# ICR Review
Operations Evaluation Department

Report Number : ICRR10672

| 1. Project Data : | | Date Posted : 06/27/2000 | | |
|---|---|---|---|---|
| PROJ ID: | P001325 OEDID: C2062 | | Appraisal | Actual |
| Project Name : | Second coffee improvement | Project Costs (US$M) | 106.8 | 68.2 |
| Country: | Kenya | Loan/Credit (US$M) | 46.8 | 48.4 |
| Sector, Major Sect .: | Agro-Industry & Marketing, Agriculture | Cofinancing (US$M) | 18.0 | 0 |
| L/C Number: | C2062 | | | |
| | | Board Approval (FY) | | 90 |
| Partners involved : | Commonwealth Development Corporation, European Union | Closing Date | 09/30/1997 | 06/30/1998 |
| | | | | |
| Prepared by : | Reviewed by : | Group Manager : | Group: | |
| Madhur Gautam | Ridley Nelson | Ridley Nelson | OEDST | |

## 2. Project Objectives and Components

### a. Objectives

The main objective was to raise incomes of smallholder, small estate owners, and farm workers through increased productivity and quality improvements. Related objectives were to: (i) increase the country's foreign exchange earnings and help it maintain its position as an efficient high quality coffee producer; (ii) strengthen the institutional capacities of the key participating agencies.

### b. Components

The project sought to remove important production, quality , financial and institutional constraints by providing for investments to:

(a) improve 275 factories and construct an additional 65 in the cooperative sector; (b) provide credit for agricultural inputs; (c) finance the initial credit requirements and improve the institutional arrangements to formulate and implement an improved coffee payment system in the cooperative sector; (d) improve production and processing on 230 small estates; (e) increase Kenya's coffee milling capacity; (f) provide training and advisory services to trainers, cooperative and factory managers and farmers to upgrade existing coffee plantings and raise the proportion of high quality arabica coffee; (g) strengthen the planning, management and implementation capacities of key participating agencies.

### c. Comments on Project Cost, Financing and Dates

About US$5.1 million of the IDA credit was pending recovery and cancellation when the ICR was written . Final costs in US dollars are higher than expected at appraisal as a result of exchange rate fluctuations against the SDR . The Commonwealth Development Corporation (CDC) withdrew from the project very early in the project. Some project activities (mostly credit) were continued with the support of funds from the European Union after the project funds for the components were used up.

## 3. Achievement of Relevant Objectives :

Project achievements were mixed. Exogenous factors, including world market prices, climatic factors, and the impact of policy and institutional uncertainty negatively impacted on smallholder behavior and project outcomes . Soon after effectiveness, the Kenya Producers Credit Union members rejected plans to expand their milling capacity, leading CDC to withdraw its support. This meant that the small estates sector, funded by CDC funds, was also dropped from the project, neglecting a significant section of the coffee producing farms in Kenya . The project succeeded in reducing industry overheads through cost reduction in cooperative society operations, improving the payment systems, and introducing an advance payment credit scheme which improved farmers' cash flow . The project also helped improve the quality of smallholder coffee, resulting in better prices in world markets . Substantial progress was also made in training and in strengthening the key institutions involved in the project . The ICR states that low-interest credit given to farmers had a direct positive influence on farm incomes . However, it also notes that input use remained at sub-optimal levels and inputs are likely to have been diverted to other crops . The interest rates charged were below market rates and project funds have in general substituted for other credit schemes . Thus the actual impact of the project's farm input credit scheme is questionable . The ICR also notes that the Cooperative

Bank is faced with delays in loan recoveries. The component for factory development, also involving a credit scheme, fell short of its appraisal targets (24 new and 226 renovated factories against 65 and 275, respectively). This was due to a downturn in overall production after project effectiveness leading to a decision in 1993 to focus on renovations instead of building new factories. Although the factory capacity is currently underutilized, this component is expected to yield benefits in the long run, as production recovers. The component, however, did have a positive environmental impact, by introducing pollution reducing systems and developing new factory designs which are now industry standards. Another positive impact of the project was the electrification of factories, which helped reduce operating costs and production interruptions but has also introduced electricity in remote locations with significant developmental impacts.

**4. Significant Outcomes /Impacts:**

The project helped improve the payments systems and introduced an effective advance payments system, with positive impact on farmer incentives. The project also helped reduce cooperative societies' operating expenses and industry overheads, also to the benefit of farmers. The project has also yielded some unintended benefits through electrification of remote areas and positive environmental impacts through new pollution control systems in factories.

**5. Significant Shortcomings (including non-compliance with safeguard policies):**

The project did not address the main policy issues facing the industry relating to its institutional and marketing systems, namely the negative influence and political control of the Coffee Board of Kenya and the mismanagement of the cooperative restructuring process. This shortcoming proved to be critical in neutralizing the positive achievements of the project's activities. A significant proportion of the coffee producing farms, in the small estate sector, were left unattended to by the project.

| 6. Ratings: | ICR | OED Review | Reason for Disagreement /Comments |
|---|---|---|---|
| Outcome: | Unsatisfactory | Unsatisfactory | |
| Institutional Dev.: | Partial | Modest | |
| Sustainability: | Uncertain | Uncertain | |
| Bank Performance: | Satisfactory | Unsatisfactory | ICR notes supervision was deficient. It also notes the failure of project design in addressing key policy and institutional issues which ultimately led to undermining the successful project components. Project appraisal also apparently failed to verify the demand by the KPCU members for expanding their mill capacity, resulting in two major components of the project being dropped almost immediately after the project was declared effective. |
| Borrower Perf.: | Satisfactory | Unsatisfactory | Despite the high degree of ownership of project components by the individual agencies involved, satisfactory covenant compliance and timely counterpart funding, the governments failure to address the main policy and institutional issues is noted as the key factor in the project's unsatisfactory outcome. |
| Quality of ICR: | | Satisfactory | |

**7. Lessons of Broad Applicability:**

1. Issues concerning the policy and institutional environment in which a project is to operate need to be address up front to ensure the project has a reasonable chance of success.
2. Field based supervision can contribute to project success through timely and responsive client service and more efficient processing of project documents and procedural matters. However, the advantages of better management of micro-issues needs to be balanced by an objective and detached assessment of macro factors influencing project outcomes. The project could have benefited in this respect from periodic external assessments to identify emerging issues, at the sectoral level and in specific components.
3. The Bank and the project design also need to be more flexible in addressing major disruptions in the implementation of important sub-components. The small estates sub-sector was essentially ignored by the project after the withdrawal of CDC.

**8. Audit Recommended?** ○ Yes ● No

**9. Comments on Quality of ICR :**

The ICR is generally of very good quality. Its conclusions are based on sound and candid discussion of the main issues. However, it does not provide a satisfactory discussion of important issues pertaining to the project's credit operations, particularly the rationale and extent of subsidy, the impact of the subsidy on the allocation of credit and on the lending agencies.