Document of
The World Bank

Report No: 22286-EC

PROJECT APPRAISAL DOCUMENT

ON A

PROPOSED LOAN

IN THE AMOUNT OF US$25.2 MILLION

TO THE

REPUBLIC OF ECUADOR

FOR A

POVERTY REDUCTION AND LOCAL RURAL DEVELOPMENT (PROLOCAL)

PROJECT

June 8, 2001

Environmentally and Socially Sustainable Develpment
Bolivia, Ecuador and Peru Country Management Unit
Latin America and Caribbean Region

CURRENCY EQUIVALENTS

(Exchange Rate Effective September 2000)

Currency Unit = Ecuadorian Sucres
1 Ecuadorian Sucre = US$0.00003984
US$1 = 25,100 Ecuadorian Sucres

FISCAL YEAR

January 1 -- December 31

ABBREVIATIONS AND ACRONYMS

BGs	Beneficiary Groups
CAS	Country Assistance Strategy
CC	Credit Cooperatives
CGAP	Consultative Group to Assist the Poorest
CONAM	Council for State Modernization
CONCOPE	Council of Provinces
EFL	Local Financial Institutions
ERR	Economic Rate of Return
FAO	Food & Agriculture Organization of the UN
FISE	Social Investment Fund
FONLOCAL	Local Development Fund
GEF	Global Environment Facility
IADB	Inter-American Development Bank
IBRD	International Bank for Reconstruction and Development
ICR	Implementation Completion Report
IFAD	International Fund for Agricultural Development
IMF	International Monetary Fund
IRR	Internal Rate of Return
LACI	Loan Administration Change Initiative
LFI	Local Financial Intermediaries
LSPs	Local Service Providers
M&E	Monitoring and Evaluation
MAG	Ministry of Agriculture and Livestock
MBS	Ministry of Social Welfare
MIS	Management Information Systems
MOSTA	Ecuador Modernization of the State Project
NCB	National Competitive Bidding
NCU	National Coordination Unit
NGO	Non-Governmental Organization
NPV	Net Present Value
ODEPLAN	National Planning Office
OM	Operating Manual
PAT	Ecuador Irrigation Technical Assistance project
PDM	Ecuador Municipal Development Program
PIP	Project Implementation Plan
PMR	Project Management Report
PRODEPINE	Ecuador Indigenous and Afro-Ecuadorian Development Project
PROLOCAL	Poverty Reduction & Local Rural Development
PROMSA	Ecuador Modernization of Agricultural Sector
PRONADER	Ecuador Rural Development Project
QCBS	Quality and Cost Based Selection
RCU	Regional Coordination Units
SICA	Ecuador Information and Agricultural Census project
SOEs	Statements of Expenditures
SSRD	Subsecretary for Rural Development of MBS

Vice President:	David De Ferranti
Country Manager/Director:	Isabel Guerrero
Sector Manager/Director:	John Redwood
Task Team Leader/Task Manager:	Norman B. Piccioni

ECUADOR
POVERTY REDUCTION AND LOCAL RURAL DEVELOPMENT (PROLOCAL)

CONTENTS

Annexes

MAP(S)

ECUADOR

Poverty Reduction and Local Rural Development (PROLOCAL)

Project Appraisal Document

Latin America and Caribbean Region
LCSER

Date: June 8, 2001
Country Manager/Director: Isabel Guerrero
Project ID: P039437
Lending Instrument: Specific Investment Loan (SIL)

Team Leader: Norman Bentley Piccioni
Sector Manager/Director: John Redwood
Sector(s): BI - Institutional Development, IL - Small Scale Enterprise, MC - Community Action Program
Theme(s): Rural Development; Poverty Reduction
Poverty Targeted Intervention: Y

Program Financing Data

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

For Loans/Credits/Others:
Amount (US$m): 25.2
Proposed Terms (IBRD): Fixed-Spread Loan (FSL)
Grace period (years): 8
Years to maturity: 20
Commitment fee: 0.85% first 4 years, 0.75% thereafter
Front end fee on Bank loan: 1.00%

Financing Plan (US$m): Source	Local	Foreign	Total
BORROWER	2.87	0.00	2.87
IBRD	19.52	5.68	25.20
LOCAL COMMUNITIES	4.08	0.72	4.80
OTHER SOURCES OF BORROWING COUNTRY	7.61	1.48	9.09
Total:	34.08	7.88	41.96

Borrower: GOVERNMENT OF ECUADOR
Responsible agency: MINISTRY OF SOCIAL WELFARE

Estimated disbursements (Bank FY/US$m):

FY	2002	2003	2004	2005	2006			
Annual	2.40	5.40	8.10	6.40	2.90			
Cumulative	2.40	7.80	15.90	22.30	25.20			

Project implementation period: 5 years
Expected effectiveness date: 09/21/2001 **Expected closing date:** 12/31/2006

A. Project Development Objective

1. Project development objective: (see Annex 1)

To strengthen local empowerment, improve quality of local services, and increase access to productive assets to improve the well-being of poor households in selected micro-regions.

2. Key performance indicators: (see Annex 1)

The following benchmark indicators have been agreed to monitor the Project performance:

- 60,000 households take active role in elaborating own local development plans;
- 150 local governments collaborate with beneficiaries in generating development plans at the *Parroquia* and *Cantón* levels*;
- 80% of expected counterpart contributions are made available by local organizations;
- 30% of individuals participating in community development planning process are women;
- 80% of beneficiaries are poor;
- Beneficiary households improve access to productive assets;
- Beneficiary households improve access to quality rural development services;
- Income level of beneficiaries of productive projects improves by 15%;
- Underemployment among beneficiary households decreases by 20%.

* A *parroquia* is the smallest territorial administrative unit. More parroquias form a *Cantón* or municipality.

B. Strategic Context

1. Sector-related Country Assistance Strategy (CAS) goal supported by the project: (see Annex 1)

Document number: R2000-102[IFC/R2000-111] **Date of latest CAS discussion:** 03/25/97

During the last three years Ecuador has experienced a series of natural disasters and economic shocks which caused its economy to plunge into the most severe recession in modern times. The Bank Group's assistance program is first focused on short-term actions to protect the poor and restore macro-economic stability. The proposed project supports the program's medium and longer-term objective of promoting sustainable development and poverty reduction. More specifically, the Project will build on the lessons learned from eight years of implementation of the recently completed Rural Development Project (PRONADER, Loan 3390-EC). It will seek to capitalize on the recognition that communities and decentralized units have the potential to more responsively and efficiently provide key public services, while simultaneously creating employment opportunities for the poor.

2. Main sector issues and Government strategy:

Poverty was widespread and income inequality was pronounced even before this economic recession cut further real income and consumption of the poor and reduced the quality and quantity of basic public services. In 1998, the incidence of poverty in the country was estimated at almost 63%, up from 56% in 1995. Similarly, extreme poverty during the same period increased by more than 30%, from 20 to 27% (Larrea et al, 1999, data from 1995 and 1998 LSMS). Research carried out for the Bank's Poverty Assessment in 1996 confirmed that poverty is higher in rural areas, characterized by lack of education, lack of access to land, and few non-agricultural employment opportunities. The Bank's recent Gender Review found that the poor, but particularly women, have more limited access to the formal labor, land, and credit markets as well as to effective political participation. Correcting these inequalities is a strategic challenge for the country.

Instability in Ecuador's institutional framework and leadership is a serious problem -- during the last six years, there have been five presidents, 13 finance ministers, and eight Central Bank heads. Regional rivalries and fragmented political parties make consensus hard to sustain. Ecuador remains a unitary state with highly centralized systems of public service delivery. Public regulatory and administrative institutions are weak and inefficient, while corruption is a long-standing problem. There is increasing cynicism and lack of trust in the political process to address these problems. At the same time the economic crisis has severely reduced government resources to finance public services, and the shrinking banking system can no longer provide formal credit to support, let alone finance, an expansion in economic activity.

In the past, the growth of most rural activities has been based on expansion of land dedicated to agriculture, but this trend has required the poor to cultivate less productive land in jungle and mountainous terrain, with negative impacts on the country's biodiversity and environment. As a result Ecuador is losing its rainforests and coastal wetlands at an alarming rate. Soil and water resources are poorly managed, especially in the Sierra, the central region of the country.

To protect the poor and vulnerable groups from declining incomes in the short term, the Government has undertaken an Emergency Social Plan to target key social safety net programs and to provide direct assistance to these groups through school feeding programs and cash transfers. To improve the efficiency of public resource use and restore confidence in public institutions, the Government is accelerating its program to reform and modernize the state. This will require both political and financial decentralization of management and decision making to sub-national entities. Congress passed a law in October 1997 which lays out the framework and principles for this, but as yet no regulations have been written. The next step is to develop a national consensus on more precisely how decentralization should occur and to begin the process. There is increasing political support for the struggle against corruption. The government has recently created several high-level commissions which are proposing changes to criminal procedures, codes on public contracting and administrative procedures to ensure conformity with legal norms and ethical principles.

Last year Congress passed a comprehensive umbrella Environmental Law that provides the framework to tackle most environmental issues, and the Government intends to at least maintain public expenditure for environmental protection activities during its IMF-approved stabilization program. The Government, with help from the Bank and FAO, is developing a national water resources strategy, and has prepared a national water use law for approval by Congress. Land issues in Ecuador are being studied in a cooperative program with the Bank, IDB and FAO, with the objective to develop an action program to improve land markets. The Ministry of the Environment is revitalizing its national program of biodiversity protection. Its program would be financed by GEF, foreign foundations and debt swaps, and implemented primarily by NGOs.

To address these issues, the Government released in August 2000 the comprehensive policy document *Plan de Gobierno 2000-2003*, which emphasizes the importance of: (i) social capital development based on the organization, (ii) human capital formation based on education and services, and (iii) access to productive assets based on the sustainable use of the productive potential of the natural resources of the country (Vicepresidencia de la República del Ecuador, ODEPLAN, Plan de Gobierno 2000 - 2003: Hacia un nuevo rumbo, Quito, August, 2000). In line with the Government's poverty reduction strategy, PROLOCAL builds on these three pillars, which are at the core of its execution strategy.

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

The Project would specifically support environmentally sustainable development in selected poor rural areas with an emphasis on narrowing the income gap between rich and poor. To be effective, economic growth must have a broader base, which includes the disadvantaged, such as women, in the lowest income groups. Surveys undertaken as part of the Ecuador Poverty Assessment have determined that these groups have almost no access to centrally- managed, productivity-enhancing public services such as technical assistance, market information, and transport infrastructure. Their local communities are usually poorly organized and also dependent on centralized services that are seldom delivered. There is a general recognition that the current system is broken and cannot be fixed, and that decentralization is the most likely answer. Unfortunately the new political and administrative model has not been devised, so the Project would go outside the current system to a large extent, to work directly with poor rural communities. PROLOCAL would attempt to transform dependent communities into proactive groups, empowered to address their development problems.

Traditional, informal systems of participation at the community level would be used to take decisions on the allocation of Project resources for rural investments and human capital formation. Project financial resources and contracting would also be managed at the local level, though supervised and audited by the center. TA services for participatory planning would be contracted from NGOs and private companies. The Project design would emphasize a strategy of participation and inclusion and would recognize that rural development depends on the linkage between farm and off-farm, vertical integration, and peri-urban economic activity.

This approach, of using communities and their territorial or second-tier organizations to implement the Project, would follow the arrangements being carried out by the Bank's Indigenous and Afro-Ecuadorian Development Project (PRODEPINE, Loan 4277-EC) approved in 1998. While PRODEPINE depends on ethnic affinity groups to channel resources, PROLOCAL would work with non-indigenous peasant communities, and its intervention would focus on different geographic areas. Although the Ecuador Poverty Assessment confirmed the linkage between poverty and access to land, the Project would not seek to address this problem specifically. The Government agencies responsible for dealing with land ownership are weak, the studies to define possible reforms are not complete, and time would be needed to develop a political consensus on future action.

C. Project Description Summary

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

Expected to last five years, the loan will start financing activities in two micro-regions, and it will progressively extend to an additional four micro-regions. Activities to be financed are grouped under four components.

Component A: Local Development Planning

The component will promote social capital formation by supporting planning for local development at (i) community, (ii) Parroquia and (iii) Cantón levels as part of a participatory development planning process. Rural communities would identify priority subprojects, a subset of which would be selected for streamlined preparation and execution. Community representatives would participate in a similar planning process at a higher, Parroquia level where similar community subprojects might be integrated in Parroquia subprojects. By the same token, Cantones would prepare their development plans which could include linkages to those of Parroquias and their subprojects.

Component B: Local Development Services

The component will train the various local stakeholders of the Project, so that they can successfully play their roles. Through a tiered sequence of activities, the Project would first contract competitively with nationally organized networks of NGOs with experience in training their own members. These groups would: (i) survey the existing technical skills in the target micro-regions and prepare capacity gap analysis; (ii) prepare and implement training programs to address local gaps and pass on the Project methodologies to be followed during implementation; (iii) promote the formation of local networks[1] of the technicians trained, certifying their capabilities to participate in the next phase of project implementation. In phase two of the training, these certified technicians would train the leadership and technical staff of the organizations which will identify and implement subprojects. In a third sequential or parallel phase, these certified local consulting service providers would provide technical assistance to local governments at the community, Parroquia and Cantón level to promote democratic participation and transparent management and administration.

Component C: Subprojects

The component will improve access to public good assets by establishing a demand-driven, matching-grant fund to finance technical assistance, infrastructure, productive capacity of socio-territorial organizations, and environmental investments. Technical screening of identified subprojects would be undertaken by project technical personnel at the regional level, according to criteria in the Operating Manual (OM). Each subproject would be implemented on the basis of a contract between the Regional Coordination Unit and the beneficiary group (BG). If the BG did not have the proper legal status, activities would be carried out by a third party, selected by the group, through a tripartite contract. BGs would be responsible for mobilizing counterpart funds from beneficiaries, administration of funds, contracting, and supervision of subproject implementation. NGOs would provide TA to fill those gaps in BGs' implementation capacity identified during subproject preparation, and would monitor counterpart contributions. Project administration personnel at the regional level would monitor subproject expenditure accounts. The component would finance around 600 community subprojects, 120 Parroquia subprojects, and 30 inter-Parroquia subprojects.

Component D: Project Coordination Unit

The component would finance costs for consultant services and equipment to carry out managerial, financial and technical coordination through a Project Coordination Unit (PCU). Under a Board that represents the public and private sectors, the PCU will be composed of a National Coordination Unit (NCU) at central level, and of up to six Regional Coordination Units (RCUs), one for each micro-region. Core staff at the central level will include an Executive Director, a Technical Coordinator, an Administrative Coordinator with financial management functions, a Procurement Specialist, three Technical Specialists for the components, a Specialist in M&E, a Specialist in communications, a Specialist in gender (shared with PROGENIAL Project) and a System Specialist. Staff at the regional level will include a Regional Coordinator and three Technical Specialists.

[1] A network is defined here as a group of development service providers, formal or informal, governmental, non-governmental or mixed, linked geographically, functionally or institutionally. In the last five years, networks have become the alternative and primary poverty reduction tool in poor micro-regions.

Component	Sector	Indicative Costs (US$M)	% of Total	Bank-financing (US$M)	% of Bank-financing
(A) Local Development Planning	Community Action Program	2.98	7.1	2.33	9.2
(B) Local Development Services	Vocational/Technical Education & Training	7.43	17.7	5.89	23.4
(C) Subprojects	Institutional Development	25.47	60.7	13.12	52.1
(D) Project Coordination Unit	Institutional Development	5.83	13.9	3.61	14.3
Total Project Costs		41.71	99.4	24.95	99.0
Front-end fee		0.25	0.6	0.25	1.0
Total Financing Required		41.96	100.0	25.20	100.0

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

PROLOCAL will not support any major policy and institutional reform. It would on an *ad hoc* basis promote transfer and delegation of responsibilities to local government entities, and greater participation by dependent provincial government entities.

3. Benefits and target population:

Benefits. Major benefits expected from the Project would include: human capital formation in local institutions and organizations; social capital building through empowerment of local organizations and communities; poverty reduction through increased employment and income generation of poor households; and improved natural resource base and environmental conditions. Income increases would essentially come from improved land and labor productivity, production value added, and increased employment opportunities. Local development subprojects would be oriented toward increased household incomes and environmental conservation. Human capital formation and empowerment of local actors would contribute to the proper execution and control of development subprojects in the short-to-medium term, and to the sustainability of local development in the longer term.

Target area and population. As a program of targeted intervention, PROLOCAL would reach the most vulnerable groups of the population through targeting at different levels. In its first level, geographical targeting would permit the Project's resources to be concentrated on those territorial entities with the greatest developmental need. A total of 120 Parroquias in 31 Cantones, grouped in 6 micro-regions, were identified as the result of a process which involved the use of statistical information and inputs from participatory exercises at the community level[1]. The Project would cover up to 19,000 square kilometers, or 8% of the national territory, and would include more than 800,000 people, of which almost three quarters are poor. This latter group, of approximately 600,000 people, represents the Project target population. Despite the already very high levels of poverty exhibited by each of the 120 selected Parroquias, a second level of targeting would make an additional effort to exclude ineligible households from accessing the Project's resources through a community-based, consensus-building process. This screening process will consider: (i) the positive externalities of heterogeneous groups reflecting the socio-economic make-up of the community; (ii) the social and administrative costs of second-tier targeting; and (iii) the moral costs associated with unintended exclusions. The effectiveness of the targeting methodology will be assessed through the Project monitoring system, as well as on the basis of the proposed ex-post evaluation study and the annual beneficiary assessments (Cfr. Annex 12 for details).

[1] South of Manabí, Western Los Ríos, Central Los Andes, Eastern Loja, High Watershed of Jubones River, and Watershed of El Angel River.

4. Institutional and implementation arrangements:

Implementation period: The loan is expected to become effective in September 2001, for a five year implementation period. It will terminate in June 2006.

Execution: The Project will be executed through an autonomous Project Coordination Unit (PCU) composed of: (i) a National Coordination Unit (NCU) and (ii) up to six decentralized regional units (RCUs), one for each micro-region. The PCU will report to the PROLOCAL Board, established by the Presidential Decree of March 15, 2001. The Board is presided over by the Minister of Social Welfare and includes the Sub-secretary of Rural Development of the Ministry of Social Welfare, the Minister of Environment, the Executive Director of ODEPLAN, and two representatives from national networks of NGOs.

Implementation: NGOs, Academia, *Juntas*, grass-roots organizations, producers' associations, and other Local Services Provides (LSPs) would implement components A and B, and Beneficiary Groups (BGs) would implement component C through contracts with RCUs.

Financial arrangements: PMRs would be used as the basis for quarterly disbursements from the Bank to the Project's Special Account. The NCU would make monthly transfers to the RCUs based on their approved annual operating plans and justification of prior disbursement. Each BG implementing a subproject would have a bank account and would receive transfers from the RCU based on the approved subprojects disbursement schedule. The correspondent RCU would provide physical and financial oversight, and would audit executing entities. Annual project financial audits, carried out by independent auditors acceptable to the Bank, would include a sample of subprojects within each region.

Procurement arrangements: The PCU would oversee project procurement including procurement training, approvals, supervision and auditing. Annex 6 specifies thresholds for prior review for BGs, RCUs and NCU. Procurement for components A, B and C would be handled by BGs. The LSPs would provide assistance to BGs, to carry out the procurement function on their subprojects based on the capacity to manage procurement. RCUs would provide backstopping and carry out procurement audits on subprojects.

Monitoring and evaluation: The Project's M&E system will consist of four modules: (i) a Management Information System (MIS), which will track the Project's progress on a set of process indicators and feed into management's decision-making; (ii) annual beneficiary assessments, which will provide the target group's perceptions of and reactions to Project progress; (iii) an impact evaluation study, which will quantify the final impact which can be attributed to the Project; and (iv) standard auditing and supervision missions, which will review the technical and fiduciary aspects twice a year or more often if required. RCUs would monitor components A and B directly, and LSPs would provide monitoring inputs to RCUs on components A, B, and C. The NCU will aggregate all monitoring and evaluation inputs for project-level decision making and reporting. The beneficiary assessments and the impact evaluation study will be contracted out, and the NCU, in the person of the Evaluation Specialist, will be in charge of the coordination and technical supervision of the studies. World Bank staff and consultants will be responsible for periodic supervision missions.

Expansion to additional micro-regions: The Project activities will start in two micro-regions. Tentatively, after two years of implementation, specific trigger indicators will be evaluated in order to assess readiness to expand up to four additional micro-regions (see addendum to Annex 1 for a complete list of the trigger indicators).

Project Implementation Plan (PIP) and Operations Manual (OM): The Project Implementation Plan (PIP) will be broken down into Annual Implementation Plans (AIP). The AIP will be the principal tool for coordination between the NCU and RCUs. AIPs would be prepared by the NCU and RCUs, approved by the PROLOCAL Board and presented to the Bank for no objection before the beginning of the budget year. The Operational Manual (OM) would include rules and regulations on the operation of all components of the Project. Updates in the OM would require the no objection of the Bank.

D. Project Rationale

1. Project alternatives considered and reasons for rejection:

For reasons outlined in Part B above, the proposed project would not follow the design of the Rural Development Project (PRONADER) as a "repeater". The Government's demonstrated lack of capability to successfully administer centrally-controlled projects called for a new approach. Two options for implementation were considered. Since the Decentralization Law of 1997 calls for provincial and municipal governments to take more responsibility, Project preparation explored the feasibility of operating through these entities and of including an objective to strengthen these institutions as agents of local development. However the continuing lack of legal regulations to clarify responsibilities at this level made this option impractical at this time, and it was dropped. The second option of relying on local communities to identify and implement activities to be financed by the Project was adopted instead. This approach would not preclude a future role in this Project for municipalities and other sub-national political entities, if legal definitions in this respect can be clarified.

The PRONADER project was managed by the Ministry of Social Welfare (MSW) as an internal activity of its Sub-Secretary of Rural Development (SRD). This arrangement proved cumbersome, bureaucratic, and exposed project staff to the internal politics of a ministry with constantly changing top management. The proposed project will therefore rely on a temporary, independent and decentralized Project Coordination Unit outside the bureaucratic chain of command.

The Government has managed much of its investment in rural infrastructure for education and public health through its Social Investment Fund (FISE), previously financed by the Bank (Loan 3707EC, which has closed). During project preparation the Bank and the Borrower seriously considered using FISE as the financial agent for the proposed project, but decided against it. FISE's more recent record in managing a

project financed by other multilateral development banks has been disappointing in several respects. It was agreed that the time and effort needed to strengthen FISE would delay project launch and add activities which would dilute the Project's primary objectives.

2. Major related projects financed by the Bank and/or other development agencies (completed, ongoing and planned).

The issues related to rural poverty are addressed most specifically by the Bank's PRONADER (recently completed), PRODEPINE and Irrigation Technical Assistance projects, while IFAD, FAO and the Netherlands also have projects in this sector. Governance issues revolving around decentralization, regulation, administration and corruption have been addressed in the Bank's PDM and MOSTA projects, and IADB's PAM project strengthens municipalities. The Financial Sector TA project is helping the Government to restore the formal banking sector. IADB has a project to provide credit to small and medium enterprises, and Swisscontact (an international NGO) is working to strengthen a network of unregulated credit cooperatives. The Bank's PROMSA and SICA projects are working to improve agricultural services, while IADB has recently completed a project to strengthen agricultural sector policy. The Bank's PATRA and the GEF I and II projects are addressing environmental and biodiversity management problems. IADB has financed the FISE II project to help communities build health and education infrastructure.

Sector Issue	Project	Latest Supervision (PSR) Ratings (Bank-financed projects only)	
		Implementation Progress (IP)	Development Objective (DO)
Bank-financed			
Rural Development	PRONADER	U	U
Indigenous and Afro-Ecuatorian Communities	PRODEPINE	S	S
Municipal Development	PDM - WB, IADB and GTZ	S	S
Irrigation – Technical Assistance	PAT – Irrigation	S	S
Modernization of the State	MOSTA	S	S
Modernization of Agricultural Sector	PROMSA	S	S
Information and Agricultural Census	SICA	S	S
Other development agencies			
Agricultural Sector Policy	PSA –IADB		
Credit - Small & Medium Scale Firms	Several – IADB		
Rural Development	Several – IFAD		
Support to Financial Intermediaries	CREA – Swisscontact (NGO)		
Assistance to Municipalities	PAM – CORDES (NGO)		
Food Security	PESA - FAO, FECD (NGO)		
Community Forestry	DFC - FAO, Netherlands		
Health and empowerment	PES Loja -PHO, Netherlands		

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

3. Lessons learned and reflected in the project design:

The findings of PRONADER's Implementation Completion Report, recently finalized, have been carefully reflected in the design of PROLOCAL. The single most important finding was that project outcomes were continually handicapped by an unstable political and economic environment. The new Government's economic policy reforms are expected to ameliorate this situation in the future, but in the meantime the proposed Project has been designed to better deal with these problems. An independent Project Coordination Unit would insulate management staff from the frequent changes in political leadership. The length of project implementation has been shortened to five years in order to maintain its focus and client commitment in an unstable political environment. The number of objectives and the corresponding components have been reduced to sharpen focus. The Government (MSW) responsibility for rural development will change from active intervenor to coordinator, regulator, and monitor of mostly private actors. The centralized approach will be replaced by a demand-driven and localized decision-making process. This will allow communities to custom design Project financed activities to reflect their geographic and cultural diversity.

The Bank's regional experience in rural investments shows that: (i) when subprojects are selected in this way, they are more likely to meet the community's needs than if they are chosen to reflect the priorities of a government agency; (ii) when a community develops a sense of ownership in a subproject, it is more willing and interested in sharing its costs and ensuring its maintenance; and (iii) once a community is given the responsibility for implementing a subproject that it identified and prepared, it has a great interest in ensuring that the private contractor chosen does it properly and honestly.

The former emphasis on agricultural production as the engine for rural development has been changed to recognize the importance of value added chains, access to markets and complementary, off-farm activities linked to urban centers. The evaluation for PRONADER showed that the sustainability of many value-added community activities and investments was compromised by a lack of local management skills and market knowledge. It also found that many activities never got started due the low levels of social capital in rural areas. Social/political links and trust between local economic and political actors, both public and private, were weak or missing. The proposed Project will have three of its four components focused on improving these deficiencies. In addition, technical assistance activities would train these community groups in subproject preparation, appraisal, procurement, environmental protection, accounting and control. All subprojects would be subject to minimum economic eligibility criteria.

4. Indications of borrower commitment and ownership:

Project identification was overseen by two institutions in the Office of the Presidency: the National Planning Office (ODEPLAN) and the Council for State Modernization (CONAM). The President publicly endorsed the concept and assigned responsibility for project preparation to the Ministry of Social Welfare. The vice-presidency, through the *Fondo de Solidariedad*, committed counterpart funds. Civil society has been actively involved in identification. At the beginning, four thematic working groups or support networks were formed to provide guidance, feedback and perform specific tasks. A group for institutional policy and decentralization had 17 institutions led by the Association of Municipalities (AME) and Council of Provinces (CONCOPE). Groups were also formed for human capital development (27 institutions), rural finance (13), and sustainability and integration (41). Several bilateral and multilateral donors also participated.

5. Value added of Bank support in this project:

The Bank has a long history of involvement in rural development issues in Ecuador. Also, over time the Bank has developed, through its PRODEPINE project in Ecuador, techniques in local participation which

are being transferred to the proposed Project. These can be complemented by the Bank's positive experiences from other countries in the region.

The Project is designed to rely on communities for implementation, while Government defines in more detail its role in a decentralized political system. The Bank's involvement in the Modernization of the State Project (MOSTA) and the Municipal Development Program (PDM) will provide important links to PROLOCAL in this respect.

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

1. Economic (see Annex 4):

● Cost benefit NPV=US$17.8 million; ERR = 18.9 % (see Annex 4)

○ Cost effectiveness

○ Other (specify)

Costs. Total project costs were included for the economic feasibility analysis. Investment and recurrent costs of potential subprojects were obtained from the economic and financial analysis in project files.

Benefits. Benefits generated by local investment subprojects include: revenues from increased production and value added; increased natural assets such as commercial and conservation forests; and improved health reflected in reduction of treatment costs. Non-quantified benefits include *inter alia*: increased water supply and soil conservation, due to proper watershed management; greater social cohesion or social capital; increased local development capacities or human capital; and expanded rural financial markets. Non-quantified negative externalities may also be generated, such as social conflicts associated to community priority setting, community subproject selection and subproject failures.

Aggregate Net Benefits. For projection purposes, aggregate economic benefits and costs were calculated for one, two and three rounds of potential subprojects (Tables 1 and 2, Annex 4). The subprojects analyzed would generate around US$17 million of economic benefits in present value and reach around 20,000 families. However, subproject failures may significantly reduce these benefits. Considering total Project costs, one round of subprojects would generate US$1.9 million of discounted net benefits. Required local investment funds would be around US$17.8 million. Two rounds of subprojects would generate US$18.8 million of discounted net benefits. Required local investment funds would be around US$24.8 million. Three rounds of subprojects would generate US$35.7 million of discounted net benefits. Required local investment funds would be around US$37.2 million. Project economic NPV and IRR could have been calculated with available information. However, considering the lack of certainty on overall Project performance, as it is largely determined by beneficiaries during implementation, they were not included as feasibility reference indicators.

Overall Sensitivity and Risk Mitigation Measures. Considering aggregate benefits of analyzed subprojects, the Project switching value would be 12% benefit reduction value in terms of economic feasibility. These margin of benefit reductions translate into a reduced margin of acceptable subproject failures. Thus the Project has been designed so as to minimize subproject failure risks, through participatory planning, technical support during subproject preparation, on-site beneficiary training, and subproject screening and design. Subproject co-financing arrangements would allow for healthy project/beneficiary risk sharing.

2. Financial (see Annex 4 and Annex 5):

NPV=US$ 34.6 million; FRR = 25.7 % (see Annex 4)

Revenues. Financial revenues generated by local investment subprojects include *inter alia*: revenues from increased production and value added; revenues from potential sale of forest products; and reduced family

spending as a result of reduction of medical treatment costs.

Subproject Feasibility. As shown in Tables 1 and 2, most feasible subprojects would be organic agriculture and artisanal sugar-cane processing. In terms of the execution level, community subprojects showed higher financial Net Present Values. On average, community subprojects yield a financial NPV of US$1,400/family. In terms of micro-regions, higher feasibility indicators were found in *Estribaciones Centrales de Los Andes* and *Región Sur de Manabí*. On average, subprojects in such regions yield a financial NPV of US$2,300/family, and US$1,000/family respectively. Finally, Agribusiness/service-supply showed higher financial Net Present Values. On average, these subprojects yield a financial NPV of US$2,800/family. However, as shown below, they are fragile in terms of potential benefit reductions.

Subproject Sensitivity. Considering the relatively high risk of failure of subprojects, generated by demand-driven investment projects, switching values of benefit reductions were calculated for analyzed subprojects. Most analyzed processing/service-supply subprojects appear fragile. They would have feasibility problems if estimated benefits are reduced by 2-20%. Noteworthy exceptions would be sugar-cane processing subprojects and associative input supply and technical assistance subprojects. In contrast, most agricultural subprojects seem to be moderately robust as their estimated benefits could be reduced by 30-50% before their financial NPV became negative.

Fiscal Impact:

Considering no recovery of value-added tax (most likely situation in rural areas and micro-enterprises) one, two and three rounds of analyzed subprojects would generate US$5.6 million, US$11.2 million and US$16.8 million, respectively, in taxes at present value –amounts significantly smaller than total discounted project costs. Rice production, processing and marketing subproject (in *Región Occidental de Los Ríos*) would generate around US$1.6 million of fiscal revenues –significantly higher than any other subproject.

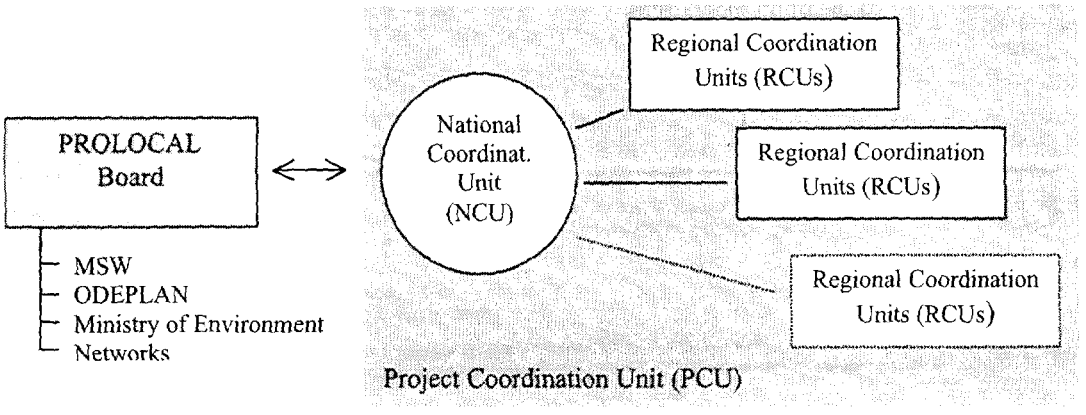
3. Technical:

The Project follows best practice for the design of rural and community-driven development programs and has been targeted to the poorest communities based on relevant criteria. It uses the principles of participation and empowerment to help communities select and implement their own productive investments. The methodologies to be followed have been largely validated in the PRODEPINE project, which has been under implementation for two years. Although the subprojects in Component C cannot be identified in advance (the process is demand-driven), models of probable investments have been validated. The capacity of the MSW to implement this Project is very limited, so it will contract with LSPs to deliver most project services.

4. Institutional:

4.1 Executing agencies:

The Board of PROLOCAL, presided by the MSW, will be responsible for project implementation through the Project Coordination Unit. While the NCU will be established up front, RCUs will increase in number (up to six) as the Project rolls out.



4.2 Project management:

The design of this Project assumed that political decentralization will take place in the future. The Project management arrangements therefore will not seek to build a permanent institutional entity which will prove irrelevant when decentralization occurs. The use of RCUs will de-concentrate administrative capacity to the rural areas, establishing local units where the subprojects will be implemented by BGs. According to the Project's administrative staffing plan, in the first year of Project implementation, 37 staff are planned for administration with a gradual increase to a maximum of 75.

4.3 Procurement issues:

A procurement assessment was carried out by authorized World Bank staff in February 2001 and certified accordingly. At the time of the assessment the Project was not expected to satisfy the Bank's minimum procurement requirements. An action plan to remedy this situation has been agreed with the MSW and the PROLOCAL team. According to the action plan, staffing requirements at the national level include one procurement specialist with substantial experience in Bank-financed procurement and support staff as needed. At the regional level up to six procurement specialists would be hired, one for each RCU. If recruits at the RCU level do not have Bank-financed procurement experience, procurement training will be provided. Training would also be provided to LSPs on Bank procurement requirements. These LSPs, along with RCU staff, would oversee the procurement of goods and services by grassroots executing groups.

The Project would utilize LACI PMR-based disbursement. A PMR reports-generating system would be installed in the national and regional units. Additional actions, include the adoption of a procurement operations manual, with a description of procurement responsibilities, processes, and internal controls, establishment of a reliable and secure filing system, and preparation of standard procurement documents acceptable to the Bank, including NCB documents, formats for shopping, and a contract for individual consultants. The current risk rating, based on the situation at the time of the assessment is "average". A Country Procurement Assessment has been carried out in April 2000. In the Bank's opinion, the general risk assessment of Ecuador is "high".

4.4 Financial management issues:

A financial management assessment was carried out by an authorized World Bank staff in February 2001 and certified according OP/BP 10.02 and the Project Financial Management Handbook dated February 1999. According to the assessment, the Project did not meet the Bank's minimum financial management requirements. An action plan has been agreed and progress monitored. Action plan items include the following: at the national level, staffing would require a financial administrator and an accountant. At the

regional level, up to 6 financial specialists/accountants would be hired, one for each RCU. In the selection criteria, preference will be given to those with Bank-financed financial management experience. An accounting system will be installed prior to project effectiveness in the national and regional offices and within 6 months of effectiveness date, will produce the financial management PMRs. A Financial Management Manual including policies and procedures for Planning, Budgeting, Accounting, Reporting, and Auditing will be prepared and approved by the Bank before Project effectiveness. Project chart of accounts and Audit Terms of Reference in accordance with the Bank Guidelines and Terms of Reference for Audits of Projects with Financing by the World Bank have already been approved by the Bank.

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.

The proposed Loan will finance small-scale rural development projects under Component C, where the range of environmental issues to be considered will be relatively narrow and specific. Most of these subprojects will not be located in environmentally sensitive areas. There will be a set of stand-alone environmental subprojects that will generate positive environmental impacts. However, because these investments cannot be identified *ex-ante* (only subprojects models have been identified), the Project is rated B. An environmental baseline survey was carried out for the six micro-regions, and environmental safeguard policies have been included in the Local Investment Fund Operational Manual. The survey, which includes a subprojects typology with a negative list and categories (A,B, and C, following the Bank's system) has been used to prepare the Operational Manual.

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

The survey provides a description of relevant physical, biological and socio-economic characteristics of these areas. The analysis was based on a review of available secondary information and complemented with information collected at the field level. The findings of the survey provide: (i) strategic guidance to the Borrower on prioritizing investments for financing; (ii) the context and recommendations for mitigation or prevention measures appropriate for different subproject types; (iii) the draft questionnaire to be used in the screening process; and (iv) guidance on which local environmental issues should be included in the capacity building and TA activities with communities and beneficiary groups. Screening using the questionnaire would identify subprojects requiring impact mitigation strategies. These would be reviewed by an environmental specialist (ES) attached to the PCU, in accordance with environmental criteria and analysis procedures included in the OM. The agreed environmental assessment procedures for subprojects are shown in Annex 13.

5.3 For Category A and B projects, timeline and status of EA:

Date of receipt of final draft:

The results of the environmental survey are discussed in Annex 13.

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?

Various environmentally sensitive NGOs are participating in the recently established inter-institutional working groups or support networks for the Project. These include: National Consortium for Training in Sustainable Management of Renewable Natural Resources (CAMAREN), Cotacachi Organic Coffee, Manabi Organic Coffee, Ecuatorian-Canadian Development Foundation (FECD), Cayambe Organic Vegetables, Chimborazo Organic Vegetables, and MCCH. The Ministry of Environment, as a member of the board of the PROLOCAL, has been actively involved in the preparation of terms of reference and

screening of consultants for the preparation of the EA.

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?

Subprojects implementation would be monitored by the Project Coordination Unit and operational audits performed on a sample basis by a specialized NGO.

6. Social:

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

A social assessment (SA) was carried out on four representative Cantones of the six micro-regions to be covered by the Project. The SA, which is summarized in Annex 14, broadly mapped potential stakeholders and identified their prior development demands. The analysis of this information highlights that unemployment, low local productivity, non-availability of credit and limited access for local decision making are identified by local settlers as aggravating facts of their poverty condition.

The Project is expected to increase social inclusion by promoting local empowerment. It is designed to strengthen the local capacity for the official decentralization process by improving the ability of local organizations to formulate participatory development plans. The social impact of these activities is expected to be positive, though the demand-driven nature of the process makes the results difficult to predict at this time. The SA provided base-line indicators which will be used in the monitoring and evaluation process and the periodic Beneficiary Assessments. The findings of the SA were an input for the Project's Gender Policy, Communications Strategy and Participatory Planning Methodology.

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

At the design and preparation phase, the social assessment methodology was mainly participatory, as it actively involved informants of each micro-region and carried out 125 semi-structured interviews, and 25 workshops with the participation of 500 people. Beginning in year two of implementation, a beneficiary assessment will be carried out, offering a high degree of involvement to all the stakeholder groups, including project staff members, NGOs' workers, municipalities and local power executives, communities and local organizations leaders, and, above all the rural poor themselves. This will allow the Project to be permanently in line with the perceptions of all the key actors for project implementation, and confer to the intended beneficiaries a strong capacity to monitor the implementation, evaluate the impacts of, and participate in depth in the Project. The planning is to be done with participatory methodologies to promote empowerment and reinforce social control and local governance. The objectives of the planning process are to seek inclusion and equity in decision making and to increase local empowerment and stakeholders' commitment.

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

Representatives of national NGO networks will be permanent members of the PROLOCAL National Council, the board of the Project Coordination Unit. NGOs and other civil society organizations such as handcrafters, irrigation water associations (*Juntas de Regantes)*, Peasant Social Security (*Seguro Campesino),* etc., on a demand-driven basis are likely to be the service providers for PROLOCAL's implementation. Among governmental institutions, municipalities are perceived by the locals as political rather than operational.

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

development outcomes?

PROLOCAL will promote alliances between local institutions and national and international NGOs. National networks of service providers will be contracted to organize local correspondent networks and train their members. Where local organizations lack institutional capacity, a local NGO would act as an intermediary for implementation. When needed, the Project would also provide support to the BGs to formalize their juridical status. Detailed eligibility criteria for the selection of BGs are to be found in the Operational Manual.

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

The first level of monitoring of project activities with regard to the local effects will be made through the Project monitoring system, essentially for physical and financial inputs/outputs. At the second level, the beneficiary assessment (BA) would allow for the early detection of bias in Project implementation, using information from the beneficiaries themselves. The BA would also be an instrument of evaluation, which would measure to what extent the outputs of the Project were effectively received, accepted and owned by the poor, and would assess the changes the Project introduced in social structures, capacities, relations, conflicts, local powers, incomes, and inclusion.

The dissemination of the BA findings, for confirmation and re-orientation of Project activities and stakeholders' roles, is planned through workshops at the local and regional level. The Project also envisions a higher level evaluation of the expected social development outcomes in the form of an impact evaluation study based on a longitudinal-control design. The aim of the system is to provide policy-makers with a rigorous quantitative assessment of the effects of the Project's innovative approach on a number of performance and impact indicators, as reported in the Logical Framework in Annex 1. Finally, periodic WB evaluation missions will provide an additional input to the Project's performance assessment (Cfr. Annex 12).

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 (OD 4.30)	○ 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.

To ensure that subprojects financed under Component C comply with the applicable safeguards, a simple standardized questionnaire will be adopted to identify any need for mitigation measures. The Project Coordination Unit would review and approve the measures proposed. If the necessary measures proved unacceptable to the beneficiaries, the subproject would not be financed.

The Project also complies with OD 4.20 (indigenous people). By definition PROLOCAL does not intervene in areas with indigenous communities (see annex 13, the Social Assessment and the Project files on the

criteria for selection of the six micro-regions for additional information).

F. Sustainability and Risks

1. Sustainability:

The Project is designed to sustain its benefits in several ways. Its demand driven nature should assure that TA and productive investments are chosen and designed by the beneficiaries. Project Components A and B would build the capacities of these communities to manage their own affairs, and they will directly contract for Project services and investments. Beneficiaries would provide counterpart funds for all productive investments financed from Component C. The reliance on GOE budget resources are minimal, and which would be mostly committed through alternative channels, like the *Fondo de Solidariedad.* All subprojects will be screened for environmental impacts, and mitigating measures taken if appropriate. If the subprojects are successful, the beneficiary groups will have an economic incentive to sustain them.

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		
Participation does not translate into equitable distribution among community groups.	M	Equity and gender oriented methodologies for community planning would be applied.
Service providers and communities do not apply sustainability criteria to subprojects.	H	Participatory subprojects feasibility analysis would be applied to ensure sustainability & a training program for service providers would be oriented to overcome this risk.
Service providers do not attract or retain trained personnel.	M	The Project would train personnel who would be directly involved in subproject support or execution and collaborate with network of NGOs & local universities to produce a larger pool of candidates.
Stakeholders' collaboration may not be maintained for the duration of the Project implementation period.	M	Several incentive mechanisms, participation of beneficiaries & transparency are built in the system.
Local governments' and inter-sectoral networks' interest in the Project would not be maintained throughout the implementation period.	S	Participation of the beneficiaries and communication strategy would encourage that the interest in the Project is maintained.
Field technicians impose their views on communities.	M	A training program in support of service providers would be oriented to overcome this risk.
Environmental projects cannot be justified as their benefits cannot be quantified.	M	Environmental benefit valuation procedures would be formalized in project operation rules.
Environmental benefits do not translate into income benefits of poor population	M	Mechanisms foreseen in the law regarding payment for environmental services would be supported.
Political interference in selection, hiring and evaluation of project personnel and in awarding contracts.	S	Clear selection procedures in project operations manual, and Bank supervision, to ensure that project personnel are hired based on technical criteria.

GOE is unable to mobilize sufficient co-financing from International Partners	M	GOE can request the Bank to increase its financing percentage to make up the difference, but the total project activities would be reduced.
From Components to Outputs		
Government administrative procedures interfere with timely disbursement of financial resources.	M	Bank supervisions would verify that disbursements to institutions involved and beneficiaries are timely and geographically targeted.
Lack of transparency on administration of financial resources.	M	Clear administrative guidelines are implemented and personnel is trained to comply with these guidelines.
Counterpart funding not available as projected.	M	Involvement of co-financing partners in project activities.
Overall Risk Rating	M	

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

3. Possible Controversial Aspects:

If Project management becomes politicized, certain communities may be favored over others, and there could be public complaints through the media. Elements of management may become corrupted into collecting bribes from service providers (contractors) or the latter may do the same with beneficiaries seeking access to project services, and this could damage the credibility of the Project. The Project has designed maximum transparency into administrative processes and includes an independent complaint resolution mechanism to discipline the system and resolve conflicts before they become more controversial. Communities receiving grants for productive projects may misuse the funds. The Project has strong auditing measures, but it also encourages public oversight by publishing in local newspapers a record of every grant, so that irregularities can be reported.

At the national level, the exclusion of some regions may raise some controversy. While this Project is a targeted intervention both in terms of regions and beneficiaries, there are other projects which cater to specific population groups. Also, the lesson learned from the last World Bank rural development project does not support national coverage.

At the local level, the possible controversial aspect of the Project is its gender targeting. This is justifiable by the fact that, although women are over-represented among the poor, economic discrimination and social norms often prevent them from actively participating in productive projects of this type. Also, the fact that 30% of women are targeted as beneficiaries is somewhat a reflection of the reality that at least the same percentage of household heads are women in rural Ecuador.

G. Main Loan Conditions

1. Effectiveness Conditions

- Appointment of Core Professional Staff for NCU;
- Issuance of the Operational Manual;
- Appointment of an independent consultant acceptable to the Bank, under terms of reference satisfactory to the Bank, to carry out a project impact evaluation baseline survey;
- Establishment of a satisfactory financial management system satisfactory to the Bank; and appointment of the independent auditors.

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

For procurement ,the PCU will not follow the national procedures contained in the laws and regulations governing public procurement and the consulting laws (See Annex 6).

Disbursement reporting. The beneficiaries will only have to report to PROLOCAL the planning, strengthening and subprojects expenditures through a simple statement of expenditures (Annex 6).

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):

- Operational Manual
- Financial Management System

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.

Norman Bentley Piccioni	John Redwood	Isabel Guerrero
Team Leader	**Sector Manager/Director**	**Country Manager/Director**

Annex 1: Project Design Summary

ECUADOR: Poverty Reduction and Local Rural Development (PROLOCAL)

Hierarchy of Objectives	Key Performance Indicators	Monitoring & Evaluation	Critical Assumptions
Sector-related CAS Goal: Protecting the poor and setting the basis for human development and poverty reduction, by supporting human capital development and broadening opportunities for "excluded" groups.	**Sector Indicators:** Reduce the percentage of target population below the poverty line by 5%. Reduce gender gap among target population.	**Sector/ country reports:** CAS Reports. Sector/Country Surveys & studies; Living Standard Measurement Surveys. Official Poverty Map.	**(from Goal to Bank Mission)** Political stability and social peace maintained. Stability in financial and economic conditions; and absence of social unrest.
Project Development Objective: To strengthen local empowerment, improve quality of local services, and increase access to productive assets to improve the well-being of poor households in selected micro-regions.	**Outcome / Impact Indicators:** 1. 60,000 households take active role in elaborating own local development plans. 2. 150 local governments collaborate with beneficiaries in generating development plans at the Parroquia & Cantón levels. 3. 80% of expected counterpart contributions made available by local organizations. 4. 30% of individuals participating in community development planning process are women. 5. 80% of beneficiaries are poor. 6. Beneficiary households improve access to productive assets. 7. Beneficiary households improve access to quality rural development services. 8. Income levels of beneficiaries of productive subprojects improves by 15%. 9. Underemployment among beneficiary households reduced by 20% .	**Project reports:** • Project reports (1, 2, 3, 4). • MIS (1,2,3, & 4). • Beneficiaries Assessments, (1, 4-8, & 9). Impact Studies (4-9).	**(from Objective to Goal)** • Improvement of macro-economic stability. • Conversion of empowerment into participatory development. • Continuity of commitments of governments at all level. • Availability of supporting infrastructure. • Continuity and presence of active & better trained labor force in the local regions. • Mitigation of or preparedness for natural disasters.

Hierarchy of Objectives	Key Performance Indicators	Monitoring & Evaluation	Critical Assumptions
Output from each Component:	**Output Indicators:**	**Project reports:**	**(from Outputs to Objective)**
1. Capacities of grass-root & second-and-third-tier organizations, and local governments in planning & implementing local development plans and subprojects developed.	1.1 70% of organized communities obtain legal status. 1.2 A total of $933,000 disbursed in support of local development planning and identification of subprojects. 1.3 A total of 750 development plans at local level, identifying at least 2,250 subprojects elaborated. 1.4 At least 80% of beneficiaries express satisfaction with participatory process.	• MIS. • Periodic reports on training. • Reports on technical assistance provided. • Periodic reports on development plans submitted & implemented. • Reports compiled by the PCU. Beneficiary Assessment.	• Participation will translate in to a balanced distribution among community groups. • Stakeholders collaboration maintained. • Local governments interest in the planning and building consensus in local development planning maintained. • Beneficiaries' expectations match the Project's activities. Agreement signed with Ministry of Social Welfare to facilitate legal status of community organizations.
2. Local training and information system established to improve the provision of local development services in each micro-region.	2.1 400 local experts trained in subproject preparation & implementation. 2.2 Six local inter-sectoral networks certify 120 Project technicians; 750 promoters; 1,440 male and 720 female leaders at the community level; and 120 administrators trained to work & provide in-service training for executing organizations. 2.3 720 local organization receive a total of $1.2M in financing for institutional strengthening. 2.4. 720 local organizations equipped.	• Periodic reports on training conducted at all levels. • Performance evaluations and qualification of trained personnel. • Reports of executing agencies. • Beneficiaries assessments workshop. MIS.	• Trained personnel maintained by institutions and/or organizations providing local development related services. • Field technician exhibit commitment in discharging their duties and follow beneficiaries' views. • Local governments and inter-sectoral networks establish and adopt methodology and maintain interest throughout implementation period.

3. Demand-driven co-financing (matching grant) mechanisms for productive & environmental investments and services established.	3.1 A total of $22 M disbursed as matching grants to implement 750 subprojects. 3.2 At least 70% of subprojects externally audited each year are rated satisfactory. 3.3 At least 80% of beneficiaries of subprojects express satisfaction with the process. 3.4 At least 25% of beneficiaries of subprojects are women.	• Documents and reports on application received and approved. • Implementation & progress reports. • Beneficiaries assessments. • Regional offices supervision reports. • MIS. Evaluation reports by independent audit firm.	• Administration of funds through transparent system. • Implementation of eligibility criteria, rules and methodology of operations. • Application for and availability of enough candidates for technical staff.
4. Project Coordination Unit established and operational.	4.1 PROLOCAL Board established. 4.2 Core PCU staff selected, trained and evaluated annually according to criteria defined in the Operation Manual. 4.3 Project MIS producing monthly & quarterly progress reports (financial, procurement, subprojects, and annual operation plans). 4.4 Communication strategy implemented, updated & evaluated annually.	• Presidential decree. • Project personnel selection & performance evaluations. • MIS. • Beneficiaries assessments. • External evaluations and audits.	• Absence of political interference in selection, hiring and evaluation of Project personnel and in award of contracts • Lessons learned from the Project are included in national policy formulation. Technicians needed for the regional offices are available in respective localities.

Hierarchy of Objectives	Key Performance Indicators	Monitoring & Evaluation	Critical Assumptions
Project Components / Sub-components:	**Inputs: (budget for each component)**	**Project reports:**	**(from Components to Outputs)**
A - Local Development Planning	US$ 2.98 million	Progress, disbursement audit and supervision reports.	Conducive government administrative procedures for timely disbursements of financial resources.
B - Local Development Services	US$ 7.43 million		Transparency in the administration of financial resources.
C - Subprojects	US$25.47 million		Availability of counterpart funding according to projections.
D - Project Coordination Unit.	US$5.83 million		

Addendum to Annex 1: Trigger indicators to expand to additional micro-regions

- Project Coordination Unit has been established and has adequate human and physical resources to comply with its functions and responsibilities;
- The Management Information System permits follow-up of Project implementation and assessment of achievement of Project objectives;
- 100 development plans at the community level, and 20 plans at the Parroquia level have been prepared through a participatory process;
- 80 subprojects at the community level, and 12 at the Parroquia level have been approved and are considered satisfactory by an external auditor;
- 80 local experts have been trained and provide services to the communities and subprojects. 300 local leaders and technicians have been trained and are fully committed to the Project activities;
- Social and environmental assessment of any additional micro-region have been conducted prior to their incorporation in PROLOCAL.

Annex 2: Detailed Project Description

ECUADOR: Poverty Reduction and Local Rural Development (PROLOCAL)

By Component:

Project Component 1 - US$2.98 million

Local Development Planning

The component will promote social capital formation by supporting planning for local development at the community, *Parroquia* and *Cantón* levels as part of a participatory development planning process. This activity would reinforce a recent law defining Parroquia responsibilities and requiring that each one prepare an annual local development plan. Rural communities would identify priority subprojects, a subset of which would be selected for streamlined preparation and execution. Community representatives would participate in a similar planning process at a higher, Parroquia level where similar community subprojects might be integrated in to Parroquia subprojects. By the same token, Cantones would prepare their development plans which could include linkages to those of Parroquias and their subprojects. The component will finance activities to allow at least 600 participating communities, 120 Parroquias and 30 Cantones to identify approximately 1,800 community subprojects, 360 parroquial subprojects and 90 cantonal subprojects.

PROLOCAL will contract with national NGOs or their networks to conduct an inventory/evaluation of local organizations and other social actors. Eligibility for participation in the Project would depend on: (i) evidence of existence for at least one year; (ii) field inspection to ratify their existence, socio-territorial nature and capacity to gather membership; and (iii) field inspection to ascertain that member families meet eligibility criteria as target population. At the same time a base-line survey would measure their social capital and execution capacities. A capacity-strengthening plan would also be prepared for each eligible organization/entity, parallel to coordination and planning activities.

Local Development Planning will be implemented through three sub-components: (i) Coordination (or Concertación) & partnership; (ii) Planning and project preparation; and (iii) Information sharing.

A.1 Coordination and partnership (CP). This sub-component will finance communications activities to fully familiarize the PROLOCAL target groups with the Project objective, strategy, opportunities, methodologies, criteria and procedures. Grass-roots organizations, local NGOs and local experts, families and juntas will be given the tools to coordinate planning at the community, parroquial and cantonal level and to create integrated projects linked at different levels. The sub-component will finance workshops at the parroquial and cantonal level and activities to prepare and disseminate methodological guidelines. Complementary communications activities financed under this sub-component include: (i) a promotion campaign for the Project; and (ii) an awareness campaign to address various forms of social inequities and human rights for men and women. Details of these activities are included in a communications strategy, a summary of which is provided in Annex 11. PROLOCAL would contract out the implementation of the strategy to a single specialist firm.

A.2 Planning and project preparation. The subcomponent will support local actors at the community, parroquial and cantonal level to prepare participatory, local development plans and subprojects. Analyzing local resources, systems, capacities, problems, solutions, opportunities, and development hypothesis, local actors will identify subproject profiles, rank them according to established priorities and prepare execution plans. Measures are included in the PROLOCAL Operational Manual to ensure that women's needs and priorities are taken into account and reflected in development plans and subproject profiles.

Under this subcomponent, PROLOCAL will sign agreements with communities to finance their preparation of local development plans. In most cases these communities and higher-level organizations will need to contract local or national consultant service providers to help them. Second-tier organizations and *juntas parroquiales* could consider community plans when making their own. These in turn could be consolidated by third-tier organizations and municipalities into cantonal or municipal plans. While this three-step process may not always occur in practice, the sub-component will try to promote it where conditions are conducive. In response to the local planning process, subprojects would be prepared, analyzed and eventually implemented at any of the three levels. PROLOCAL will provide local actors with guidelines for participatory, local development planning and the methodology to prepare subproject profiles. National and certified local consultants will have already been trained in these methodologies (Para 2.1 below) and will help their clients obtain financing for eligible subprojects from NGOs and Government programs (para. 3.2 below).

A.3 Information sharing. This subcomponent aims to systematically organize and disseminate relevant information in a timely manner at the local and national level about PROLOCAL activities, promote feed-back and discussion, and allow relevant organizations, development networks, technical staff, policy makers, researchers, students and the general public to take well-informed decisions. The subcomponent will finance workshops, reports, brochures, radio transmission, events, special studies (marketing, engineering designs, etc.), databases, maps, methodologies, progress reports, monitoring reports, audit reports, and supervision & evaluation reports, among others. This information will be shared with Project participants under the assumption that major Project risks can be mitigated by improved information flow and timely feedback from concerned stakeholders, while increasing local empowerment and ownership.

Project Component 2 - US$7.43 million

Local development Services

A critical first step in project implementation is to train the various local stakeholders of the Project, so that they can successfully play their roles. The component will use a tiered sequence of activities beginning with a "train the trainers" phase. The PCU would first contract competitively with nationally organized networks of NGOs with experience in training their own members. These groups would: (a) survey the existing technical skills in the target micro-regions and prepare capacity gap analysis; (b) prepare and implement training programs to address local gaps and pass on the Project methodologies to be followed during implementation; (c) promote the formation of local networks of the technicians trained, certifying their capabilities to participate in the next phase of project implementation. In phase two of the training these certified technicians would train the leadership and technicians of the organizations which would identify and implement subprojects. In a third phase, which is not necessarily sequential, these certified local consulting service providers would also provide technical assistance to local governments at the community, Parroquia and Cantón level to promote democratic participation and transparent management and administration.

Component B will be implemented through four sub-components: (i) strengthening of local consulting service providers; (ii) strengthening of human capital of grass-roots & second/third-tier organizations; (iii) strengthening of human capital of local governments and promotion of democratic processes; and (iv) establishment of an information system on prices, technologies and market opportunities (ECUALOCAL).

B. 1 Strengthening of local consulting service providers. The subcomponent aims to develop a cadre of local technical service providers, required by local implementing agencies of the Project. Field studies show that local technicians would most likely require training on: (i) natural resource management, conflict resolution, water management for irrigation and human consumption; (ii) finance and agro-business administration; (iii) local development planning; (iv) subproject analysis and management; and (v)

social/gender equity. In all about 120 planning and project preparation specialists, 60 project analysts, 120 accountants, 100 professionals in various fields (agriculture, irrigation, natural resources, marketing, agro-industry, nutrition, etc.) would be trained. In addition to the training of individuals, this subcomponent would seek to develop social capital by strengthening the social relationships and commercial linkages between local service providers by promoting local networks. These would serve as a combination of affinity group and professional association to develop a common view of local problems and their solutions. Individual activities could be coordinated and mutually supportive.

B. 2 Strengthening of human capital of grass-roots & second/third-tier organizations. This subcomponent aims at strengthening the management and technical capacity within existing local and second-tier organizations. The social assessment showed that the organizational tradition of these groups requires: (i) leaders able to mobilize social capital, to guide membership to concrete action proposals, and to negotiate with external parties; (ii) trained members with basic accounting, administration, procurement and secretarial skills; and (iii) promoters/facilitators able to guide reflection processes, to organize action initiatives and to facilitate liaison between organization leaders and external technicians/experts. When endowed with this minimum human capital, organizations will be more likely to develop longer term development processes that extend beyond the Project's life, to negotiate financial resources with a wider range of partners, and to mobilize new resources for their development. The Project will sign contracts (*convenios*) with implementing agencies which will employ certified local or national consulting service providers. These consultants would be selected by implementing agencies to provide in-service training to the latter's leaders, technical staff and promoters. About 120 local project managers, 750 local promoters (extensionists or facilitators), 1,200 leaders (men) and 650 leaders (women) would be trained. The sub-component will finance four clusters of activities: (i) basic equipment & training to those organizations that satisfactorily complete the institutional strengthening program; (ii) training of leaders, administrative support staff and facilitators on technical aspects requested by organizations; (iii) training of female leaders on local development issues, democratic processes, conflict resolution, and negotiation skills; and (iv) on-site assistance and training of accounting and administration for the organizations executing the subprojects.

B.3 Strengthening of human capital of local governments and promotion of democratic processes. Local governments can play a more important role in supporting development by more actively coordinating and participating in planning processes and promoting democratic initiatives. To properly undertake these activities, local governments need new leadership and trained technical teams. To finance this training, the Project will sign contracts which these local governments (community, Parroquia and Cantón) which will employ certified local or national consultants. About 750 local organizations, 120 *juntas parroquiales* and 30 *consejos cantonales* would receive this support. The training program would involve: (i) educating consejos cantonales and juntas parroquiales on development issues and public administration; (ii) provision of basic equipment & training as a reward to those local governments that satisfactorily completed the institutional strengthening program; and (iii) funding of expenses for carrying-out municipal and parroquial initiatives to debate and execute democratic processes such as environmental regulations, campaigns to promote civil rights, collective responsibilities, social organization and land-use planning or *ordenamiento territorial.*

B.4 Information system on prices, technologies and market opportunities, ECUALOCAL. This program is aimed at widening opportunities for local development and facilitating local development planning/subproject preparation processes, through access to useful and updated information. The system would be based on information needs of stakeholders, namely: social/local organizations, service providers and local governments. The system will collect, examine and diffuse information on prices, opportunities, technologies and territories involved. The system will use on the one hand popular media channels to provide previously digested information, and on the other hand modern and economic tele-centers to access

internet information. In essence, two sub-systems would be involved: (i) ECUAGRO, run by MAG and NGOs , which contains useful information on agricultural production and competitiveness (production alternatives, appropriate technologies, market opportunities, etc.); and (ii) INFOPLAN, run by ODEPLAN, which includes basic territorial information for decision-making of governments and local development institutions.

Project Component 3 - US$ 25.47 million

Subprojects

Focus group interviews, workshops and research by the social assessment have confirmed that communities in the target rural areas share a common view of their situation. They believe that a key element for their development is access to productive and marketing activities in their communities. They want to improve the quality and diversification of their production, and its access to larger markets through improved infrastructure and commercial links to urban centers.

The component will improve access to public good assets by establishing a demand-driven, matching-grant fund to finance: technical assistance, infrastructure, productive capacity of socio-territorial organizations, and environmental investments. Technical screening of identified subprojects would be undertaken by Project technical personnel at the regional level, according to criteria in the Operating Manual, technical reference tables and an output-input price database. Each subproject would be implemented on the basis of a contract between the Regional Office of PROLOCAL and the beneficiary group (BG). When BGs lack the necessary legal status, tripartite contracts will be signed including a third institutions, typically an NGO. BGs would be responsible for mobilizing counterpart funds from beneficiaries, administration of funds, contracting, supervision of subproject implementation. Project administration personnel at the regional level would monitor subproject expenditure accounts. The component would finance around 750 community subprojects, 150 parroquial subprojects, and 30 inter-parroquial subprojects.

Subproject eligibility criteria -- Subproject proposals would need to meet the following criteria in order to qualify for grant financing: (a) they would benefit the general public or community ; (b) they would generate direct or indirect employment or income to beneficiary groups; (c) they would be identified, prioritized, prepared, negotiated, implemented and maintained by the beneficiaries; (d) they would be co-financed by beneficiaries; (e) productive investments would be technically, economically, and environmentally sustainable; and (f) they would comply with the other conditions of the Operations Manual (OM). Beneficiary groups would not be eligible to receive financing for a second project until they had successfully completed the first one.

Types of Subprojects – the following types of subprojects would be financed under this component: (a) public infrastructure such as roads, health posts etc.; (b) productive community assets which create employment, diversify production, and increase income (including value added processing and marketing which benefit socio-territorial organizations and their membership); (c) environmental and natural resource management investments which preserve biodiversity, improve the environment, promote sustainable development of natural resources (including erosion control, soil restoration, protection of water sources, better use of agricultural chemicals, and pollution control); and (d) investments to strengthen social capital by building networks and links between local government and civil society to deepen the democratic process. (including TA to help communities improve democratic processes through improved citizen participation, local regulations and enforcement, strengthen human rights, improve local information systems and dissemination): and (e) training and technical assistance.

Levels of Execution - Subprojects will have varying levels of technical and administrative complexity. Local development plans will be prepared by three levels of political jurisdiction: community (smallest), parroquia, and cantón (largest) within the target micro-regions. These plans would identify and prioritize

subprojects to be implemented by the corresponding political jurisdictions.

Subproject financing criteria - The component would finance from a minimum of 60 percent up to a maximum of 100 percent of subproject costs, as per the cofinancing matrix below. In any case the amount would be limited to a maximum of US$800 per beneficiary family. Subprojects at the community level would have total financing limited to US$12,600, at the parroquial level to US$63,000, and at the cantonal level to US$252,000.

Investment Categories to be financed with Matching Grants.

Expense category	Description	Grant Contribution	Other Financing Sources
Works	*Community Infrastructure (CI)* - Plant/storage/office buildings, training centers, irrigation canals, animal production and aquaculture facilities, demonstration/trial greenhouse facilities, etc.	Up to 80%	-Beneficiary contributions (goods and/or labor). -Third party contributions. -Credit (when available and accessible) for financially feasible enterprises.
	Environmental Works (EW) - Waste recycling and/or treatment facilities, community forestry nurseries, terraces and other soil conservation works.	Up to 90%	-Beneficiary contributions (goods and/or labor) -Third party contributions.
	Social Works (SW) - Rehabilitation of roads and bridges outside protected and/or environmentally fragile areas.		
	Other Works (OW) related to *social positive externalities* such as commodity quality enhancing facilities (e.g. coffee, cocoa, rise) when financial benefits are not captured directly by producers.		
Durable Goods or Assets	*Investment Goods (IG)* - Machinery and equipment for associative enterprises, equipment for institutions and organizations, fences.	Up to 60%	-Beneficiary contributions. -Third party contributions. -Credit (when available and accessible) for financially feasible enterprises.
	Animals or Insemination Capsules (AI) for genetic improvements of community herds and/or livestock banks.		
	Plants and Seeds (PS), or vegetative material, for community reforestation and pasture improvements and watershed improvement/management/protection.	Up to 100%	-Beneficiary contributions. -Third party contributions.
Expendable Goods	*Training/operation Inputs (TI)* - Start-up (one-time) agricultural and non-agricultural inputs for demonstration/trial farms or activities, training/workshop materials.	Up to 80%	-Beneficiary contributions. -Third party contributions.

	Operation Inputs (OI) - Start-up (one-time) agricultural and non-agricultural inputs when local, regional or national credit sources are not accessible.	Up to 60%	-Beneficiary contributions. -Third party contributions. -Credit when available and accessible.
Services	*Technical Assistance (TA)* - Preinvestment, subproject promotion/awareness building, organization, legal counseling, technology transfer, start-up operations, training.	Up to 100%	-Beneficiary contributions. -Third party contributions.
	One-Time Services (OS) - Cattle insemination, deep plowing of degraded soils, land leveling, special studies/inventories/surveys, laboratory analyses, publicity/market/communication services, special training and education.		

Approval and Supervision of Subprojects - The Local Investment Fund will be administered in accordance with the directives contained in three documents: (i) Operations Manual (OM); (ii) methodology for evaluating the financial, economic, social and environmental benefits of subprojects; and (iii) standards for the design of projects.

Subprojects would be identified and prepared through local planning activities financed by Component A. The RCUs would review and confirm that subprojects are prepared in accordance with the Project's Operational Manual. Approvals by RCUs would be in writing and published in newspapers. To mitigate politicization of the selection process, the OM would prohibit discrimination in the selection of beneficiaries or service providers based on political affiliation, religion or race. There would also be a formal complaint process by which participants could use an ombudsman to present their case to the Managing Council of PROLOCAL. The OM would include the rules for operating the component process. Supervision of subproject implementation would first and foremost be the responsibility of the local BGs. Disbursements by the Project Management Units (NCU or RCU) would be made on a tranched basis, with each sponsor group providing evidence of the proper expenditure of the prior advance to justify the next one. The first disbursement would have to be covered by a performance guarantee from a third party. Regional Project staff would make sample field visits to verify that this documentation was correct. A technical consulting firm would be hired on a longer term contract to audit subproject results and impacts.

Project Component 4 - US$5.83 million

Project Coordination Unit

The component will finance costs for consultant services and equipment to carry out managerial, financial and technical coordination through a Project Coordination Unit (PCU). The PCU will be composed of a small National Coordination Unit (NCU) and up to six Regional Coordination Units (RCUs). The PCU will report to a board representing the public and private sectors. Core staff at the central level will include an Executive Director, a Technical Coordinator, an Administrative Coordinator with financial management functions, a Procurement Specialist, three technical specialist for the components, a specialist in M&E, a specialist in communications, a specialist in gender (shared with PROGENIAL project) and a system specialist. Staff at the regional level include a regional coordinator and three technical specialists. A detailed description on functions, responsibilities and associated procedures is to be found in the PIP and OM.

Planning Annual Implementation Plans (AIPs). AIPs would be prepared by the NCU and RCUs. The plans would reflect the activities, goals and objectives of each component and the planned outputs including

the financial and human resources needed to complete the plans. The AIPs will be the principal tool for coordination within each unit and between the NCU and RCUs. AIPs would have to be presented before the new budget year begins. These plans would first analyze how much of the previous plan was actually accomplished and recommend changes to overcome shortfalls, if justified. The annual implementation plans would be approved by the PROLOCAL Board.

Financial Management. The administrative unit in the NCU will administer and control financial flows. Each regional unit will be staffed with a financial and procurement specialist. Detailed financial operation procedures are provided in the OM, which defines the processes for budgeting, accounting, treasury, internal control and auditing for both the Regional and NCUs. Consultants will be hired to design and install a project management information system. The Project's Plan of Accounts would be broad and flexible enough to accommodate the needs of the Government's budget (SIGEF) and audit agencies, the Bank, and co-financiers.

LACI financial PMRs would be generated from this system and sent to the Bank quarterly. The NCU would carry out the annual budgeting coordination with the Ministry of Finance to assure timely release of counterpart funds. The NCU would operate the Project's Special Account and each RCU would have a Project account in a local bank. Disbursements for component C (Subprojects) would be made to a bank account for each subproject opened by the beneficiary group. Annual project financial reports would be audited by a private accounting firm and under terms of reference, both acceptable to the Bank, and presented within four months after the accounting period.

Procurement – Each RCU would have a specialist that would process its procurement and monitor local organizations and implementing agencies responsible for procurement on subprojects. Detailed procurement procedures are included in the OM for national, regional and local procurement. These procedures include how each type of procurement will be evaluated and selected with associated evaluation tables and methodology. Contract management arrangements for each type of contract are also defined.

Personnel – The PCU is expected to implement a rigorous system of personnel selection, evaluation and performance incentives. Selection of personnel will be carried out by external institutions (private firm, NGO or development institution) contracted for this purpose. The firms will interview, evaluate and nominate candidates for a short list to be confirmed by the PROLOCAL Board. Annual performance evaluations would be conducted by external firms based on benchmarks for each position included in the terms of reference.

Monitoring and Evaluation – In view of the nature of the Project's approach, and its importance for the country's rural development strategy, attention has been paid to design a rigorous monitoring and evaluation (M&E) system. The envisioned M&E system will consist of four subcomponents: (i) a monitoring system, which will track the Project's progress on a set of process indicators and feed into management's decision-making; (ii) a beneficiary assessment module, which will provide on an annual basis the target group's perceptions and reactions about Project progress; (iii) an impact evaluation baseline survey, which will quantify the impact which can be attributed to the Project; and (iv) auditing and supervision missions, which will review the technical and fiduciary aspects on a six-month basis, or more often if required.

Project Management Information System (MIS) – The PROLOCAL PCU would prepare, install and operate a project MIS. The system would consist of accounting; human resources; subprojects; procurement; risk management; planning; internal communication; and external communications.

Risk Management – Management at the national and regional levels would be responsible for defining and implementing the risk management mechanism for the Project. This would include the processes and tools for: (i) identifying and describing internal and external potential risk events; (ii) quantifying potential Project risks -- the probability and impact of the potential risk event; (iii) risk response preparation which defines potential risk mitigation measures; and, (iv) risk response control which focuses on monitoring potential risk, regularly updating the risk management plan -- archiving outdated risks and adding new ones and continuing the cycle from risk identification through risk mitigation. One staff member in each coordination unit would carry out risk management functions by working with each technical specialist and other teams members to update and present the risk management plan at the coordination unit's regular coordination meetings.

Communications – A specific communication strategy will support PROLOCAL implementation (see annex 11). A Bank communications audit has been carried out as part of the Project activities, and a communication strategy acceptable to the Bank has been prepared by a specialized consultant. The strategy supports a communication program to: (i) disseminate information about the Project's objectives, its implementation strategy and the eligibility criteria; (ii) establish a two-way channel to motivate stakeholders and ensure beneficiaries' ownership; and (iii) build a mechanisms for dialogue and exchange of information across the PROLOCAL micro-regions, which will play an important role in helping translate this diversity into policies in tune with local realities. Accordingly, the Project will show an important degree of flexibility in order to incorporate the peculiarities of each individual community. While most creative activities and graphic design and production will be contracted out, a senior communication specialist in the PCU will manage and supervise the process.

Annex 3: Estimated Project Costs

ECUADOR: Poverty Reduction and Local Rural Development (PROLOCAL)

Project Cost By Component	Local US $million	Foreign US $million	Total US $million
A. Local Development Planning	2.16	0.64	2.80
B. Local Development Services	4.87	2.10	6.97
C. Subprojects	20.39	3.68	24.07
D. Project Coordination Unit	4.43	0.68	5.11
Total Baseline Cost	31.85	7.10	38.95
Physical Contingencies	0.50	0.18	0.68
Price Contingencies	1.73	0.35	2.08
Total Project Costs	34.08	7.63	41.71
Front-end fee		0.25	0.25
Total Financing Required	34.08	7.88	41.96

Project Cost By Category	Local US $million	Foreign US $million	Total US $million
Goods	0.65	1.76	2.41
Consultants Services and Training	8.11	2.02	10.13
Subprojects	20.39	3.60	23.99
Operating Costs	3.91	0.00	3.91
PPF	1.02	0.25	1.27
Total Project Costs	34.08	7.63	41.71
Front-end fee		0.25	0.25
Total Financing Required	34.08	7.88	41.96

[1] Identifiable taxes and duties are 0 (US$m) and the total project cost, net of taxes, is 41.96 (US$m). Therefore, the project cost sharing ratio is 60.06% of total project cost net of taxes.

Annex 4: Cost Benefit Analysis Summary

ECUADOR: Poverty Reduction and Local Rural Development (PROLOCAL)

Methodology

Analytical work initially involved local development planning and feasibility analysis workshops in representative *cantones* of selected micro-regions. In planning workshops, potential subprojects were identified according to basic methodological guidelines considered in component C. In feasibility analysis workshops, area coverage, physical scale, investment costs, revenues or benefits and operational costs were estimated on a preliminary basis, with groups of potential beneficiaries, local technicians, and personnel of key local actors, such as technical colleges and credit and saving cooperatives. Prices and technical parameters provided in workshops were revised and validated based on qualified information sources. Without project "situations" of identified subprojects were revised and/or reconstructed with technicians and other qualified informants in the micro-regions involved. Finally, revised technical parameters and financial budgets of identified subprojects were incorporated in a Farmod model. Feasibility was analyzed at various levels: area unit (for crops and plantations); activity unit (herd for live-stock activities); production unit (farm, enterprise or firm, plant or processing unit); and subproject (when various farms, firms or plants are involved. For further details, see reports and models in the Project files.

Aggregated results were estimated based on: execution level, subproject category and micro-region. As stated in the Subprojects component, execution levels are: community, parroquia and inter-parroquia or cantón. Analyzed subproject categories include: productive subprojects; environmental/natural resource management subprojects; and social investment subprojects. In general, productive subprojects include: integration or network building subprojects; agriculture subprojects (which include agroforestry and aquaculture); natural resource and environment subprojects (which include forestry); and agribusiness and service supply subprojects. According to Project area and population, the selected micro-regions are: *Región Sur de Manabí, Zona Occidental de Los Ríos, Estribaciones Centrales de Los Andes, Región Oriental de Loja, Cuenca Alta del Río Jubones* and *Cuenca del Río El Angel.*

Results

Subproject Funds. On average, analyzed subprojects would require around: US$400 per family of community investments; US$120 per family of working capital; US$30 per family of private investments; and US$80 per family of technical assistance (pre-investment, promotion, organization and start-up technical assistance). On average, inter-parroquia or cantón subprojects would involve around: 400 families; US$160,000 community investments; US$48,000 working capital; US$12,000 private investments; and US$32,000 of technical assistance. Parroquia subprojects would involve around: 100 families; US$40,000 community investments; US$12,000 working capital; US$3,000 private investments; and US$8,000 of technical assistance. Lastly, assuming 5 beneficiary communities per Parroquia involved, community subprojects would involve around: 20 families; US$8,000 direct investments; US$2,400 working capital; US$600 private investments; and US$1,600 of technical assistance. Larger investments would take place in *Estribaciones Centrales de Los Andes*; followed by *Región Sur de Manabí* and *Cuenca del Río Jubones*.

Employment and incremental financial income. Family employment –indirectly remunerated through production gains– was significantly high in organic agriculture and artisanal sugar-cane processing subprojects. These subprojects were identified in *Estribaciones Centrales de Los Andes*. However, they are relevant in all micro-regions (especially organic agriculture). In terms of execution level, community subprojects generated around 2,100 person-years equivalent; parroquia subprojects, around 1,500 person-years equivalent; and inter-parroquia subprojects around 200 person-years equivalent. In terms of

subproject categories, agricultural/agroforestry subprojects generated 2,100 person-years equivalent; agribusiness/service subprojects, 1,500 person-years equivalent; and integration subprojects, around 200 person-years equivalent. According to micro-regions, subprojects in *Estribaciones Centrales de Los Andes* generated 3,300 person-year equivalent. In terms of incremental income per family, subprojects at different execution levels do not differ much (US$240-310/family). In terms of subproject categories, agribusiness/service subprojects generated US$650/family; and agriculture/agroforestry, around US$310/family. Among micro-regions, *Estribaciones Centrales de Los Andes* averaged US$480/family and *Cuenca del Río Jubones*, US$280/family. In contrast, *Región Oriental de Loja* averaged US$80/family.

Employment associated to Investments. In terms of investment-related family labor (major investment of target population), the most demanding subprojects include: pasture improvement, reforestation and agroforestry. Most demanding micro-regions are: *Cuenca del Río Jubones* and *Región Sur de Manabí.*

Subproject Feasibility. As shown in Tables 1 and 2, the most feasible subprojects were: organic agriculture and artisanal sugar-cane processing. In terms of execution level, community subprojects showed higher economic and financial Net Present Values. On average, community subprojects yield a financial NPV of US$1,400/family. In terms of micro-regions, higher feasibility indicators were found in *Estribaciones Centrales de Los Andes* and *Región Sur de Manabí.* On average, subprojects in such regions yield financial NPV of US$2,300/family and US$1,000/family, respectively. Finally, agribusiness/service-supply showed higher economic and a financial Net Present Values. On average, these subprojects yield a financial NPV of US$2,800/family. However, as shown below, they are fragile in terms of potential benefit reductions.

Aggregate Net Benefits. For projection purposes, aggregate economic benefits and costs were calculated for one, two, and three rounds of subprojects similar to the ones herewith described. The analyzed subprojects would generate around US$17 million of economic benefits in present value and reach around 20,000 families. However, subproject failures may significantly reduce these benefits. Considering total Project costs, one round of subprojects would generate US$1.9 million of discounted net benefits. Required local investment funds would be around US$17.8 million. Two rounds of subprojects would generate US$18.8 million of discounted net benefits. Required local investment funds would be around US$24.8 million. Three rounds of subprojects would generate US$35.7 million of discounted net benefits. Required local investment funds would be around US$37.2 million. Project economic and financial NPV and IRR could have been calculated with available information. However, considering the lack of certainty of overall Project performance, as it is largely determined by beneficiaries during implementation, they were not included as feasibility reference indicators.

Summary of Benefits and Costs:

Costs. Total Project costs were included for the economic feasibility analysis. Investment and recurrent costs of potential subprojects were obtained from the economic and financial analysis in the Project's files. Base costs (with physical contingencies) relative to planning and management for local development, as well as strengthening of local service providers and rural financial systems, were extracted from Cost Summary Tables in the Project's files.

Benefits. Benefits generated by local investment subprojects include: revenues from increased production and value added; increased natural assets such as commercial and conservation forests; and improved health reflected in the reduction of treatment costs. Non-quantified benefits include inter alia: increased water supply and soil conservation due to proper watershed management; greater social cohesion or social capital; increased local development capacities or human capital; and expanded rural financial markets. Non-quantified negative externalities may also be generated, such as social conflicts associated with

community priority setting, community subproject selection and subproject failures. Financial revenues generated by local investment subprojects include inter alia: revenues from increased production and value added; revenues from the potential sale of forest products; reduced family spending as a result of a reduction in medical treatment costs.

Main Assumptions:

- Future economic financial benefits and cost flows were discounted based on a 12% annual rate. The projected analysis period was 20 years.
- Shadow prices for family labor were calculated for one micro-region on the coast and one in the highlands. The average shadow price for family labor would be 70% of financial or market price. Price distortions for other goods and services were not significant.
- Family labor use within family labor availability was not included as an operation cost. Family labor use in excess of family labor availability was valued at financial or market prices. Financial deficits for operation were covered with short-term credit. Their average real interest rate was estimated at 20% per annum. Medium-term credit was considered for capital investments of individual families (such as cattle) based on: a 5-year repayment period; and a 20% annual real interest rate.
- Fiscal revenues would essentially be the increased value-added tax generated as a result of increased investment and operation costs induced by the Project. Value-added tax was estimated at 10% of value without changes during the evaluation period. Total Project costs excluding credit funds would be the fiscal cost for the Government.

Sensitivity analysis / Switching values of critical items:

Subproject Sensitivity. Considering the relatively high risk of failure on subprojects generated by demand-driven investment projects, switching values of benefit reductions were calculated for analyzed subprojects. As shown in Tables 1 and 2, environmental and social subprojects are very robust in terms of economic and financial feasibility, since estimated benefits could eventually be reduced by 40-90%. In case of forestation subprojects, this is essentially due to the long period elapsed between plantation (investment) and full forest growth (cumulative benefits -including carbon captured- in the form of wood). On the negative side, environmental and social subprojects do not generate incremental family income or employment, and thus contribute marginally to poverty reduction.

Certain agricultural and agroindustrial subprojects are very robust in financial terms and moderately robust in economic terms, namely: organic agriculture and artisanal sugar-cane processing. This is essentially due to the high contribution of recurrent family labor. Estimated economic benefits can be reduced around 30% and still be feasible. In general a 30% margin is acceptable, however, in organic agriculture subprojects -which are essentially technical assistance subprojects- it implies a challenging (but feasible) 70% adoption rate. There is also a service supply subproject which is moderately robust -benefits could also be reduced by 30%- namely associative input supply and technical assistance. As in the case of organic agriculture, this is essentially due to the production cost-saving nature of the subproject, and the relatively small administrative structure. In this case, a 30% margin implies a reasonable 70% participation rate -in the analyzed case, there is a target population of 240 small producers.

Besides the above-mentioned cases, most analyzed processing/service-supply subprojects appear fragile. They would have feasibility problems if estimated benefits were reduced by 2-20%. In contrast, feasible agricultural subprojects seem to be moderately robust –estimated benefits could be reduced by 30-50%.

Overall Sensitivity and Risk Mitigation Measures. Considering aggregate benefits of analyzed subprojects, the Project switching value would be 12% benefit reduction value in terms of economic

feasibility, and 21% benefit reduction in terms of financial feasibility. These reduced margins of benefit reductions translate into reduced margins of acceptable subproject failures. Thus the Project should be designed so as to minimize subproject failure risks. Participatory planning and participatory subproject preparation (already incorporated in the Project design) significantly contribute to ensuring social sustainability of future subprojects. However, other complementary mechanisms are necessary. Appropriate technical support during subproject preparation, especially in complex subprojects, would allow for on-site beneficiary training as well as better subproject screening and design, thereby increasing subprojects' technical sustainability. Finally, subproject co-financing arrangements would allow for healthy project/beneficiary risk sharing, especially in subproject categories which appear to be more fragile.

Table 1. Financial Feasibility of Potential Subprojects (US$ of May 2000)

Category	Type	Analyzed Subprojects	NPV	IRR (%)	Switching value (%)
Productive	Those intended to integrate production, processing and/or marketing	*Río Jubones* – Cattle Improvement, Milk Processing	839,887	28	12
		Río Jubones – Onions, Production and Marketing	47,979	55	13
		Loja – Peanuts, Production and Marketing	45,533	93	13
		Los Ríos – Rice Production, Processing and Marketing	1,070,282	162	6
		Manabí – Improved Coffee Production and Processing	2,202,390	45	40
		Estribaciones – Coffee Post harvest and Marketing	498,464	112	11
		Río El Angel – Value Added for Agricultural Products	82,350	83	28
		Río El Angel – Textiles Production and Marketing	24,010	37	19
	Agriculture - Aquaculture	*Río Jubones* – Cattle Improvement	(189,457)	7	(10)
		Río Jubones – Trout production	29,845	25	19
		Manabí – Corn Seed Multiplication	196,808	46	52
		Manabí – Agroforestry	1,858,537	62	54
		Estribaciones – Organic Corn Production	4,878,001	>200	93
		Estribaciones – Baby Banana Production	436,924	93	28
		Río El Angel – Greenhouse Horticulture	914,990	75	45
		Río El Angel – Irrigation Infrastructure	(112,597)	9	(10)
		Río El Angel – Cattle Improvements	158,240	17	15
	Agroindustry - Services	*Loja* – Balanced Foodstuff based on Corn	88,085	64	7
		Los Ríos – Rural Tourism	27,659	20	2
		Los Ríos – Inputs Supply and Technical Assistance	204,450	56	28
		Estribaciones – Corn Processing and Marketing	611,604	119	8
		Estribaciones – Citrics Processing	1,327,131	23	17
		Estribaciones – Artisanal Sugar-cane Processing	4,708,648	>200	81
Environment	Natural Resources	*Río Jubones* – Reforestation, Watershed Management	1,241,650	35	93
		Manabí – Caña Guadúa for Riverlands Protection	629,303	41	86
		Manabí – Reforestation, Watershed Management	2,334,964	36	91
		Estribaciones – Reforestation in Coffee Areas	48,736	17	45
		Estribaciones – Reforestation in Sugar-cane Areas	19,779	17	50
		Río El Angel – Reforestation of Degraded Lands	1,004,864	33	91
Social	Infrastructure	*Río El Angel* – Potable Water Supply	59,988	31	50

Switching values represent percentage reductions of annual benefits which generate a NPV close to zero.

Table 2. Economic Feasibility of Potential Subprojects (US$ of May 2000)

Category	Type	Analyzed Subprojects	NPV	IRR (%)	Switching value (%)
Productive	Those intended to integrate production, processing and/or marketing	*Río Jubones* – Cattle Improvement, Milk Processing	725,136	26	11
		Río Jubones – Onions, Production and Marketing	22,567	30	6
		Loja – Peanuts, Production and Marketing	18,023	48	5
		Los Ríos – Rice Production, Processing and Marketing	1,033,063	157	6
		Manabí – Improved Coffee Production and Processing	2,202,390	45	40
		Estribaciones – Coffee Post harvest and Marketing	381,952	90	9
		Río El Angel – Value Added for Agricultural Products	16,021	29	6
		Río El Angel – Textiles Production and Marketing	6,533	19	5
	Agriculture - Aquaculture	*Río Jubones* – Cattle Improvement	(351,201)	2	(17)
		Río Jubones – Trout production	(8,120)	8	(5)
		Manabí – Corn Seed Multiplication	139,185	38	37
		Manabí – Agroforestry	1,508,660	>200	38
		Estribaciones – Organic Corn Production	1,512,225	>200	29
		Estribaciones – Baby Banana Production	384,283	109	25
		Río El Angel – Greenhouse Horticulture	857,235	71	42
		Río El Angel – Irrigation Infrastructure	(258,237)	5	(25)
		Río El Angel – Cattle Improvements	(74,881)	9	(8)
	Agroindustry - Services	*Loja* – Balanced Foodstuff based on Corn	41,965	38	3
		Los Ríos – Rural Tourism	15,740	17	2
		Los Ríos – Inputs Supply and Technical Assistance	204,450	56	28
		Estribaciones – Corn Processing and Marketing	592,186	116	7
		Estribaciones – Citrics Processing	1,314,185	23	17
		Estribaciones – Artisanal Sugar-cane Processing	1,650,193	200	28
Environment	Natural Resources	*Río Jubones* – Reforestation, Watershed Management	1,239,141	35	93
		Manabí – *Caña Guadúa* for Riverlands Protection	530,092	38	88
		Manabí – Reforestation, Watershed Management	2,296,501	34	92
		Estribaciones – Reforestation in Coffee Areas	48,736	17	45
		Estribaciones – Reforestation in Sugar-cane Areas	18,089	17	40
		Río El Angel – Reforestation of Degraded Lands	966,403	30	88
Social	Infrastructure	*Río El Angel* – Potable Water Supply	58,370	30	47

Switching values represent percentage reductions of annual benefits which generate a NPV close to zero.

Conversion factor from financial to economic price of family labor was estimated at 70%.

Annex 5: Financial Summary

ECUADOR: Poverty Reduction and Local Rural Development (PROLOCAL)

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	2.3	7.0	13.2	10.7	4.6	0.0	0.0
Recurrent Costs	0.2	0.9	0.9	0.9	0.9	0.0	0.0
Total Project Costs	2.5	7.9	14.1	11.6	5.5	0.0	0.0
Front-end fee	0.3	0.0	0.0	0.0	0.0	0.0	0.0
Total Financing	2.7	7.9	14.1	11.6	5.5	0.0	0.0
Financing							
IBRD/IDA	2.4	5.4	8.1	6.4	2.9	0.0	0.0
Government	0.2	0.5	1.7	0.7	0.4	0.0	0.0
Central	0.0	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	0.1	1.4	2.4	2.9	1.5	0.0	0.0
User Fees/Beneficiaries	0.0	0.6	1.9	1.6	0.7	0.0	0.0
Others	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total Project Financing	2.7	7.9	14.1	11.6	5.5	0.0	0.0

Main assumptions:

Annex 6: Procurement and Disbursement Arrangements
ECUADOR: Poverty Reduction and Local Rural Development (PROLOCAL)

Procurement

Procurement will be carried out in accordance with World Bank "*Guidelines: Procurement Under IBRD Loans and IDA Credits*", published in January 1995 (revised January/August 1996, September 1997 and January 1999); and "*Guidelines: Selection and Employment of Consultants by World Bank Borrowers*" published in January 1997 (revised in September 1999 and January 1999), and the provisions stipulated in the Credit Agreement.

Assessment of the agency's capacity to implement procurement

An assessment of the implementing agency's procurement capacity was carried out by an authorized Procurement Specialist and cleared by the RPA in February 2001. Procurement risk was assessed as "AVERAGE". The following action plan, based on the assessment, was agreed upon with the implementing agency to address the shortcomings identified. All actions listed below would be implemented before effectiveness.

- Retain a qualified consultant with a minimum of 5 years experience in Bank-financed procurement to work on a full-time basis in the PCU and serve as procurement officer for the Project.
- Retain a qualified procurement assistant to support the procurement officer.
- Organize a training program on applicable Bank procurement policies and procedures for the Regional Coordination Units and the grant beneficiaries. A detailed training plan, methodology and materials acceptable to the Bank would be prepared before effectiveness. However, the training plan would be implemented after effectiveness.
- Adopt standard NCB and shopping documents to be agreed by the Bank.

Procurement Planning.

A procurement plan has been submitted and approved by the Bank. The plan will be updated quarterly throughout the life of the Project and submitted annually for Bank review and approval. Quarterly updates will be reviewed during supervision missions.

Procurement methods.

The methods to be used for the procurement described below, and the estimated amounts for each method, are summarized in Table A.

Procurement of Goods

The Project would finance contracts for the purchase of vehicles, computer and office equipment estimated to cost a total amount of approximately US$2.41 million for the operation of the PCU, and strengthening of social organizations and local financing intermediaries. Contracts for goods estimated to cost more than US$250,000 equivalent would be awarded on the basis of ICB procedures. Contracts estimated to cost less than US$ 250,000 up to an aggregate amount of US$0.4 million may be procured on the basis of NCB procedures acceptable to the Bank. Prior review of the first two NCB contracts shall serve as the basis for agreement on a standard model to be used in subsequent contracts. Contracts for goods estimated to cost less than US$50,000 per contract for miscellaneous equipment that includes replacement of vehicles, computers, and office equipment, up to an aggregate amount of US$1.58 million may be procured following shopping procedures in accordance with paragraphs 3.5 and 3.6 of the Guidelines.

Consulting Services and Training

The Project would finance consulting services to: (i) prepare diagnoses of local financial institutions; (ii) carry out pre-investment studies, prepare and implement subprojects; (iii) provide technical assistance to beneficiaries in participatory planning and Project identification and implementation; and (v) monitor and evaluate the Project.

Training would consist of: (i) workshops for project formulation and implementation; and (ii) courses for technical staff, promoters and leaders. The Project would finance trainers' fees, rental of training facilities, per diem of trainees, and training materials. Training would include workshops on procurement for Regional Coordination Units and beneficiaries.

Firms

Contracts for firms would be awarded following the Quality and Cost Based Selection (QCBS) process, in accordance with Section II of the Consultant Guidelines; Selection under a Fixed Budget for simple and precisely defined assignments; Least-Cost Selection for audits; and Selection Based on Consultants' Qualifications for very small assignments for which the need for preparing and evaluating competitive proposals is not justified; in accordance with Section III of the Consultant Guidelines. The total amount of these contracts is estimated to be approximately US$6.35 million.

Individuals

Individual consultants would be retained for specialized advisory services, services for project administration and monitoring, and direct technical assistance to beneficiaries, up to an aggregate amount of approximately US$2.18 million. The recruitment of these individuals would be based on competitive selection processes described in the Implementation Manual, considering the total amount of the contracts for the overall duration of the assignments.

Subprojects:

The Project would finance grants for subprojects proposed by eligible organized communities, civil society, NGOs, and local government. These subprojects are demand-driven and cannot be defined *a priori*. The Operational Manual describes in detail eligibility and selection criteria, the process for identifying, developing and approving subprojects, and applicable procurement procedures. The maximum cost of a subproject will depend on the type of subproject, i.e. US$12,600 for community subprojects, US$63,000 for parroquial subprojects and US$252,000 for subprojects at the cantón level. A subproject could consist of goods, works or services, or a combination of the three. Most goods financed by the subprojects would be procured following shopping procedures. However, contracts above the threshold specified in table B, if any, would be procured following NCB procedures either by or under the direct supervision of the PCU, depending on the beneficiary's capacity. It is anticipated that only small works will be financed under the subprojects following the price comparison procedures described above. Procedures to be used by local government, NGO's s and/or the direct community beneficiaries would incorporate community-based concepts, where appropriate and as with the Bank and included in the Implementation Manual.

Operating Costs:

The Project will finance operating costs which include equipment and vehicle maintenance, office supplies, basic services, travel and per diem for PCU staff, and incremental salaries of project implementation unit.

Procurement methods (Table A)

Table A: Project Costs by Procurement Arrangements
(US$ million equivalent)

Expenditure Category	Procurement Method[1] ICB	NCB	Other[2]	N.B.F.	Total Cost
1. Goods	0.38 (0.34)	0.44 (0.39)	1.58 (1.39)	0.00 (0.00)	2.41 (2.12)
2. Consulting Services and Training	0.00 (0.00)	0.00 (0.00)	10.13 (7.73)	0.00 (0.00)	10.13 (7.73)
3. Subprojects	0.00 (0.00)	2.40 (1.20)	21.59 (10.79)	0.00 (0.00)	23.99 (11.99)
4. PPF	0.00 (0.00)	0.00 (0.00)	1.27 (1.11)	0.00 (0.00)	1.27 (1.11)
5. Operating Costs	0.00 (0.00)	0.00 (0.00)	3.91 (1.99)	0.00 (0.00)	3.91 (1.99)
6. Front-end fee	0.00 (0.00)	0.00 (0.00)	0.25 (0.25)	0.00 (0.00)	0.25 (0.25)
Total	0.38 (0.34)	2.75 (1.44)	38.83 (23.42)	0.00 (0.00)	41.96 (25.20)

[1] Figures in parenthesis are the amounts to be financed by the Bank Loan. All costs include contingencies.

[2] Includes goods to be procured through national shopping, consulting services, training, technical assistance services, and incremental operating costs related to staff managing the Project, and travel and perdiem for this staff, operation and maintenance of equipment and vehicles, office supplies, and basic services.

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	5.96 (4.55)	0.00 (0.00)	0.00 (0.00)	0.09 (0.07)	0.30 (0.23)	0.00 (0.00)	0.00 (0.00)	6.35 (4.85)
B. Individuals	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)	0.00 (0.00)	2.18 (1.66)	0.00 (0.00)	2.18 (1.66)
Total	5.96 (4.55)	0.00 (0.00)	0.00 (0.00)	0.09 (0.07)	0.30 (0.23)	2.18 (1.66)	0.00 (0.00)	8.53 (6.51)

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 (per Section V of Consultants Guidelines), Commercial Practices, etc.

N.B.F. = Not Bank-financed
Figures in parenthesis are the amounts to be financed by the Bank Loan.

Prior review thresholds (Table B)

The proposed thresholds for prior review are based on the procurement capacity assessment and are summarized in Table B. Any contract awarded on a single-source basis, assignments of a critical nature, and amendments raising contract values above the said thresholds would also be subject to prior review. In addition, the plan and budget for Operating Costs under the Project will be reviewed and approved by the Bank annually.

Table B: Thresholds for Procurement Methods and Prior Review [1]

Expenditure Category	Contract Value Threshold (US$ thousands)	Procurement Method	Contracts Subject to Prior Review (US$ millions)
1. Goods	>250	ICB	All
	50-250	NCB	First 2 contracts
	<50	Shopping	First 2 contracts
3. Services			
Consulting Firms	>100	Independent of method	All
	<100	Independent of method	TOR & Shortlist
Individual Consultants	>50	Chapter V	All
	<50	Chapter V	TOR only
4. Subprojects	>50	As described in the Operational Manual[2]	First 2 contracts
	<50		First 2 contracts
5. Training	N/A	N/A	N/A
6. Miscellaneous	N/A	N/A	N/A

[1] Thresholds generally differ by country and project. Consult OD 11.04 "Review of Procurement Documentation" and contact the Regional Procurement Adviser for guidance

[2] Goods financed by the subprojects estimated to cost less than US$50,000 equivalent per package would be procured following shopping procedures. Contract packages estimated to cost more than US$50,000, if any, would be procured following NCB procedures.

Overall Procurement Risk Assessment
"AVERAGE"

Frequency of procurement supervision missions proposed: One every 6 months (includes special procurement supervision for post-review/audits).

Disbursement

Allocation of loan proceeds (Table C)

Table C: Allocation of Loan Proceeds

Expenditure Category	Amount in US$million	Financing Percentage
Goods	1.8	100% FE/ 80% LE
Consultant Services and Training	7.5	100%
Sub Projects	11.85	100% of Government share
Operating costs	1.69	80% until December 31, 2003; 45% until December 31, 2005; 3 thereafter
Front-end fee	0.25	
PPF	1.11	
Unallocated	1.0	
Total	25.20	

Financial Management Responsibility

The PCU will be responsible for the implementation and maintenance of a financial management system, in order to efficiently manage the Project's funds and prepare the Project Management Reports (PMR) in a timely manner. The financial management system will include policies, norms and procedures for Planning, Budget, Procurement, Accounting, Reporting, and Auditing to ensure the provision of accurate and timely information to the Word Bank regarding project funds resources and expenditures, as required by OP/10.02. The system will provide information on physical performance, according to the Project's outputs and indicators included in Annex 1.

Disbursement Procedures

Until a PMR-compliant financial management system is in place, the PCU will follow traditional disbursement procedures for the withdrawal of funds under the loan agreement, in accordance with the guidelines setforth in the Disbursement Procedures Handbook. The Bank and the Borrower have agreed that if by Project effectiveness the PCU has not fully implemented a financial management system to produce the PMR required by the Bank, the traditional disbursements procedures will apply for the first two quarters of Project implementation. SOE documentation will be maintained by the PCU for post-review and audit purposes. Special Account replenishment requests should be sent to the Bank on a monthly basis. Once the accounting and financial management system is deemed to be able to produce timely project management reports, and is certified as such by the Bank, migration to a PMR-based disbursements may be implemented.

Use of statements of expenditures (SOEs):

Except for contracts requiring prior review, disbursements would me made against certified statements of expenditure (SOEs), that is: (i) contracts for goods and works below US$250,000; (ii) contracts with consulting firms below US$100,000; (iii) contracts with individual consultants below US$50,000; (iv) training activities and operation costs; and (v) subprojects. SOE documentation will be maintained by RCUs for post-review and audit purposes for one year after the end of the year in which the last disbursement takes place.

Use of Project Management Reports (PMRs)
The PMRs will serve as support for disbursement requests. Transition to PMRs will be subject to the satisfactory results of new financial management and procurement assessments. Once the PCU becomes PMR-compliant, disbursements would be in accordance with guidelines set in the Loan Administration Change Initiative (LACI) Implementation Handbook. Each application for withdrawal should separately identify the funds requested from the loan account, and would be supported by a PMR or such other documents and evidence as the Bank may request. PMRs should be submitted within 45 days from the preceding quarter. Upon receipt of each application for withdrawal, the Bank, on behalf of the Borrower, shall withdraw from the credit account and deposit into the Special Account an amount equal to the lesser: (a) the amount requested; and (b) the amount the Bank has determined, based on the PMR accompanying the application, is required to be deposited in order to finance eligible expenditures during the six month period following the date of the report, but in no case should the advance to the Special Account exceed 20% of the total loan funds without prior authorization from the Loan Department.

Special account:

The PCU will set up a Special Account (SA) in the Central Bank of Ecuador on terms and conditions satisfactory to the World Bank. In addition to the SA, a Central PROLOCAL Account (CPA) will be opened at a private bank as well as regional project accounts at provincial branch offices of the same bank.

PROLOCAL will request advances from the SA to the CPA to make payments directly to consultants and suppliers contracted under components A and B of the Project. These requests will be accompanied by a list of checks to be issued. The request for the advance will be reviewed by the Executive Director before the transfer can be authorized. Advances from the special account should be documented within 30 days of transfer to the CPA.

For consulting services and civil works contracted by regional offices under components B and C, payments will be made directly to consultants and contractors by the private bank based on "ordenes de pagos" prepared by the regional accountant and approved by the coordinator of the regional office. Advances to regional accounts will be made from the counterpart funds. Upon documentation of expenditure by the RCU, the PCU will reimburse the counterpart fund account for eligible expenditures from the Special Account. The advances to the regional bank accounts will be made based on "solicitudes de fondos" prepared by the regional accountant and approved by the PCU Administrative Coordinator. Details of this flow of funds together with guidelines for each step are included in the Project Operation Manual.

Flow of Funds:
Payments from the Loan proceeds would be administered by the PCU from a Special Account. The Special Account would be maintained in US dollars in a financial institution acceptable to the Bank. Under traditional disbursement procedures, the maximum authorized allocation, sufficient for financing 4 months of eligible expenditures, would be US$2.0 million. Under PMR-based disbursement, the maximum amount that can be on deposit is US$4.0 million.

Auditing Arrangements:
An external auditor, acceptable to the Bank, will be contracted by the PCU to carry out the annual review of the Project financial reports. The auditor will be selected according with the Bank's Guidelines for the Selection and Employment of consultants by the World Bank Borrowers dated January 1997, revised in September 1997, so that the audit can be performed throughout each year of project implementation.

The Project financial statements, Special Account Statement, SOEs (if applicable) and the PMRs will be reviewed and audit report will be submitted to the IBRD within 4 months of the close of the year ending

December 31. The Guidelines and Terms of Reference for Audits of Projects with Financing by the World Bank in the Latin American and Caribbean Region should be followed when preparing the terms of reference for the audit and these guidelines should be provided to the selected auditors.

Apart from financial auditing, the Project will also carry out a technical audit of the subprojects, training and technical assistance which will assess the technical quality of the subprojects, training and technical assistance, the accounting arrangements and justification of expenditures, and issues related to economic, financial and social sustainability.

Retroactive Financing:
There will be no retroactive financing.

Justification by Beneficiaries of Subproject Expenditures:
Beneficiaries will only have to report the subproject expenditures through a simple statement of expenditure (excluding the normal requirement for other financial reports). The RCU will keep the proofs of payment, invoices and other expenditure justification for audit purposes up to two years after the expenses have been incurred. PROLOCAL will review the reports of the beneficiaries and the auditors will on a sample basis analyze the expenditures of the beneficiaries and verify whether they have been done in compliance with the subproject agreement and the administrative and financial requirements established in those agreements.

Annex 7: Project Processing Schedule

ECUADOR: Poverty Reduction and Local Rural Development (PROLOCAL)

Project Schedule	Planned	Actual
Time taken to prepare the project (months)	19	19
First Bank mission (identification)	08/04/99	08/03/99
Appraisal mission departure	02/14/2001	02/14/2001
Negotiations	04/19/2001	05/07/2001
Planned Date of Effectiveness	09/21/2001	09/21/2001

Prepared by:

Government of Ecuador, Ministry of Social Welfare

Preparation assistance:

TF025961

Bank staff who worked on the project included:

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Annex 8: Documents in the Project File*
ECUADOR: Poverty Reduction and Local Rural Development (PROLOCAL)

A. Project Implementation Plan

- Operational Manual, April 2001. *
- Project Implementation Plan, April 2001. *

B. Bank Staff Assessments

- Project Target Group, Micro-regions, Institutions and Subprojects. July 2000. *
- Component C: Prototype Projects Analysis and Projections. July 2000. *
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- Project Financial and Economic Analysis. March 2001.*
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3 Targeting
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4 Social Aspects and Assessments
- Jordan F. et al. May 2000. *Evaluación Social: Propuesta de Evaluación de la Realidad Social de Territorios Microregionales para el PROLOCAL.**
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5 Environmental Aspects
- CEPLAES. February 2001. *Environmental Baseline Study.*

6 Institutional Aspects
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- Armas, G. October 2000. *Diagnostico Institucional en el Universo PROLOCAL.**
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*Including electronic files

Annex 9: Statement of Loans and Credits

ECUADOR: Poverty Reduction and Local Rural Development (PROLOCAL)

May-2001

Project ID	FY	Purpose	Original Amount in US$ Millions IBRD	IDA	Cancel.	Undisb.	Difference between expected and actual disbursements* Orig	Frm Rev'd
P049924	2001	Rural Water Supply & Sanitation	32.00	0.00	0.00	32.00	0.00	0.00
P064045	2000	Fin Sectr TA Ln	10.00	0.00	0.00	9.30	1.97	0.00
P070337	2000	EC-SAL	151.52	0.00	0.00	151.52	101.52	0.00
P040106	1998	INTL TRDE/INTEGRATIO	21.00	0.00	0.00	11.30	3.97	0.00
P040086	1998	INDIGENOUS PEOPLES	25.00	0.00	0.00	8.86	2.93	0.00
P039084	1998	EC- HEALTH SERVICES MODERNIZATION PROJ.	45.00	0.00	0.00	39.48	14.92	0.00
P007135	1998	AGRIC CENSUS & INFO	20.00	0.00	0.00	4.84	-2.06	0.00
P036056	1997	EC JUDICIAL REFORM	10.70	0.00	0.00	3.32	1.80	0.00
P007131	1997	AG RESEARCH	21.00	0.00	0.00	15.04	3.37	2.28
P007128	1996	ENV MANAGEMENT PROJ	15.00	0.00	4.99	2.29	7.28	4.29
P007105	1994	IRRIG TA	20.00	0.00	0.00	2.07	2.07	1.07
P007087	1993	EC- SOCIAL DEV. II: HEALTH & NUTRITION	70.00	0.00	0.00	16.34	-3.86	0.00
		Total:	441.22	0.00	4.99	296.36	133.90	7.64

ECUADOR
STATEMENT OF IFC's
Held and Disbursed Portfolio
May-2001
In Millions US Dollars

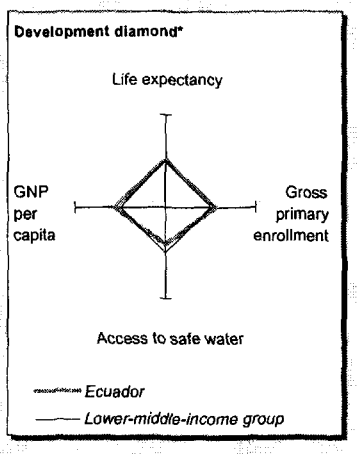
		Committed				Disbursed			
		IFC				IFC			
FY Approval	Company	Loan	Equity	Quasi	Partic	Loan	Equity	Quasi	Partic
1997	Agrocapital	3.50	0.00	0.00	0.00	3.50	0.00	0.00	0.00
1969/73/77/81/82/87	COFIEC	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
1998	Concessionaria	11.50	1.30	0.00	15.00	2.93	0.33	0.00	3.82
1999	FV Ecuacobre	9.00	0.00	0.00	0.00	9.00	0.00	0.00	0.00
1998	Favorita Fruit	10.00	5.00	0.00	0.00	10.00	5.00	0.00	0.00
1999	La Universal	8.20	5.00	0.00	0.00	8.20	5.00	0.00	0.00
1993	REYBANPAC	4.65	0.00	0.00	0.00	4.65	0.00	0.00	0.00
	Total Portfolio:	46.85	11.30	0.00	15.00	38.28	10.33	0.00	3.82

		Approvals Pending Commitment			
FY Approval	Company	Loan	Equity	Quasi	Partic
2000	ERSA	8.00	4.00	0.00	0.00
	Total Pending Commitment:	8.00	4.00	0.00	0.00

Annex 10: Country at a Glance

ECUADOR: Poverty Reduction and Local Rural Development (PROLOCAL)

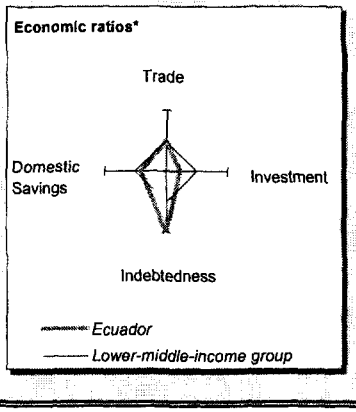
POVERTY and SOCIAL	Ecuador	Latin America & Carib.	Lower-middle-income
1999			
Population, mid-year *(millions)*	12.4	509	2,094
GNP per capita *(Atlas method, US$)*	1,360	3,840	1,200
GNP *(Atlas method, US$ billions)*	16.9	1,955	2,513
Average annual growth, 1993-99			
Population *(%)*	2.0	1.6	1.1
Labor force *(%)*	3.4	2.5	1.2
Most recent estimate (latest year available, 1993-99)			
Poverty *(% of population below national poverty line)*	35	..	..
Urban population *(% of total population)*	64	75	43
Life expectancy at birth *(years)*	70	70	69
Infant mortality *(per 1,000 live births)*	32	31	33
Child malnutrition *(% of children under 5)*	45	8	15
Access to improved water source *(% of population)*	70	75	86
Illiteracy *(% of population age 15+)*	9	12	16
Gross primary enrollment *(% of school-age population)*	127	113	114
Male	134	..	114
Female	119	..	116



KEY ECONOMIC RATIOS and LONG-TERM TRENDS

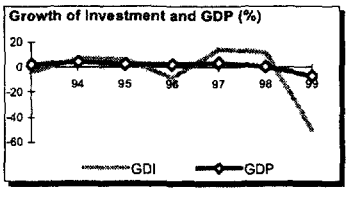
	1979	1989	1998	1999
GDP *(US$ billions)*	9.4	9.8	19.7	19.1
Gross domestic investment/GDP	25.3	20.7	24.7	12.2
Exports of goods and services/GDP	25.9	29.4	25.3	37.3
Gross domestic savings/GDP	25.9	18.9	18.0	24.9
Gross national savings/GDP	22.0	12.5	17.7	24.8
Current account balance/GDP	-4.8	-5.2	-11.0	5.0
Interest payments/GDP	2.9	4.2	3.8	3.6
Total debt/GDP	48.4	115.2	76.8	80.2
Total debt service/exports	60.1	35.6	28.8	22.8
Present value of debt/GDP	..	..	72.2	..
Present value of debt/exports	..	..	240.0	..

	1979-89	1989-99	1998	1999	1999-03
(average annual growth)					
GDP	2.0	2.4	0.4	-7.3	..
GNP per capita	-0.8	0.2	2.1	-14.4	..
Exports of goods and services	4.5	5.2	-3.8	-2.6	..

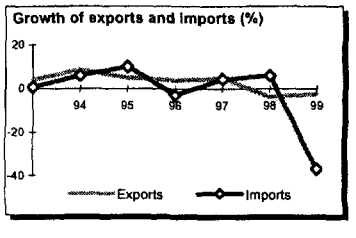


STRUCTURE of the ECONOMY

	1979	1989	1998	1999
(% of GDP)				
Agriculture	13.5	14.0	12.0	12.4
Industry	38.6	37.4	32.7	37.4
Manufacturing	19.2	21.1	21.9	21.3
Services	47.9	48.6	55.2	50.3
Private consumption	61.2	71.7	70.4	65.0
General government consumption	12.9	9.4	11.7	10.1
Imports of goods and services	25.4	31.2	32.0	24.7



	1979-89	1989-99	1998	1999
(average annual growth)				
Agriculture	4.1	2.7	-1.4	1.8
Industry	1.6	2.8	-0.6	-6.0
Manufacturing	0.5	2.4	0.4	-7.1
Services	1.6	2.0	1.8	-11.3
Private consumption	2.1	1.8	2.1	-9.5
General government consumption	-1.2	-1.2	-1.1	-12.9
Gross domestic investment	-3.5	0.4	11.8	-50.5
Imports of goods and services	-1.7	1.8	5.9	-37.0
Gross national product	1.8	2.3	4.1	-12.8

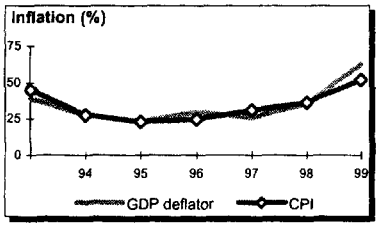


Note: 1999 data are preliminary estimates.

* 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.

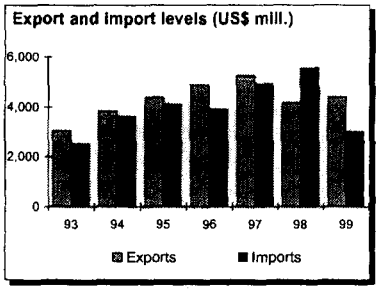
PRICES and GOVERNMENT FINANCE

	1979	1989	1998	1999
Domestic prices				
(% change)				
Consumer prices	10.3	75.6	36.1	52.3
Implicit GDP deflator	16.1	70.8	35.4	62.9
Government finance				
(% of GDP, includes current grants)				
Current revenue	..	14.8	16.2	19.3
Current budget balance	..	2.3	0.4	1.9
Overall surplus/deficit	..	1.9	-4.8	-3.4



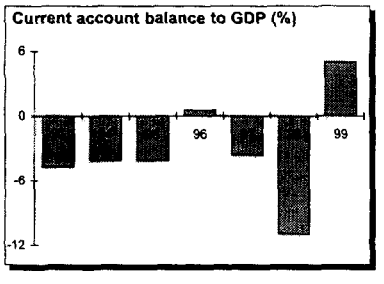
TRADE

	1979	1989	1998	1999
(US$ millions)				
Total exports (fob)	1,659	2,354	4,203	4,451
Oil	720	1,033	789	1,312
Bananas	140	370	1,070	954
Manufactures	..	328	1,004	1,062
Total imports (cif)	1,505	1,693	5,576	3,017
Food	..	..	..	..
Fuel and energy	63	66	326	244
Capital goods	544	625	1,874	815
Export price index *(1995=100)*	123	101	84	100
Import price index *(1995=100)*	93	104	91	84
Terms of trade *(1995=100)*	132	97	92	119



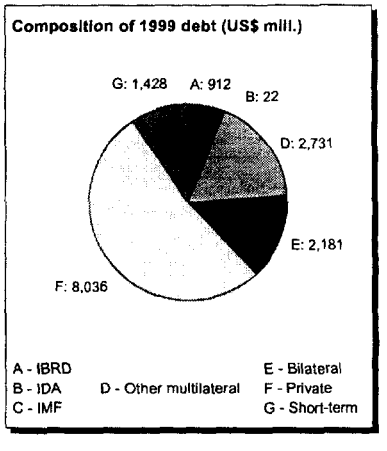
BALANCE of PAYMENTS

	1979	1989	1998	1999
(US$ millions)				
Exports of goods and services	1,838	2,871	5,007	5,263
Imports of goods and services	1,985	2,296	6,409	4,090
Resource balance	-146	575	-1,402	1,173
Net income	-337	-1,186	-1,543	-1,319
Net current transfers	31	97	776	1,101
Current account balance	-453	-514	-2,169	955
Financing items (net)	521	703	1,774	-1,294
Changes in net reserves	-68	-189	395	339
Memo:				
Reserves including gold *(US$ millions)*	740	706	1,786	1,809
Conversion rate *(DEC, local/US$)*	25.0	526.3	5,446.6	8,496.1



EXTERNAL DEBT and RESOURCE FLOWS

	1979	1989	1998	1999
(US$ millions)				
Total debt outstanding and disbursed	4,525	11,317	15,140	15,310
IBRD	85	761	854	912
IDA	37	32	23	22
Total debt service	1,121	1,029	1,706	1,475
IBRD	13	115	136	141
IDA	0	1	1	1
Composition of net resource flows				
Official grants	13	40	66	..
Official creditors	-45	186	188	205
Private creditors	618	242	-247	-30
Foreign direct investment	63	80	831	690
Portfolio equity	0	0	0	0
World Bank program				
Commitments	58	45	111	20
Disbursements	31	75	85	90
Principal repayments	6	46	84	83
Net flows	25	30	0	7
Interest payments	7	70	52	59
Net transfers	18	-40	-52	-52



Additional
Annex 11

Communications Strategy

The implementation of PROLOCAL involves a wide variety of stakeholders, among whom a proactive participatory dynamic needs to be generated. Therefore, a communication strategy has been designed in order to accomplish the following challenges:

⇒ Motivate the beneficiaries so that they get involved in all the implementation stages of the program and recognize it as an opportunity to become the agents of their own sustainable development process.
⇒ Adequately inform the beneficiaries about the objectives and working strategy of PROLOCAL in such a way that expectations about the program are in accordance with what it proposes and the available tools and resources are utilized conveniently.
⇒ Promote, among direct beneficiaries and micro regional actors, the concept of local development as an integral strategy based on a decentralized management model, which respects socio-cultural diversity of the different stakeholders who participate in it and who contribute to the empowerment of local communities.
⇒ Facilitate the exchange of experiences and information among the objective groups to strengthen local development processes supported by PROLOCAL.
⇒ Avoid the risks of politicizing the program, which could derive from the lack of timely and adequate information about its concept, objectives and intervention strategy.

In accordance with the above risks, PROLOCAL considers that communication activities should fulfill the following functions:

⇒ Facilitate the adequate and timely exchange of information among the different components and executing units at the national and regional level, as well as between the beneficiaries and the regional executing units.
⇒ Promote the innovative approach of PROLOCAL in order to reach--through dialogue and debate--agreements among the different stakeholders.
⇒ Facilitate the systematization, evaluation and feedback of experiences promoted by PROLOCAL among the beneficiary population and the rest of direct and indirect stakeholders of the process, in such a way that they can contribute to the consolidation of social capital in the Project intervention zones.
⇒ Encourage social transparency and responsibility in all stages and components of the Project in order to have all involved actors exercise control over Project activities.

PROLOCAL's communication strategy has been designed as an action which will in the long run permit:

⇒ Strengthening dialogue capacity among the different involved stakeholders in local development for the attainment of agreements and consensus that permit sustainability of the process in the long run.

PROLOCAL's communication strategy aims to achieve the following specific objectives:

⇒ Accomplish real participation of beneficiaries in all stages of the process.
⇒ Ensure that the Project gathers the aspirations of the beneficiaries.
⇒ Diminish the risk of political pressure from the part of external actors that could affect the execution of the program and distort future prospects.

PROLOCAL's communication strategy has two components:

a) Organizational communication component: Will facilitate the transference of information from PROLOCAL to all the involved stakeholders with the purpose of positioning the Project.

Results expected to attain with the execution of this component are:

R1. PROLOCAL's organizational identity is known by external and internal actors of the process.

R2. Knowledge of PROLOCAL's organizational identity has reduced the risk of politicizing the Project and has optimized its implementation.

R3. The external actors support PROLOCAL's management and contribute to achieving its goals.

R4. The internal actors consciously assume PROLOCAL's action strategy.

b) Community communication component: Will facilitate the transference of information from the target population to PROLOCAL to ensure that their demands, perceptions and opinions are reflected in project activities.

Results expected to attain with the execution of this component are:

R1. PROLOCAL's organizational identity is known by Project's target population.

R2. Knowledge of PROLOCAL's organizational identity allows the target population to clearly identify the Project's management strategy.

R3. Target population actively participates in the process promoted by PROLOCAL.

R4. Target population provides feedback to PROLOCAL's proposal while implementation of the Project progresses.

Each component will be executed by a specialized firm under the supervision of a communications specialist integrated within the team of the Program Implementation Unit.

Additional
Annex 12

Targeting, Monitoring and Evaluation

Targeting

The PROLOCAL development objective is to improve the well-being of poor rural households in selected areas of the country. Implicit in this objective is the Project's effort to reach the most vulnerable groups of the population. To achieve this goal, targeting at different levels is envisaged in the Project's design.

In its first level, geographical targeting permits concentration of the Project's resources in the poorest areas of the country. Based on the Project methodology, parroquias are the basic units of planning and managing local development, and define the territorial entities of the Project's execution. A total of 120 parroquias in 31 cantones, grouped in 6 micro-regions, were identified as the result of a process which involved the use of statistical information available from various sources and inputs from participatory exercises at the community level. The Project covers an area of 19,000 square kilometers, or 8% of the national territory, and includes more than 800,000 people, of which almost three quarters are poor. Among rural households, representing almost 84% of the entire population, four people out of five are poor. This segment of approximately 600,000 poor people (120,000 households) represents the Project's target population.

The selection of the micro-regions responded to a number of criteria that facilitated the geographical delimitation of areas with strong economic, social and cultural links. To avoid duplications and overlapping with PRODEPINE, it was initially agreed to exclude all parroquias which fell within its area of influence. For the identification of the micro-regions, a multidisciplinary group was formed and a set of criteria established, and included, among others, the geo-political boundaries, average size of the production unit, poverty levels, and availability of infrastructure. Based on these criteria, a total of 14 socio-agro-environmental zones were first identified. Consultations with qualified informants led to a refinement of the potential area of intervention to a total of 42 cantones in 9 micro-regions. A further screening was conducted and 11 cantones in three micro-regions were excluded because, at a closer look, they did not meet some of the selection criteria. The resulting scenario was superimposed with the ODEPLAN's poverty maps to identify the poorest areas.

The selected micro-regions and their characteristics are listed in the following table:

Microregion	# Cantones	# Parroquias	Population	% Rural	% Poor
1. Zona Sur de Manabi	6	26	218,609	76	75
2. Zona Occidental de los Rios	6	16	253,474	68	66
3. Estribacion Central de los Andes	5	12	107,140	78	75
4. Zona Oriental de Lojas	5	29	99,023	84	86
5. Cuenca Alta del Rio Jubones	4	12	51,275	100	79
6. Cuenca del Rio El Angel	5	25	76,132	100	78
Total	**31**	**120**	**805,653**	**84**	**74**

In spite of the great environmental potential of the target areas (soil, water and climate, among others) and of isolated successful entrepreneurial initiatives, the condition of poverty and destitution faced by the vast majority of households in the selected micro-regions is also evident from a number of non-income poverty indicators. The average number of years of schooling is less than four years. The infant mortality rate is 64 per thousand, less than 40% of households have access to a latrine, only one household in seven have sewage and almost half have no

electricity. Within the economically active population, less than 30% receive a regular salary. Field work realized during Project preparation revealed extremely precarious living conditions, lack of opportunities and high inequalities, as well as low self-confidence, widespread social mistrust and poor organizational capacity and leadership.

The depicted scenario of extreme poverty and widespread destitution makes uncertain the feasibility and cost-effectiveness of household-level targeting within each of the selected parroquias. However, in light of the nature of the subprojects, with beneficiary households having to share the burden of the investment, it is likely for the Project to attract a large number of unintended better-off beneficiaries, resulting in unacceptable levels of leakage of the Project's resources.

For this purpose, the Project contemplates the inclusion of procedures at the community and subproject level in an attempt to curb the formation of groups whose majority of participants are among wealthier households, and thus meet the developmental objectives of the Project. The positive externalities of a heterogenous group reflecting the socio-economic make-up of the community are recognized, together with the social, administrative costs of a second-tier targeting and the moral costs associated with unintended exclusions. Therefore, the focus of the second-tier screening will be on introducing community-based processes and implementation procedures at different stages of the Project cycle to prevent and monitor excessive leakage of the Project's resources.

The effectiveness of the targeting methodology will be assessed through the Project's monitoring system as well as on the basis of the proposed ex-post evaluation study and beneficiaries assessment.

Monitoring and Evaluation

The monitoring and evaluation (M&E) system will assess first the provision, then the utilization and coverage of the target population, and finally the impact of the services and inputs provided. It will consist of: (i) a computerized information system, which will track on a continuous basis the Project's progress against process indicators and feed into management's decision-making in almost real time; (ii) periodic beneficiaries assessments, which will provide on an annual basis the target groups' perceptions and reactions about Project progress; (iii) an impact evaluation study, which will quantify in statistical terms the final impact which can be attributed to the Project; and (iv) annual audits and the Bank's regular supervision missions, which will review the technical and fiduciary aspects.

Monitoring system

National and regional coordination units would have the responsibility to collect, analyze, archive and distribute relevant and timely information to assist decision making for Project management. An information system would help in monitoring financial and procurement management, physical implementation, performance of coordination units, performance of local technical assistance service providers, and the achievement of the indicators from the logical framework.

The financial information needed for LACI Project Management Reports (PMRs) would be provided from the financial management module of the monitoring system. Monitoring and processing of procurement of services, goods, works and subprojects would be carried out by the procurement system and by the subprojects information system module. The PMRs for procurement management would be generated from this module. Both the annual planning processes for the coordination units and local development planning would be monitored with specific indicators on planning performance defined in the logical framework.

Physical implementation would be monitored based on the outputs and monitoring indicators for the four components of the Project as defined in the logical framework. The subprojects module would be designed to provide most of the information needed to monitor the actual progress on the implementation of each component. The PMR on project progress would be prepared utilizing the output monitoring indicators.

Regional coordination unit staff would be responsible for obtaining physical implementation progress, local procurement and financial information on subprojects and maintaining the information in the subprojects, financial and procurement information system. This information would be sent periodically to the national

coordination unit for review, approval and aggregation.

Information from the monitoring system would be analyzed by the Project management and disseminated according to the Project's communication strategy to appropriate stakeholders. The Project would provide the LACI PMRs quarterly, and an update on legal covenants compliance every six months, to the Bank.

Beneficiary Assessment

The Project intends to induce changes in a complex rural society, whose subtleties and in-depth functioning are still partly ignored. The assumptions about the positive effects of, and expected reactions to, the Project's activities, although strongly justified, are often hard to substantiate, at least for some groups of stakeholders, and unexpected collateral effects can appear, which could, if not timely detected, play against the Project's objectives. On the other hand, the whole Project is designed to achieve improvements in the life of a target group of people, who become the main actors for the Project's success. It must therefore receive regular feedback from them, to verify if their understanding and eagerness to participate is in line with expectations.

To provide the Project with an adequate tool to achieve these goals, a Beneficiaries Assessment (BA) will be conducted throughout the Project's life.

This BA study has three functions:

1. to permanently feed the Project with qualitative information about the reactions of the poor, and in a timely manner detect unexpected or collateral (positive or negative) effects, in order to better steer Project activities (monitoring function);
2. to assess and measure (although not statistically) the nature, quality and depth of the Project's impact with respect to the Project's KPI, thus complementing the statistical impact evaluation study (evaluation function);
3. to allow the rural poor to express their concerns and own perceptions all along the Project steps, thus gaining empowerment and ownership of the whole process (participation function).

The ex-ante social assessment produced a first insight of the social situation in 4 representative cantónes, and a set of indicators to characterize by component the perceptions of social actors in the field. These elements, together with grassroots information required from the PCU, will be used as inputs to define the themes to be inquired through the BA, and prepare the sampling and interview guides.

The main topics to investigate relate to the Project's performance in: targeting, transparency, efficiency, compliance with beneficiaries' expectations, grade of participation of different stakeholders, and collateral effects of the Project's activities.

Taking into account the lessons learnt from similar projects (Pronader, Prodepine) and the risk of clientelism and political pressures already identified by the ex-ante social assessment as important in the 6 micro-regions, the BA will be conducted yearly, with different objectives according to the Project's progress:

- Year 1: complete the weak social assessment already done, realize a social situation baseline allowing further comparisons, and assess the beneficiaries' perceptions of participatory planning
- Year 2: monitor the effects of participatory planning, training and first subprojects implementation
- Years 3,4,5: monitor all Project activities and measure impacts as activities go along

All Project long: to better understand the reactions of the rural poor and increase their ownership and participation.

Adequate coverage for the study will be obtained with 12 parroquias (2 from each micro-region) for the first session, adding 2 more each year, selected within the ones newly attended by the Project each year.

The sampling will have to be stratified according to gender and age, in a total sample of about 600 persons inquired.

While the rural poor are the main target of the beneficiary assessment, special research will be conducted among other key actors involved, such as: field Project staff, T.A. and NGOs workers, local organizations, community leaders and municipal executives, so as to complete the understanding given by the poor, with information to which they have no access, especially about subprojects, local planning, and the Project's communication and management information systems. This must allow the Project's management to better understand the part played

by, specific interests of, and risks carried by, all these groups of stakeholders.

The Project (specifically its M&E unit, in the person of the evaluation specialist), will prepare terms of reference, and coordinate and supervise, while the BA itself is conducted by a contracted external firm.

Impact Evaluation

The impact evaluation study to be implemented aims at assessing the effectiveness of the Project's targeting and at establishing the degree to which observed changes in both service coverage and final outcomes can be attributed to the Project.

In line with the logical framework developed during Project preparation, the objective of the evaluation system is multifold and includes: (1) assess the Project's contribution in enhancing human and social capital among its beneficiaries; (2) measure changes in access to services and productive assets in the target population; (3) evaluate the Project's effectiveness in reaching the poor and vulnerable groups; and (4) quantify the impact of the Project on poverty, employment and equity.

The proposed evaluation system is based on a longitudinal-control study, consisting of a baseline survey before the implementation of the Project's activities and a follow-up survey of the same households towards the end of the Project on both beneficiary households, as well as a control group. To enable the results of the impact evaluation to feed into future activities, the latter survey is scheduled for the beginning of year five.

The design of the evaluation study is conditioned by three main factors: 1) low Project coverage in the area of intervention; 2) intervention is demand-driven; and 3) areas of intervention have already been identified.

The Project will begin operating in two micro-regions, and will later expand to four additional micro-regions. The expected coverage of the Project within each micro-region is expected to vary substantially depending on the type of Project being implemented, with social investments likely to involve the majority of people in a community, and productive investments to be more restricted to smaller groups. In view of the expected low coverage of the Project in these areas of intervention, and to ensure that a sufficiently large treatment group is included in the baseline sample, oversampling of beneficiaries will be necessary. The treatment group will be drawn from the list of early entrants among the project's beneficiaries, once participating communities have been identified. The timing of the baseline becomes very important as data on the treatment group must be collected immediately after identification of a sufficiently large pool of participating communities but before disbursement of the Project's resources. To partly offset the selection bias caused by only including early entrants in the treatment group, the possibility to conduct the data collection in two separate waves a few months apart will be considered.

As differentiated impact can be expected from certain types of projects, and as to ensure that several, if not all, types of subproject are represented among the selected beneficiaries, if feasible the universe of beneficiaries will be stratified by subproject type prior to selection of the treatment households, and at least two domains of estimation among beneficiaries will be considered.

The identification of a proper counterfactual is key to establishing causality between the Project and any observed change in the chosen indicators. The possibility of randomizing the allocation of project resources was thoroughly evaluated. However, because of certain features in the Project's design, a quasi-experimental design was ultimately deemed more feasible. An external control group will be drawn from a number of Parroquias similar to the ones in the initial area of intervention but beyond Project reach in its five years of implementation. Using data from ODEPLAN at the parroquia level, the control parroquias will be matched based on a number of available socio-economic variables. Also, the presence of development institutions and programs in the areas will be considered as criteria for the matching.

To allow for ex-post matching, a control group larger than the treatment group is foreseen. The ex-post matching might be necessary because of the fact that, despite the proposed ex-ante matching at the parroquia level, it is still possible to end up with a substantially different group of control households. In addition, a larger control group will enable for ex-post corrections in the undesirable event that project activities affect some of the control areas. It is of paramount importance for the Project not to enter the control parroquias at least until year five, as the entire evaluation is premised on this assumption.

The evaluation study will also collect information at the household and community level to statistically control for the non-random nature of the participation process at both levels. To this end, and in an attempt to measure the indirect effect of the Project on non-participating households, a random sample of households within the selected micro-regions will also be included in the study. Finally, the evaluation will also allow for an econometric analysis of the relationships between the different types of Project intervention and the observed changes in key indicators.

The set of socio-economic indicators to be measured by the system reflects the objectives and outputs at different levels proposed in the logical framework of the Project and relates to human and social capacity strengthening and access to productive assets and services at the local level, differentiated by gender whenever feasible, as well as to poverty and equity. Although the former indicators are measures of the Project's achievements in their own right, the evaluation will also aim at estimating the contribution of the Project's productive investments in raising the well-being of its beneficiaries in income terms.

The evaluation study will be carried out by consultants who are not involved in the Project's design or implementation. The Project Implementation Unit, in the person of the evaluation specialist, will be responsible for preparing the TOR for the external consultants and supervising their operations. The evaluation specialist will also be responsible for finalizing the design of the impact evaluation study, including sample selection, as well as for supervising the external consultants during the analysis of the baseline and the impact evaluation study. Provision is made in the budget for hiring an evaluation specialist on a part-time basis and the contracting of external consultants to conduct an analyze the baseline and the follow-up surveys.

Audits and supervision

Standard financial and procurement audits will be performed by independent, specialized firms on an annual basis. World Bank supervision missions will review the technical and fiduciary aspects on a six-month basis, or more often if required. Supervision of specific technical aspects, in particular those under component D, will be performed by specialized firms with relevant experience in the sector and in the area.

Additional
Annex 13

Environmental Assessment Procedure for Financing Local Development Subprojects

I. Procedure for Subprojects Screening

To ensure that acceptable environmental criteria and standards are included in subprojects financed under Component C - Local Investments Fund, the following measures are being introduced in to the Operational Manual: (i) collection of environmental information during subprojects preparation through a standard questionnaire to be completed by proponents; (ii) screening of the environmental procedure by an environmental specialist (ES) in the PCU; and (iii) based on the screening, an environmental analysis and/or environmental management/mitigation plan may be requested as a prerequisite for financing.

The Operational Manual will contain specific guidelines for the evaluation of impacts. The environmental specialist at the PCU will be responsible for preparing these guidelines, which will include procedures for the identification and assessment of significant positive and negative impacts resulting from proposed subprojects. The identification of impact will provide the basis for the identification and description of each mitigating measure, including the type of impact to which it relates and the conditions under which it is required and recommendations for environmental enhancement. This process is explained in more detail as part of the Environmental Management Plan described below.

An Environmental Management Plan would include the following steps:
Identification of Mitigation Measures: In order to significantly reduce adverse environmental impacts, the most feasible and cost-effective measures will be proposed. The plan should seek to: i) identify all anticipated significant adverse impacts; and ii) describe and develop technical details of each mitigation measure, including an estimation of potential impacts of these measures.
Monitoring and Evaluation Plan: Monitoring and evaluation plans will be designed for each one of the four categories or typologies of subprojects. Such plans would provide information about key environmental aspects and the effectiveness of mitigation measures throughout subproject implementation and would give the opportunity to apply corrective actions when needed. Each monitoring plan will set up clear objectives and will include the following key issues: i) description and technical details of monitoring measures, parameters to be measured, methods to be applied; ii) monitoring and reporting procedures to provide information on a permanent basis on the progress and results of mitigation; iii) an implementation schedule for measures that must be carried out as part of the Project, showing phasing and coordination with overall Project implementation plans; and (iv) detailed institutional arrangements necessary for the effective implementation of mitigating and monitoring measures.

A sound monitoring mechanism should allow the PCU to oversee the subproject implementing entity's adherence to environmental requirements (cfr. Annex 13). The mitigation plan will be integrated into the subproject's overall planning, design, budget and implementation. Such integration would be achieved by establishing the mitigation plan as a component of the subproject. In this way, the plan will receive enough funding and will be supervised along with other investment components. When applicable the monitoring plan would be attached to the subproject's tripartite implementation agreement (convenio). If a less extensive analysis is required and the development of a management plan is not necessary the incorporation of best practice standards for specific activities, followed by the design of preventive or mitigating measures, would be enough to ensure that sound environmental practices are incorporated to Project design and implementation.

PROLOCAL will not finance the subprojects specified in a negative list under the OM, which would include:

a) Any type of activities not legally authorized in protected areas;
b) Agricultural activities that would entail the deforestation or transformation of native forests into cultivation or pasture areas;
c) Forestry activities that would imply the deforestation of native forests;

d) Colonization of areas with native forests;
e) Use of mangroves;
f) Development of cultivars in steep areas that would produce soil erosion;
g) Purchase and use of equipment for logging;
h) Construction of dams or roads in areas occupied by native forest;
i) Any type of activity that will threaten endangered species or their habitat;
j) Purchase and use of pesticides classified as dangerous and extremely toxic by the World Health Organization.

Capacity Development and Training: The PCU and Regional Coordination Units (RCUs) will carry out screening, environmental assessment and monitoring. Both units will be staffed with environmental specialists whose job descriptions and work experience will permit them to accurately review and process subprojects.

II. Environmental Baseline Survey

Considering that specific subprojects will be known only during the implementation phase, it was agreed that an environmental baseline survey would be carried out during the preparation phase to provide: (i) a strategic guidance to the Borrower on prioritizing investments for financing; (ii) the context and recommendations for mitigation or prevention measures appropriate for different subproject types.

A local consulting firm was contracted in December 2000 to develop the environmental baseline survey in the six micro-regions in which the Project will be implemented. The survey was completed at the end of February, 2001. It is a first approach to the understanding of the main environmental issues affecting the six micro-regions as the initial step in the environmental assessment process. The survey provides a description of current physical, biological and socio-economic characteristics. It also makes an initial approach to the identification of relevant environmental impacts in each micro-region and provides preliminary recommendations to address such impacts.

The Survey comprises reports with the environmental baseline (one per micro-region), and a questionnaire to be used in the screening process to help identify subprojects requiring impact mitigation measures.

Methodology

The analysis of the environmental status of the six micro-regions was based on a review of available secondary information. The main sources of information were the surveys and studies carried out by PROLOCAL and PRONADER, and reports issued by public agencies such as the Ministry of the Environment, National Council of Water Resources (Consejo Nacional de Recursos Hídricos), National Mining Directorate (Dirección Nacional de Minería), National Institue of Statistics and Census (Instituto Nacional de Estadísticas y Censos), Ministry of Social Welfare, National Herbarium and the Planning Unit of the President's Office (ODEPLAN). Basic Cartography was provided by CLIRSEN and the Instituto Geográfico Militar.

Secondary information was complemented with additional data collected at the field and interviews to representatives from Municipalities, Ministry of Agriculture, Centros Agrícolas Cantonales, NGOS, and local leaders.

The survey in each micro-region was based on the analysis of physical, biotic, social, economic and cultural parameters. The level of detail for each parameter varied according to the availability of secondary information among the six micro-regions.

Results

As mentioned in previous sections, the six micro-regions were selected among the poorest in the country. They hold around 800,000 inhabitants, of which almost three quarter are poor. In spite of the benefits provided by the existing environmental characteristics (soil, water, and climate), the condition of poverty among the six micro-regions is very evident. The access to basic services such as health, education, water and electricity is very limited, so living conditions are precarious. It is well known that poverty and the lack of knowledge about critical environmental problems are the main causes for the unsustainable use of natural resources.

Additional
Annex 14

SOCIAL ASSESSMENT FINDINGS

The social assessment (SA) gathered and analyzed qualitative information in six cantones. Four of them 24 de Mayo, Ventanas, Paltas, and Santa Isabel represented the area of PROLOCAL, and two of them, Daule and Guano represented the area of PRONADER (Loan 3390-EC).

These rural ccntones contain several micro-climates ranging from 200 mts a.s.l. and up to 4.000 mts a.s.l. with poor local economies based on agricultural activities. Testimonies confirmed that local populations perceive themselves as blanco-mestizos peasants (colonos) who inhabit this region for more than approximately three generations. This finding applies to all six micro-regions in the Project as they were selected to not include indigenous people, so an Indigenous Peoples Development Plan, as described in OD 4.20 would not apply to this Project. The main local survival strategies among poor peasant families, combine small-scale agriculture and recurrent migration to national and international destinies. The SA confirmed the high incidence of poverty and exclusion resulting from overlapping their geographical isolation with low income, poor educational levels, poor market integration, lacking credit access and deficient basic services provision.

The Social Assessment in the Project files provide the extensive information that was used to design PROLOCAL. As a summary, the table below offers a synoptic view of the perceived needs relatively to the Project components A, B and C, and to the need for rural financial services.

Gender Issues

The consulting group which carried out the SA received active assistance from the Bank's regional gender studies team, which had already prepared the "Ecuador Gender Review 2000". This assured that field methodologies and subsequent analysis had a gender equity perspective. The SA found that continuing immigration of male heads of household to urban centers and foreign countries is enhancing the role of women in agricultural production, commerce and in their communities. Their active roles in local organizations and new sources of family income have made them key stakeholders for PROLOCAL. At the same time the SA found evidence of a high rate of alcoholism among men with women being most affected by domestic violence.

Table 1
Indicators of perceptions by component and strategic objective of PROLOCAL

Component	Strategic Objective	Qualitative Result	Indicators for baseline for evaluation of beneficiaries of the project
1. Management of local development	· Strengthening of the local organizations · Empowerment of the different poverty groups	1.1 Capacity and quality of the actors for local development management has improved. 1.2 Participatory methodology applied in the formulation of plans and subprojects. 1.3 Design of development plans realized 1.4 Design of subprojects realized.	1. Perception by differentiated group consider that their demands to improve quality of life are incorporated in the activities of the organization. 2. Perception by differentiated groups if the organizations represent them before the state and the institutions. 3. Perception by differentiated groups if the organizations are legal and democratically constituted. 4. Perception by differentiated groups if the economic handling of the organization is transparent. 5. Availability of communication systems (telephone, computer, email). 6. Perception differentiated of the importance of planning. 7. Perception by differentiated groups of the degree of participation of the main organizations and private and public institutions in the elaboration of the plan. 8. Perception of the differentiated groups if the main ideas of the action plan respond to their demands. 9. Degree of responsibility by differentiated groups that perceives to have in the development plans. 10. Dimension of the demands of the plans (short term versus development). 11. Adjustment of the project to the demands differentiated by gender, ethnicity and age. 12. Opinion by gender, ethnicity and age groups of the effectiveness and efficiency of the project. 13. Opinion by gender, ethnicity and age groups of the focus of the project regarding the most poor. 14. Perception of women and men regarding changes in the manner in which decisions are made within the family.

2. Support to supplier of services	· Strengthen capacity of supply of local development services.	2.1 Institutional and social actors with adequate demand 2.2 Increase of supplies of local development services 2.3 Increase capacity of supply services	15. Perception differentiated of the technical capacity and management of the local personnel to carry out the activities of the plans and project in the microregion. 16. Perception differentiated of the technical capacity and management of the local institutions to carry out the plans and project in the microregion. 17. Demand differentiated demand of training in participative methodologies, communication, administration and sustainable local development..
3.Local investment fund	· Dispose of the necessary assets to drive the local development process · Projects that drive local development	3.1 Co-investments possibilities (resources not reimbursable) 3.2 Institutional suppliers providing services 3.3 Projects operating	1. Demand differentiated of the services of trained men and women. 2. Demand differentiated of the services of the strengthened institutions by PROLOCAL 3. Perception differentiated of the roles that must be fulfilled in the functioning of the PROLOCAL co-investment projects. 4. Assessment differentiated of the quality of local development services in the management of the development plans and projects.
4.Strengthening of rural financial systems.	· Increase available capital for development of the local financial system.	4.1 Local financial organizations with more technical capacity. 4.2 Credit fund operating. 4.3 Risk and guarantee fund operating.	5. Perception differentiated of power to be subject of credit by type of local offerer (bank, local cooperative...) 6. Perception differentiated perception of responsibility as opposed to the payment (to those who pay and those who do not) 7. Role of the different systems of credit in its productive programming. 8. Confidence differentiated in the stability of the credit service. 9. Confidence differentiated in the transparency of the credit service. 10. Confidence of differentiated groups to save by type of local offerer (bank, local cooperative).