Equity	Quasi	Partic
1997	SEF G&M Leather	1.05	0.20	0.00	0.00	1.05	0.20	0 00	0.00
	Total Portfolio:	1.05	0.20	0.00	0.00	1.05	0.20	0.00	0.00

		Approvals Pending Commitment			
FY Approval	Company	Loan	Equity	Quasi	Partic
2001	SEF XAC	0.40	0.00	0.00	0.00
	Total Pending Commitment:	0.40	0.00	0.00	0.00

Annex 10: Country at a Glance

MONGOLIA: Sustainable Livelihoods Project

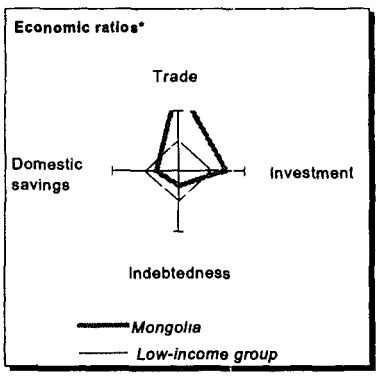
POVERTY and SOCIAL	Mongolia	East Asia & Pacific	Low-income
2000			
Population, mid-year *(millions)*	2.4	1,853	2,459
GNI per capita *(Atlas method, US$)*	390	1,060	420
GNI *(Atlas method, US$ billions)*	0.95	1,964	1,030
Average annual growth, 1994-00			
Population *(%)*	1.1	1.1	1.9
Labor force *(%)*	1.9	1.4	2.4
Most recent estimate (latest year available, 1994-00)			
Poverty *(% of population below national poverty line)*	36	..	..
Urban population *(% of total population)*	64	35	32
Life expectancy at birth *(years)*	67	69	59
Infant mortality *(per 1,000 live births)*	58	35	77
Child malnutrition *(% of children under 5)*	13	13	..
Access to an improved water source *(% of population)*	60	75	76
Illiteracy *(% of population age 15+)*	37	14	38
Gross primary enrollment *(% of school-age population)*	88	119	96
Male	86	121	102
Female	91	121	86



KEY ECONOMIC RATIOS and LONG-TERM TRENDS

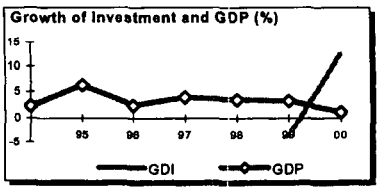
	1980	1990	1999	2000
GDP *(US$ billions)*	..	..	0.91	0.97
Gross domestic investment/GDP	..	38.1	28.5	30.0
Exports of goods and services/GDP	..	24.0	61.2	65.5
Gross domestic savings/GDP	..	9.2	15.1	13.6
Gross national savings/GDP	..	..	14.8	12.9
Current account balance/GDP	.	.	-13.7	-17.1
Interest payments/GDP	..	.	1.0	1.0
Total debt/GDP	..	..	98.4	88.6
Total debt service/exports	.	..	4.6	4.5
Present value of debt/GDP	.	.	55.9	..
Present value of debt/exports	..	.	89.1	..

	1980-90	1990-00	1999	2000	2000-04
(average annual growth)					
GDP	5.4	1.0	3.2	1.1	4.0
GDP per capita	3.0	-0.3	2.3	0.3	2.0
Exports of goods and services	..	..	4.7	12.8	3.9

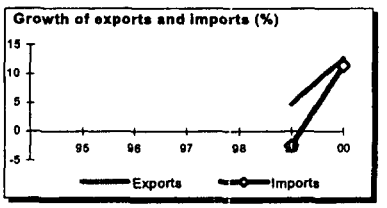


STRUCTURE of the ECONOMY

(% of GDP)	1980	1990	1999	2000
Agriculture	..	17.4	37.0	33.3
Industry	..	30.4	20.7	18.5
Manufacturing	..	..	5.9	5.4
Services	..	52.2	42.4	48.2
Private consumption	..	58.4	66.8	66.3
General government consumption	..	32.4	18.1	20.0
Imports of goods and services	..	52.9	74.6	81.9



	1980-90	1990-00	1999	2000
(average annual growth)				
Agriculture	1.4	3.2	4.2	1.6
Industry	6.6	-0.5	1.1	1.1
Manufacturing	..	..	-2.7	3.2
Services	8.4	0.1	3.4	0.6
Private consumption	..	..	1.4	-4.8
General government consumption	..	..	-5.0	6.2
Gross domestic investment	..	..	-3.6	12.4
Imports of goods and services	..	..	-2.4	11.4

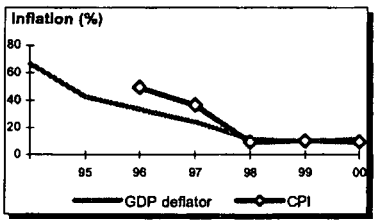


Note: 2000 data are preliminary estimates.

* The diamonds show four key indicators in the country (in bold) compared with its income-group average. If data are missing, the diamond will be incomplete.

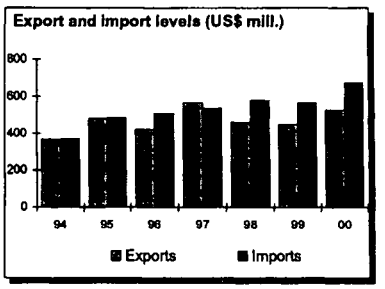
PRICES and GOVERNMENT FINANCE

	1980	1990	1999	2000
Domestic prices				
(% change)				
Consumer prices	..	..	10.0	9.5
Implicit GDP deflator	..	0.0	9.7	11.6
Government finance				
(% of GDP, includes current grants)				
Current revenue	..	54.1	..	..
Current budget balance	..	-1.5	..	..
Overall surplus/deficit	..	-14.5	-11.9	-9.9



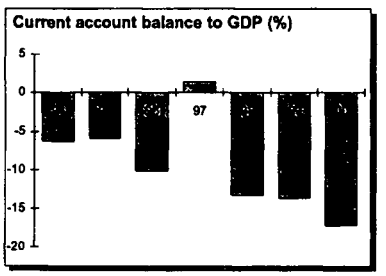
TRADE

	1980	1990	1999	2000
(US$ millions)				
Total exports (fob)	..	661	454	529
Copper	..	260	119	..
Meat	..	56	..	..
Manufactures	..	..	..	..
Total imports (cif)	..	924	567	679
Food	..	..	..	..
Fuel and energy	..	..	..	..
Capital goods	..	..	..	..
Export price index *(1995=100)*	..	..	..	..
Import price index *(1995=100)*	..	..	..	..
Terms of trade *(1995=100)*	..	..	..	..



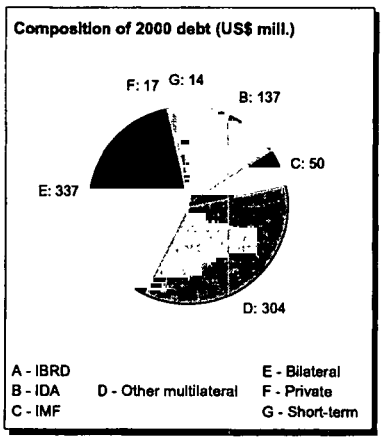
BALANCE of PAYMENTS

	1980	1990	1999	2000
(US$ millions)				
Exports of goods and services	..	493	554	635
Imports of goods and services	..	1,101	675	794
Resource balance	..	-608	-121	-159
Net income	..	-44	-10	-15
Net current transfers	..	0	7	8
Current account balance	..	-651	-124	-166
Financing items (net)	..	598	140	224
Changes in net reserves	..	53	-16	-58
Memo:				
Reserves including gold *(US$ millions)*	..	..	157	188
Conversion rate *(DEC, local/US$)*	..	..	1,021.9	1,076.7



EXTERNAL DEBT and RESOURCE FLOWS

	1980	1990	1999	2000
(US$ millions)				
Total debt outstanding and disbursed	..	..	891	859
IBRD	..	..	0	0
IDA	..	..	130	137
Total debt service	..	..	26	29
IBRD	..	..	0	0
IDA	..	..	1	1
Composition of net resource flows				
Official grants	..	..	49	..
Official creditors	..	..	151	46
Private creditors	..	..	-3	-3
Foreign direct investment	..	..	30	..
Portfolio equity	..	..	0	..
World Bank program				
Commitments	..	..	12	32
Disbursements	..	..	14	14
Principal repayments	..	..	0	0
Net flows	..	..	14	14
Interest payments	..	..	1	1
Net transfers	..	..	13	13



Additional Annex 11: Program Vision and Approach, with Letter of Development Program MONGOLIA: Sustainable Livelihoods Project

Program Vision

The overall *program purpose* is: "*vulnerability reduced and secure and sustainable livelihoods achieved by targeted poor and vulnerable near-poor households and individuals nationwide*". The Sustainable Livelihoods Program is intended to support the shift in Mongolia's national anti-poverty strategy away from welfarist measures towards those that promote secure and sustainable livelihoods for all.

The *program development objective* is: "*target groups and individuals adopt improved livelihood strategies that build and maintain human, social, financial, physical and natural capital while reducing vulnerability to shocks*". This would be achieved through investments in four components: pastoral risk management; micro-finance outreach; local initiatives fund; and program management and policy support. Synergies among the components are an important feature of program design. These synergies derive from their complementary approaches to promoting asset creation so as to reduce vulnerability and enhance livelihood security.

By the end of the program, a national strategy would be in place and resourced appropriately to ensure that adequate steps are taken by actors at various levels (national, *aimag*, *sum*, *bag*, household) to reduce herders' exposure to risk in the pastoral livestock sector, prepare for risk episodes, and respond quickly and effectively in the event of serious covariant risks to reduce their overall impact on pastoral livelihoods. To the extent that external financing remained necessary, this strategy would have the force of national policy, such that all donor-financed activities support the overall strategy. Restocking, for example, may remain part of a post-risk recovery strategy, but would be financed in such a way that it did not undermine management incentives or sustainability of the micro-finance sector more generally.

A wide range of micro-finance services would be available to low-income and vulnerable households, including those in remote rural areas, to enable them to smooth consumption and manage risk without needing to liquidate assets. Herders would be able to sell animals rapidly and destock in advance of risk episodes, facilitated by livestock marketing (including marketing facilities created through demand-driven local investments) and by the possibility of converting livestock into alternative, more liquid, assets including secure savings. Those in rural areas who do not see a future for themselves in livestock production have opportunities open to them to pursue alternative livelihood strategies, facilitated by access to affordable micro-credit. Some of these activities may be in livestock product processing, for example, but may also be in areas unrelated to livestock production such as tourism. Institutionally and financially sustainable approaches to livestock insurance would also form part of the available range of micro-finance products. Indemnification would promote management incentives.

Vibrant local economies in rural areas would be facilitated by public expenditure allocation responsive to local needs and demands. Local infrastructure creation and maintenance, and social service provision, among other public goods, would help to provide a supportive environment for private sector-led growth, in turn facilitated by opportunities to build private assets through access to appropriate financial products and services. Ecologically appropriate investments in the infrastructure required for pastoral risk management, including sustainable pasture land management, would be made as necessary, determined by the particular needs of each agro-ecological zone and locality. Local governments would have discretionary control over a significant share of the total state budget, but would be downwardly accountable to local communities in

determining how these public funds are spent. Participatory, community-based mechanisms for determining the pattern of such expenditures would operate throughout the country, irrespective of 'sectoral' boundaries. Public access to information about such expenditures would be widely available. This higher level of transparency would result in the creation of public goods of higher quality, yet at lower cost than at the start of the program.

Sustainable Livelihoods Approach

The emphasis of a sustainable livelihoods approach is on reducing *vulnerability* so as to enhance *livelihood security*. The program therefore focuses on ways to improve the *assets and capabilities* of poor and vulnerable groups, and therefore their future income-earning potential or *livelihood sustainability*, rather than their current income or consumption levels alone.

The relevant assets to be created under the program include both *private goods* (via access to micro-finance products and services) and *public goods* (community-level infrastructure and social services, and institutional arrangements for pasture land management and conflict resolution, for example). Certain assets will fall between these two extremes, such as wells or revolving funds owned and managed by small groups of herders, and may be thought of as *semi-public goods*.

The public subsidy element in asset creation will vary along the continuum between private and public goods, requiring a sliding scale of beneficiary contributions. There would be little or no subsidy in the provision of private goods/assets; that is, no subsidy of interest rates in micro-credit, for example, although the MDF would implicitly subsidize institutional innovation in the development of new micro-finance products accessible to the poor and those in remote rural areas. Public assets created under the LIF would require beneficiary contributions of around 10% to ensure local ownership and sustainability.

Government Letter of Development Program

MINISTRY OF FINANCE AND ECONOMY OF MONGOLIA

210646 Negdsen undestnii gudamj 5/1, Zasgiin gazriin II bair,
Chingeltei duureg, Ulaanbaatar, MONGOLIA
Tel./Fax: (976-11) 32-02-47, E-mail: ulaan@pmis.mof.gov.mn
http://www.mof.gov.mn

Date 28.03.2002
Ref. 4/1016

To: H.E. Ian Porter
Country Director for Mongolia
East Asia and Pacific

Dear Mr Porter,

Letter of Development Programme

Since July 2000, the Government of Mongolia has made poverty reduction the cornerstone of its Action Plan. Over the last 18 months, we have sought to develop policies and operational programmes to help make this goal a reality. A Poverty Reduction and Growth Facility has been agreed with the IMF, and the Interim Poverty Reduction Strategy Paper (I-PRSP) we have prepared has been approved by the Boards of the IMF and the World Bank. The full PRSP is currently being elaborated in a participatory manner for completion by autumn 2002, and will identify the Government's priorities in bringing about a sustained reduction in the incidence of poverty over the medium term.

A great deal of valuable experience was gained in the implementation of the National Poverty Alleviation Programme (NPAP) over 1994-2000, with support from the World Bank and other international donors and organizations. While NPAP achieved some notable successes, particularly in building local capacity to realize needed investments in the physical and human development infrastructure vital for private sector-led growth, it did not succeed in reducing the overall number of people living below the poverty line. New economic opportunities continued to be denied to many people, particularly those living in remote rural areas. Insufficient attention was also paid to reducing vulnerability to natural hazards, such as the summer droughts and harsh winters experienced in 1999-2002.

At least two major lessons were learned under NPAP. First, policies to promote economic growth should not be separated from those designed to reduce poverty; these twin goals should be considered together. And second, poverty is not only a matter of insufficient income or levels of consumption; it is also characterized by vulnerability to external shocks such as international commodity prices or natural hazards.

With these lessons in mind, and in the broader context of our evolving PRSP, the Government of Mongolia enacted several important pieces of legislation in 2001. One was Resolution 47 (March 13, 2001) to improve risk preparedness and protect those who depend on livestock from the effects of drought and harsh winter/spring conditions. A second was our regional and rural development concept, designed to reduce rural and urban development disparities and bring more sustainable use of natural resources such as pasture land. And a third was Resolution 108 (May 10, 2001), which established the National Household Livelihoods Capacity Support Programme (NHLCSP) as a follow-up programme to NPAP.

Over the period 2001-2006, the NHLCSP seeks to build on the past successes of NPAP while also addressing its shortcomings. It aims to reduce the incidence of poverty among poor and extremely poor households, and prevent vulnerable non-poor households from falling below the poverty line, by extending the coverage of social services and promoting the economic opportunities necessary for developing human capacity and promoting sustainable development. Several important principles underlie the NHLCSP, and the PRSP more broadly, including: developing mechanisms to tailor public policies and expenditures to the specific needs of the population in different geographical contexts and bridging urban and rural arenas; promoting opportunities for enhanced participation and coordination of the public and private sectors and civil society; encouraging gender equity; and fostering transparency and accountability in governance through more open public access to information.

These recent efforts on the part of the Government are putting in place policies and operational programmes to bring about more widely shared economic growth and a sustained reduction in poverty over the medium term. However, they are also laying the foundations for a more prosperous future for Mongolia, the full effects of which may not be realized for perhaps a decade or more. We envisage the Sustainable Livelihoods Programme as making an important contribution to realizing this longer-term vision, with a primary focus in the main areas of the development strategy outlined in the following paragraphs.

Consistent with its regional and rural development concept, and Resolution 47 to promote risk preparedness, the Government of Mongolia will promote more widely shared economic growth in order to bring about a sustained reduction in both the incidence of poverty and vulnerability to external shocks. In keeping with the goals of the NHLCSP, this will result in improved life conditions for the extremely poor; the graduation of the able-bodied poor out of poverty; and reduced vulnerability of low-income, non-poor groups. These goals will be realized by empowering communities to select and execute infrastructure improvements and other activities to contribute to economic diversification; and through the further development of the micro, small, and medium enterprise sector. This will expand the range of market-responsive employment opportunities, including alternative income-generating strategies for marginal herders to enable them to exit the livestock sector. Increasing access to financial services, and training in business and vocational skills, are critical to achieving this vision.

The Government recognizes the central role that a vibrant rural sector must play in contributing to sustained poverty reduction at the national level. We believe that rural and urban development should not be treated separately, but must be approached in an integrated manner so as to enable Mongolia's comparative advantage in extensive livestock production to be combined with the pursuit of human development goals through urban-based services. Sustainability in livestock production has been compromised in recent years with an increase in grazing pressure in more market-accessible areas, leaving much good pasture under-utilized. Over the medium- to long-term, the Government will pursue a strategy of restoring the competitiveness and sustainability of livestock production combined with rural economic diversification. Vital elements in achieving this vision include putting in place measures to increase risk management in the livestock sector, consistent with Resolution 47; productivity enhancing investments in the agriculture sector more broadly, including water supply, hay and fodder development, and agricultural services; investments in basic infrastructure to improve market access; and access to financial services to facilitate sustained private sector-led growth in rural areas.

With the support of international organizations, the Government is pursuing a long-term strategy to ensure that public administration and fiscal affairs are decentralized to the extent appropriate for Mongolia's large and diverse territory. In the short run, we are taking steps to improve the level and efficiency of public revenue-raising. But in parallel with this we are also developing a transparent, formula-driven approach to determining inter-governmental transfers so as to ensure a fair and equitable distribution of public resources, taking into account poverty-targeting and other criteria. At the local level, it is essential that scarce public resources are then made available and used in a manner which is responsive to local needs, priorities, and aspirations. The Local Initiatives Fund of the Sustainable Livelihoods Programme, building on experience with the Local Development Fund under NPAP, aims to develop such local-level mechanisms for resource allocation across sectors while remaining consistent with national-level sector strategies. The development of transparent mechanisms for resource allocation across sectors and between regions and localities is critical to achieving the Government's overall vision in fostering widely shared economic growth.

The Government is committed to increasing the outreach of micro-finance services to able-bodied poor and vulnerable non-poor groups in remote rural areas on a sustainable basis, and believes that this will make a vital contribution to securing more widely shared and diversified economic growth over the long term. Savings mobilization and the anticipated development of micro-insurance products to help smooth consumption, manage external shocks, and diversify the assets of low-income and vulnerable households are as important to this vision as promoting the sustainable outreach of micro-credit. The possible development of a profitable and sustainable commercial scheme for livestock insurance is one such area in which the support of the Sustainable Livelihoods Programme will be vital, building on international experience with innovative, index-based approaches that are consistent with incentives for sustainable livestock management. The proposed Mongolia Micro-finance Development

Fund (MMDF) also provides clear evidence of the Government's support for a newly emerging privately owned micro-finance industry. Over the medium- to long-term, the MMDF would continue to play a role as an apex micro-finance institution and technical assistance agency independent of Government support.

The Government of Mongolia believes that the Sustainable Livelihoods Programme would make an important contribution to making this long-term development vision a reality, and looks forward to a sustained cooperation with the World Bank and other donors over the proposed 12-year programme period.

Sincerely,

Ch. Ulaan
Minister

Additional Annex 12: Relevant Donor-Supported Activities
MONGOLIA: Sustainable Livelihoods Project

Project identification over September 1999-January 2000 was conducted jointly with **ADB, UNDP** and **SIDA**, in conjunction with the joint evaluation of the National Poverty Alleviation Program (NPAP) for which these agencies had also been co-financiers. Although they do not have an operational program in Mongolia, UK **DFID** also financed additional consultant inputs in project identification, guided by a sustainable livelihoods approach, and in parallel with their support for the Participatory Living Standards Assessment (PLSA).

Several priorities for future anti-poverty efforts in Mongolia were identified in the course of the joint evaluation of NPAP and the national stakeholder workshop conducted in December 1999 as part of the identification process for the Sustainable Livelihoods Project. Among these were (i) vocational training; (ii) national-level capacity building in poverty-related policy research and advice; (iii) reform of the state social welfare system; (iv) support for the development of a national strategy and investments to support pastoral risk management; (v) micro-finance outreach, particularly in rural areas; and (vi) community-driven investments in local infrastructure and social services provision.

Agreement was reached in dialogue among Government and leading donor agencies to follow-up NPAP with a coordinated set of programs and projects, all or most of which would fall under the auspices of the Government's Household Livelihoods Capacity Support Program (HLCSP), the successor anti-poverty program to NPAP. Most notable among these complementary initiatives were: (a) support from **UNDP** and **SIDA** for a 'Poverty Research and Employment Facilitation for Policy Development' project, aimed at building institutional capacity in poverty research, monitoring, and policy advice (issue (ii) above); and (b) support from **ADB** for a 'Social Security Sector Development Program', aimed at reform of the social welfare system and increasing support for vocational training (issues (i) and (iii) above). It was agreed at this time that World Bank would take the lead in supporting efforts to address issues (iv), (v), and (vi) above, under the Sustainable Livelihoods Program/Project.

Identification of the *pastoral risk management* component also drew on detailed lessons learned from (i) the **FAO**-supported TCP project on herd restocking in Arkhangai *aimag* in 1995; (ii) the **IFAD**-supported Rural Poverty Alleviation projects in Arkhangai and Khuvsgul *aimags* that scaled-up the approach to restocking piloted under the earlier FAO TCP project; and (iii) the **World Bank**-supported emergency restocking response to the 1999-2000 *dzud*, financed from the Poverty Alleviation for Vulnerable Groups Credit, that further refined the restocking 'model' developed in Mongolia to date. Other relevant experience on restocking was offered by the smaller-scale **SCF(UK)**-supported initiatives in Bayan-Olgii, Uvs, Khovsgol, and Dornod *aimags* that fell under the auspices of NPAP. It was widely recognized that NPAP had done little to reach the rural poor and herders in particular, or to reduce vulnerability to drought and *dzud*. The serious *dzud* episodes of 1999/2000 and 2000/2001 brought home to Government and the international donor community the overwhelming importance of promoting livelihood security for herders and others dependent on livestock production by improving risk preparedness.

A second **FAO**-supported TCP project began activities in 2000 to pilot-test in Tov and Uvs *aimags* certain elements of a pastoral risk management strategy (e.g. hay and fodder development). This TCP project is explicitly designed as a 'testing ground' for ideas that could be scaled-up operationally under the Sustainable Livelihoods Project, which includes the same two *aimags* in Phase I. Other donor-supported efforts that complement the pastoral risk management component include: (i) **ADB** support for community-based pasture land management pilots under the Agriculture Sector Development Program that

will begin work in 2002 in a number of western *aimags;* (ii) **USAID** support for pastoral and agricultural development under the Gobi Regional Economic Growth Initiative; (iii) **UNDP** support for community-based pilots in sustainable grasslands management executed by the Ulaanbaatar-based Center for Policy Research (CPR) in three sums of Tov, Bayankhongor, and Khentii *aimags*. There is close, operational-level interaction between local teams working on these activities and on the pastoral risk management component, in areas such as: Gobi Initiative's experience in promoting radio and newsprint communications with herders on issues of market prices, land tenure, and weather forecasting; and CPR's experience in promoting herder self-help groups and land tenure mapping.

The other major area in which the SLP is coordinating with other donor-supported activities concerns *micro-finance outreach*. Most important among relevant donor-supported activities are: (i) the **ADB** -supported Rural Finance Project, which is focusing primarily on savings and credit cooperatives; (ii) a small-scale pilot project financed by **DFID** and **EU-TACIS** through the local MFI Credit-Mongol to explore ways of expanding rural micro-finance outreach; (iii) **USAID**'s support for the MFI 'Goviin-Ekhlel', founded under the Gobi Regional Economic Growth Initiative, which has recently merged with the highly successful urban-based 'XAC' MFI to form 'XACBank'. (XAC, in turn, was created under **UNDP**'s Micro-Start Initiative). Relevant work has also been supported by the **Canadian Cooperative Association** in supporting savings and credit cooperatives, primarily though not exclusively in urban areas. To varying degrees, each of these MFIs has been planning to increase outreach in rural areas, and would be potential partners for the Micro-finance Development Fund under SLP.

Additional Annex 13: Institutional Capacity-Building Measures
MONGOLIA: Sustainable Livelihoods Project

The NPAP succeeded in creating capacity to manage poverty alleviation programmes at central level and in establishing a well-functioning network of Poverty Alleviation Councils (PACs) in all *aimags* and *sums* across the nation. These units (renamed Household Livelihoods Support Councils, HLSCs) now form an integral part of local governments' institutional structure and the structure through which many of the project's activities will be implemented. If the project management structure is to be responsive to community demands, it requires that management capacity be created and strengthened at the lowest effective administrative level – the *sum* in rural areas and the *duureg* in peri-urban areas – and that clear links be built to the communities and procedures established to facilitate their involvement in the system. This has been a guiding principle for the management of all three project components.

The three components, while all contributing to improving household livelihoods, will have different types of operations and thus place different demands for institution- and capacity building. The PRM component is technical in nature with operational activities that will directly address key constraints on risk management in livestock production. The MFO component, while to an extent pilot in nature, will upgrade and restructure an ongoing nation-wide credit programme (Revolving Loan Funds, RLFs); in parallel, develop a national micro-finance outreach apex structure for wholesale lending to MFIs; and develop an index-based approach to commercially viable livestock insurance. The LIF component will operate a large nation-wide funding facility (LDF), while at the same time piloting and developing a new funding facility driven by community participatory and fiscal decentralization (LIF).

With regard to capacity building, the program components will receive technical guidance from three different Working Groups made up of senior technical staff from various ministries, agencies, private sector, and civil society groups relevant to the implementation of their respective component. Within the Household Livelihoods Support Program Office (HLSPO) and at the national level, a coordinator for each component will be responsible for coordinating all activities with their respective Working Group (or Board, in the case of MFO). The coordinators would also play a policy advisory role as required for the implementation of their respective components.

The composition of the Working Groups will vary by component: Ministry of Food and Agriculture would take the lead in Pastoral Risk Management, but include representation from the Ministry of Nature and Environment and relevant affiliates (Institute of Hydrology and Meteorology and the Land Administration Authority); while Ministry of Finance and Economy would take the lead in both the Micro-finance Development Board (with representation from the central bank and leading private finance institutions) and the LIF Working Group (with representation from other relevant line ministries including infrastructure, health and education).

Implementation and capacity building will thereafter be undertaken at the sub-national and district levels for the activities of the PRM and LIF components, with a separate working group at *aimag* level for the PRM component. The *aimag* HLSC would: (a) coordinate project activities in the *aimag* and ensure adequate support from line ministries; (b) compile and harmonize *sum*-level sustainable livelihood strategies, in order to eliminate double-counting of sub-projects under different programs; (c) provide technical, financial and administrative backstopping of *sum* HLSC operations; (d) evaluate the performance and impact of project activities within the *aimag* and monitor the attainment of targets; (e) coordinate training activities; and (f) provide overall financial oversight for project operations within the *aimag*.

The *sum* HLSC would interact directly with and be accountable to participating communities, primarily through *bag khurals* and herder groups established through the project. The *sum* HLSC would be administratively responsible to the Governor of the *sum*. They will also be responsible and accountable to the *aimags* which will provide technical support and backstopping for the activities carried out under the project. Each *sum* HLSC currently has a part-time secretary, financed from the Government budget. In all the *sums* in which pilot activities will be implemented under the project, this position will be upgraded to a full-time position, financed from the proceeds of the Credit.

The *sum* HLSCs will ensure that the activities implemented are consistent with the overall development strategy and plans of the line ministries and government. They will be responsible for preparing the *sum* -level sustainable livelihoods plan to supplement the existing *sum*-level development plans. The *sum* HLSCs would directly manage the LIF activities and ensure that procedures and processes and adhered to in the identification and approval of all activities, provide support to the MFO Coordinator through the activities of the revolving loan funds, and coordinate implementation of the PRM component.

Numerous specialized training events will be held and consulting services for technical assistance will be provided throughout the duration of the project. Most of these will be to enhance capacity at the *sum* and *aimag* levels in management and program implementation. In addition, numerous workshops have also been envisaged for community leaders, herders, and other community members in areas such as leadership, livestock management, and training of trainers. Total expenditure on training and technical assistance services accounts for some 3% of total project cost. Grant financing is being sought to meet the costs of additional technical assistance and capacity-building efforts.

Additional Annex 14: Environmental and Social Assessment Summary
MONGOLIA: Sustainable Livelihoods Project

Introduction and process

Consistent with the World Bank's Operational Policy OP4.01, environmental and social assessment for the proposed SLP is regarded as an ongoing process that began around the time of project identification. This assessment (hereafter referred to as 'the EA') therefore draws upon several steps in the process of project identification and design. The environmental component was carried out over three stages from August-October 2001: firstly scoping of impacts and desk-based review of reports; secondly, in-depth stakeholder consultation carried out over three weeks in Mongolia in September 2001, including a series of interviews and workshops with stakeholders and key informants in Ulaanbataar and rural Mongolia; and finally the preparation of a draft EA report, on which detailed comments from GoM, the World Bank, and the team responsible for PIP preparation were received. During drafting of the report, the key conclusions of a separate, dedicated social assessment (conducted over October-November 2001) were incorporated. The final report (December 19, 2001), in two volumes, presents both the dedicated EA and dedicated social assessment in a single, consolidated document.

Major EA Findings

The SLP has the potential to deliver a significant overall positive environmental impact, through a contribution to reduced land degradation in Mongolia. This conclusion is based on the following reasoning:

- There is evidence of climate change in Mongolia, which is probably accelerating land degradation directly due to drought, and indirectly due to the socio-economic impact of drought and *dzud*.
- In addition, current pasture management patterns in Mongolia are accelerating land degradation, particularly in localized areas, for example due to concentration of herds around *sum* centers and *aimag* centers.
- Therefore, successful actions to reduce herders' vulnerability through pastoral risk management offer a significant opportunity to contribute to reduced extent and severity of land degradation. Indeed it will be necessary to reduce land degradation in order to reduce herders' vulnerability to drought and *dzud*.
- Community-level or *bag*-level management planning of pasture is proposed as a key part of the project's integrated approach to pastoral risk management. The empowerment of herders or herder associations to manage their pasture is of potential for reducing land degradation, both in times of drought and *dzud*, and at all other times.

The SLP therefore will contribute to several commitments of the GoM to address land degradation, including those set out in the draft National Environmental Action Plan.

Furthermore, the SLP has the potential to deliver an overall positive social impact, by empowering herders to manage their livelihoods, and by contributing to rising living standards among poor households and herder households. This conclusion is based on the following reasoning:

- The intensive learning ICR carried out for the PAVGP, concluded that the PAVGP had a positive impact on poverty. The continuation of the LDF should maintain and further extend this impact.
- The Micro-finance Services Outreach component will improve the currently limited access of poorer households to micro-finance. Limited access constrains the ability of the poor to act to

reduce their poverty and their vulnerability through savings, livelihood diversification and other actions.

- The design of the LIF component is based on the recognition of the perceived weakness of the LDF to adequately target the poor and to ensure social investments are demand driven. By paying additional attention to these issues, the SLP will ensure that positive social impacts are maximized and negative impacts avoided.
- Positive social impact should be greater still in the 8 core *aimags* where the combined actions of the LDF, LIF, PRM and micro-finance components will reduce the vulnerability of the poor and the rural poor. In the no-project situation, drought, *dzud*, land degradation, and increased vulnerability would continue to significantly reduce living standards among poor and middle-poor herder households.
- Lower living standards in rural Mongolia are associated with rising malnutrition, increased incidence of disease, lower school attendance, depression, increased incidence of drunkenness, divorce, and higher incidence of domestic violence.

Mitigation of Potential Negative Impacts

The potential of the SLP to deliver positive improvements in reduced land degradation should far outweigh any localized environmental impacts of activities to be supported by the project. But in spite of the overall positive impact, certain of the project activities could have localized negative impacts.

Most of the developments under the PRM and LIF components will be small in scale, and the significance of the direct negative environmental impacts is likely to be small. This is especially the case in comparison to other developments that are increasing in frequency in rural Mongolia, for instance mining projects. However, in the event that some of the activities are scaled-up to wider areas following their successful piloting, there may be cumulative impacts. This provides the SLP with an opportunity to ensure that the pilot activities fully integrate the mitigation of environmental risks, in order that negative cumulative impacts are avoided when the activities are scaled-up.

The Micro-Finance Outreach component is not expected to have any direct environmental impacts, but it is likely to have indirect impacts. Indirectly, by contributing to an increased tendency amongst herders to convert their livestock assets into cash savings, it has potential to deliver positive environmental impacts. But there is also a risk that individual herders might use their access savings and credit to increase their herd sizes or to invest in income-generating activities that have a negative environmental impact. This provides opportunity to ascertain whether the improved access to micro-finance does indeed result in a more sustainable management of the environment by herders. Therefore the EA proposes that this issue is explicitly examined during the project MTR and ex-post evaluation.

Due to the demand/community driven nature and 'open menu' approach of the LIF component, and the consequent unpredictability of specific LIF and LDF sub-projects, it is difficult to assess their potential environmental impacts. But the negative impacts of community infrastructure projects are not likely to be significant. Whether particular sub-projects have significant negative impacts will depend on their scale & location, and will be context-specific and localized. Those with potentially significant environmental impacts should undergo environmental screening or EIA, under the Mongolian system of EIA, before a decision on approval.

The EA has considered all of the potential negative impacts of SLP activities, in particular in discussion with GoM and the FAO team that assisted with preparation of the PIP. GoM and the FAO team have striven to ensure that potential negative environmental impacts of the project will be avoided or minimized,

and indeed have proposed a number of suggested alternative actions or strategies. The full EA report provides details on several activities that may have negative impacts, and proposes mitigation actions based on discussions with GoM and the FAO team. These are: community-based rodent control, community-based control of predation, community-based construction and rehabilitation of wells, emergency restocking, haymaking, inter-*sum*/inter-*aimag otor* reserves, and veterinary services.

Maximizing positive social impacts

The dedicated social assessment identified a series of recommendations to enhance the positive social impact of the project. Examples of are that: the stated target groups for SLP should be broadened, so they include all groups implicitly included in project documents, including herding and settled communities in rural and peri-urban areas; local contributions under the LDF/LIF should be calculated on a project-by-project basis, rather than by a standard percentage; three-way contracts should be used under LDF/LIF and PRM components to define responsibilities of local government and groups or herders' associations; members of members of sum local government should act as community social workers, to ensure that the poorest herding households gain access to herder associations and other benefits of the PRM component; there should be allowance for participatory M&E; and that social assessment is integrated into the system of identifying, planning and monitoring projects.

Environmental and Social Management Plan

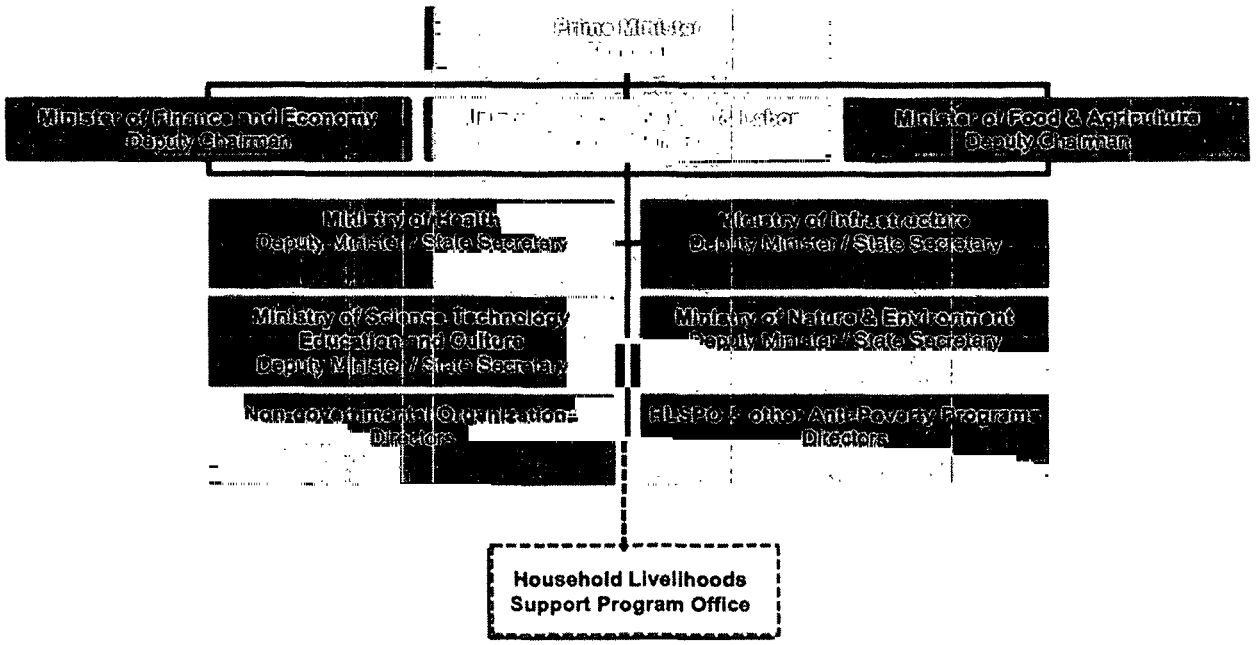
The EA sets out an environmental and social management plan (EMP), with an associated environmental management system. The design of the EMP will ensure that environmental sustainability is not considered in isolation of social, economic and institutional sustainability in the rural space. For example, it would be counterproductive if the SLP were to place a disproportionate burden on *sum*- or *aimag*- level environmental inspectors while other work, such as EIA of mining projects, deserve a more significant proportion of their time.

The bulk of inputs to this project are required at *aimag* and *sum* levels. At these levels, there is an opportunity to build on the close working relationship of agricultural, environmental, social and health officers, and improve awareness of sustainable pastoral risk management among all officers. The SLP also provides an opportunity to build a closer working relationship and a shared understanding between the Ministry of Food and Agriculture and the Ministry of Nature and Environment on sustainable livelihoods.

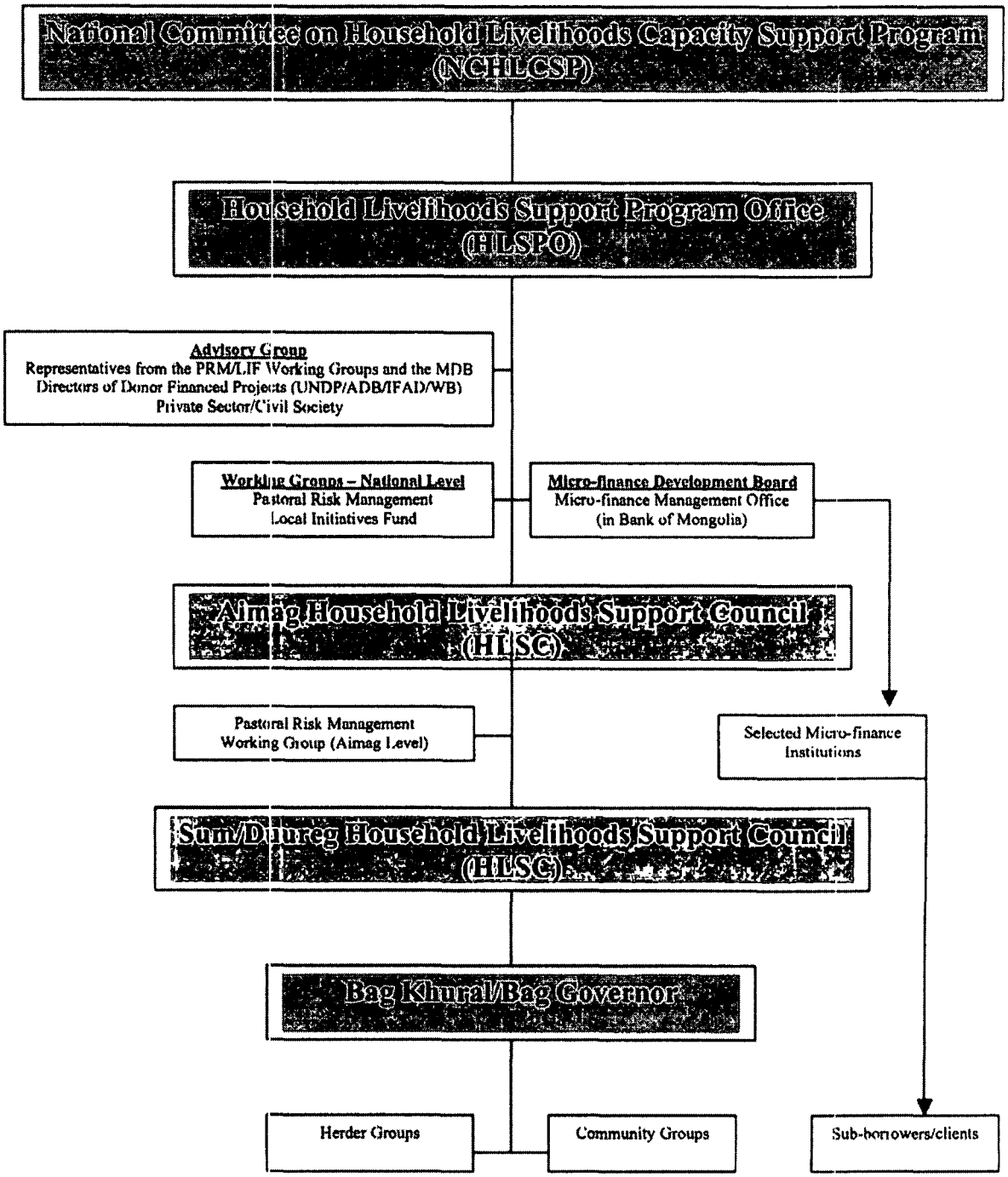
The proposed screening system is intended to be fully mainstreamed into the process for identifying, planning, implementing and monitoring activities of sub-projects. A concise set of forms and checklists have been developed, which will be merged fully with the LDF/LIF project implementation manual, and the overall system of project management.

The EMP sets out limited training requirements to ensure that environmental sustainability is fully mainstreamed into the SLP. The most significant training activity is to improve awareness of sustainable livelihoods and pastoral risk management among government officials and herders. There is a natural tendency to equate pastoral risk management (i.e. reducing people's vulnerability) with pasture management, although there is a clear difference. Other areas in which training is required are the environmental management system, and integrated pest management (in association with the rodent control activities). In addition, opportunities should be found to allow officers from *aimags* and *sums* to join together to train one another on their experiences as the project progresses.

National Committee on Household Livelihoods Capacity Support Program (NCHLCSP)



Sustainable Livelihoods Program
Implementation Arrangements



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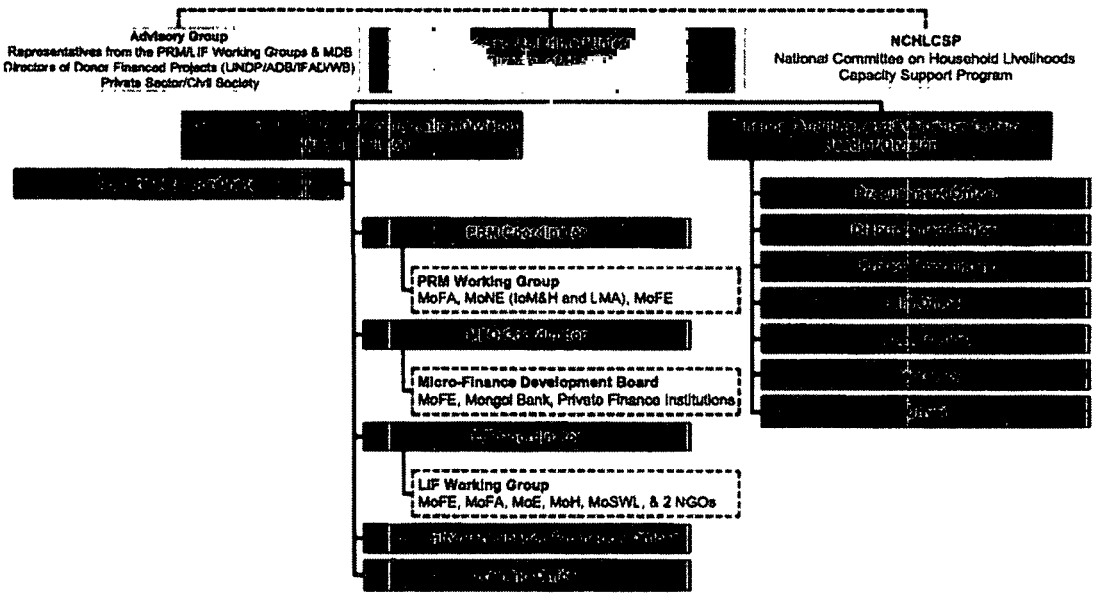

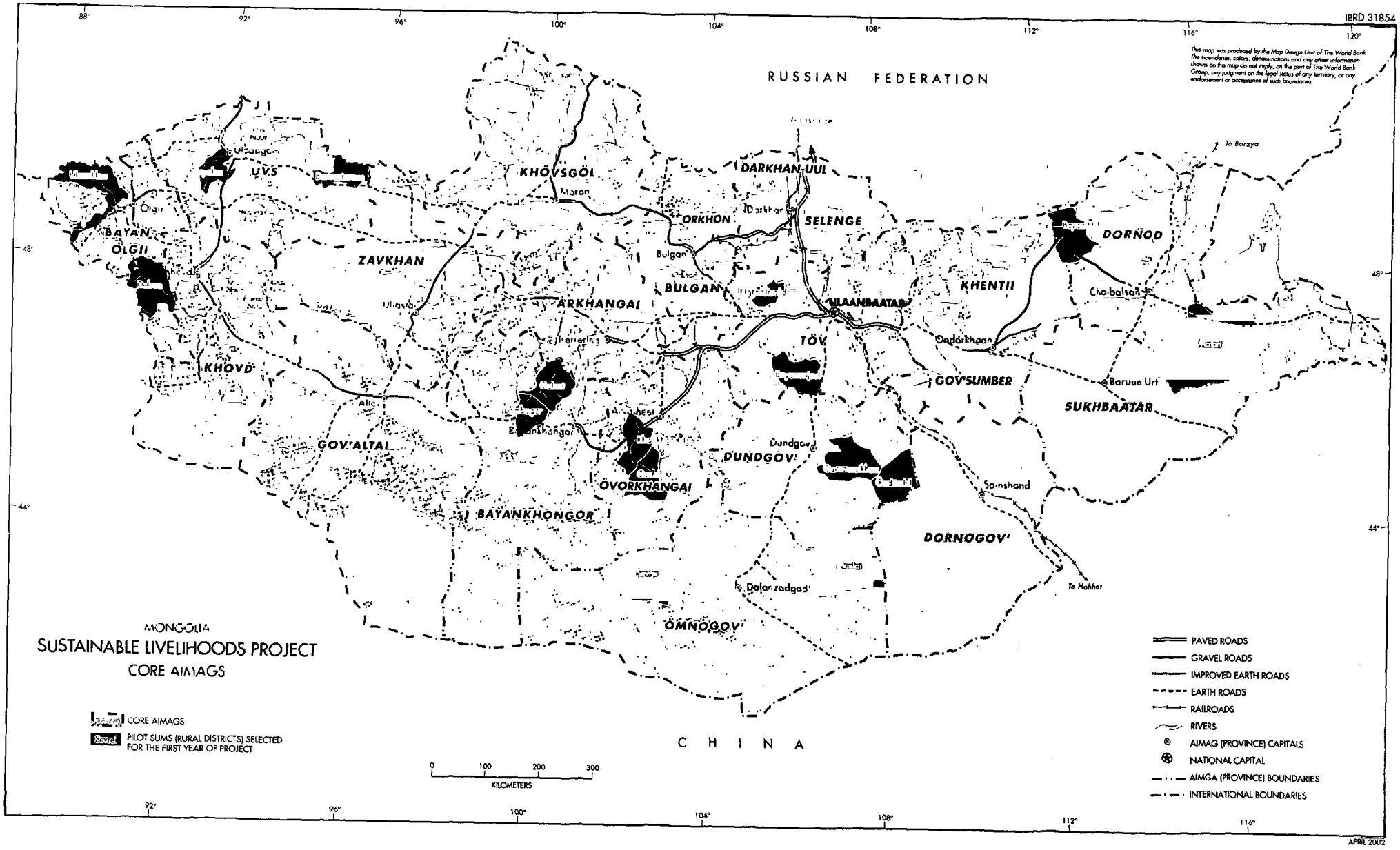
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BAYANKHONGOR
DORNOGOV'
OMNOGOV'
To Borzya
To Hohhot
MONGOLIA
SUSTAINABLE LIVELIHOODS PROJECT
CORE AIMAGS
CORE AIMAGS
PILOT SUMS (RURAL DISTRICTS) SELECTED FOR THE FIRST YEAR OF PROJECT
KILOMETERS
PAVED ROADS
GRAVEL ROADS
IMPROVED EARTH ROADS
EARTH ROADS
RAILROADS
RIVERS
AIMAG (PROVINCE) CAPITALS
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AIMGA (PROVINCE) BOUNDARIES
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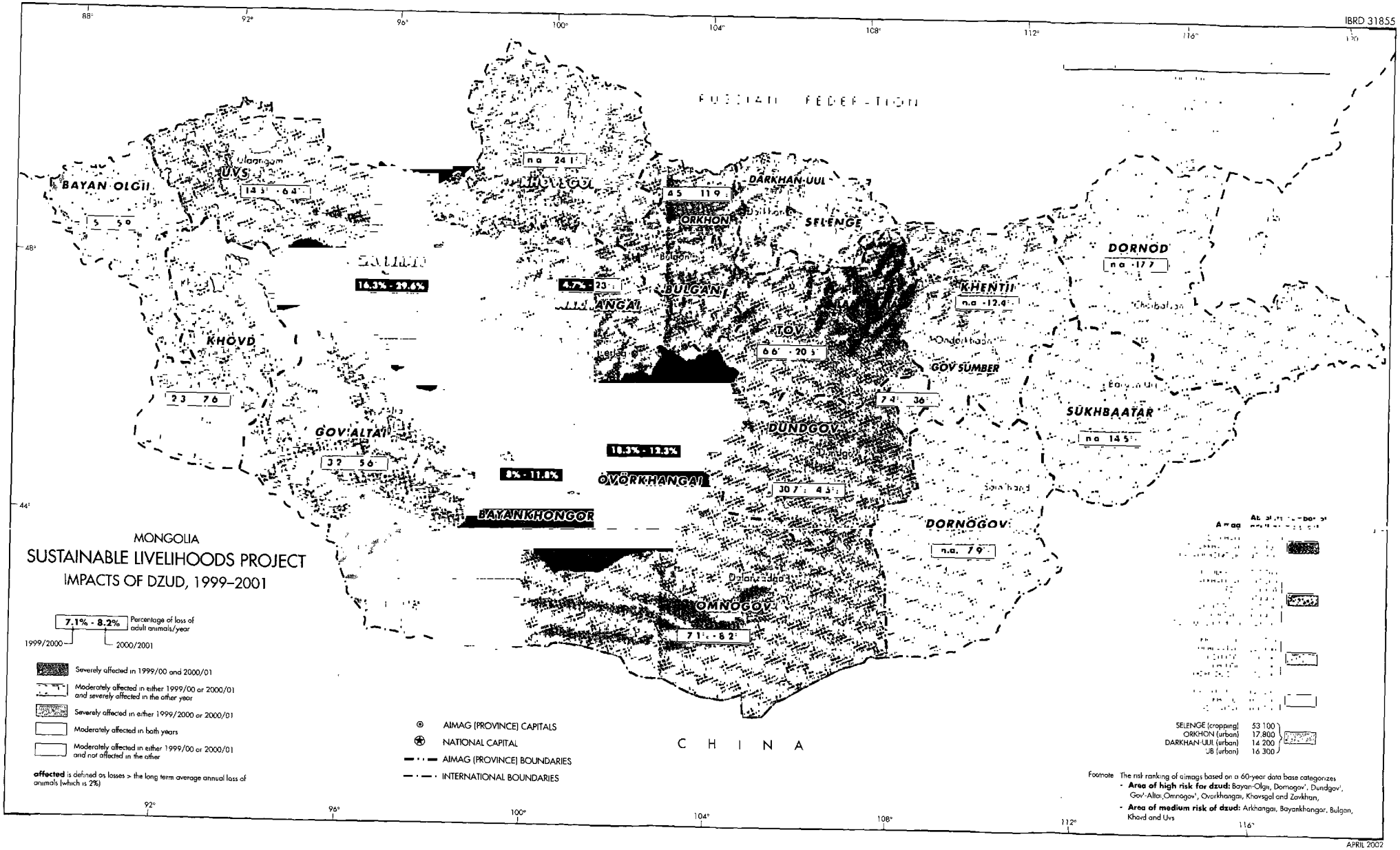

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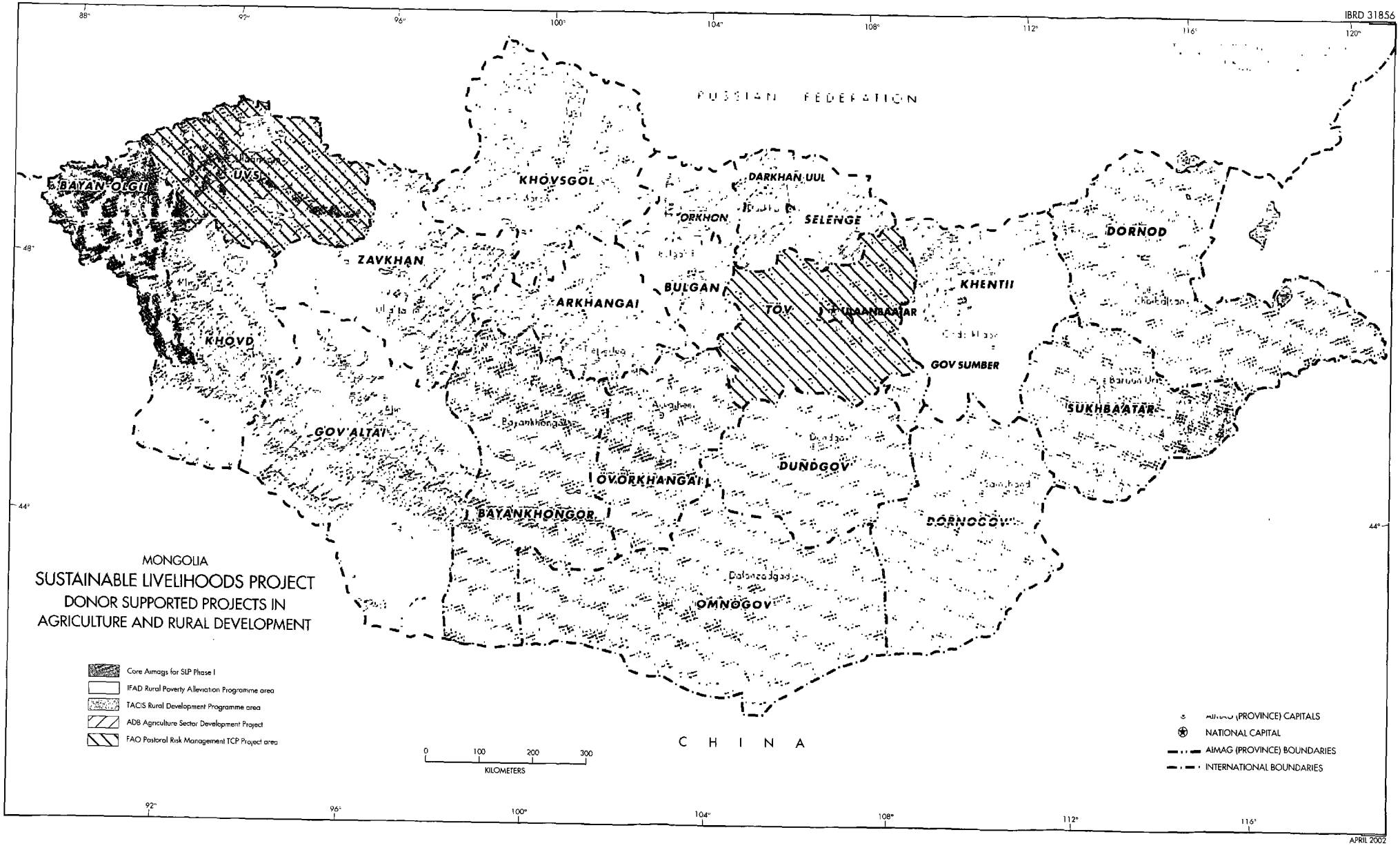
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GOV ALTAI
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OVORKHANGAI
BAYANKHONGOR
DORNOGOV
OMNOGOV
MONGOLIA
SUSTAINABLE LIVELIHOODS PROJECT
DONOR SUPPORTED PROJECTS IN
AGRICULTURE AND RURAL DEVELOPMENT
Core Aimags for SLP Phase I
IFAD Rural Poverty Alleviation Programme area
TACIS Rural Development Programme area
ADB Agriculture Sector Development Project
FAO Pastoral Risk Management TCP Project area
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KILOMETERS
CHINA
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