

PROJECT INFORMATION DOCUMENT (PID) CONCEPT STAGE

Report No.: PIDC1112

Project Name	Horticulture Development Project (P133703)
Region	EUROPE AND CENTRAL ASIA
Country	Uzbekistan
Sector(s)	Crops (50%), Agricultural extension and research (50%)
Theme(s)	Rural markets (100%)
Lending Instrument	Specific Investment Loan
Project ID	P133703
Borrower(s)	Ministry of Finance
Implementing Agency	Rural Restructuring Agency
Environmental Category	B-Partial Assessment
Date PID Prepared/ Updated	12-Nov-2013
Date PID Approved/ Disclosed	14-Nov-2013
Estimated Date of Appraisal Completion	23-Jan-2014
Estimated Date of Board Approval	14-Mar-2014
Concept Review Decision	Track II - The review did authorize the preparation to continue
Other Decision (as needed)	N/A

I. Introduction and Context

Country Context

Uzbekistan, a low middle-income, resource rich, landlocked country, is the third largest country in Central Asia by land mass, and the largest in terms of population. It accounts for nearly half of the region's population, and its economic and social development is critical both Uzbekistan's 29.8 million population and the Central Asia region. Since independence in 1991, in contrast with most of the Commonwealth of Independent States (CIS) countries, Uzbekistan has adopted a gradual approach to transition and market development. This approach resulted in less painful economic and social conditions than experienced in most CIS countries and, in recent years, strong macroeconomic performance.

Today Uzbekistan has a fast-growing economy with an average real growth rate of Gross Domestic

Product (GDP) at 8.4 percent between 2008 and 2012. Per capita income has more than doubled in real terms since 2004. Poverty declined from 27.5 percent of the population in 2001 to 16.0 percent in 2011 due to rapid economic growth, large government investments in education, health and infrastructure development, increases in public sector salaries, and increased remittances. However, the elasticity of poverty reduction to GDP growth remains low due to a number of factors, including low productivity of agricultural sector and regional divergences in growth. Over the past decade growth has been driven by commodity exports (cotton, gold and gas), industry (energy, chemicals, cars, food-processing, and textile) and more recently by services. The structure of the economy has also changed with the contributions to domestic production shifting away from primary agriculture (mainly cotton) to industry and services. Prudent macro-management, favorable terms of trade and limited integration of the financial system with the world economy have made Uzbekistan's economy resilient to the global financial crisis.

The Uzbek development strategy aims to transform the country into an industrialized upper middle-income country by the year 2030. This implies that per capita income, which is presently estimated at US\$ 1,715, would need to increase almost ten-fold by then. To reach this level of per capita income in 2030, the economy of Uzbekistan would need to grow at an average of 6.0 percent per annum. The global environment for growth in the medium-term has become more challenging since the global economic crisis of 2008-09 and the current situation of growing uncertainty in the Eurozone. The weak outlook for global growth means that more attention will need to be paid in Uzbekistan to remove structural impediments to growth and generate enough jobs for the rapidly expanding labor force. In order to achieve this objective, the Uzbek economy needs to improve in the short term the functioning of institutions and to develop infrastructure, improve in the medium term its efficiency and, ultimately, provide a more favorable environment for innovation.

Sectoral and Institutional Context

Uzbekistan is a major agricultural producer, regionally and globally. Agriculture remains an important component of national income, and has grown at a robust pace in recent years. Agriculture generates about 16 percent of GDP and contributes to the well-being of the nearly 14.5 million people who live in rural areas. The horticulture subsector has been a source of growth within agriculture and offers an opportunity to sustain recent gains in agricultural productivity. Traditionally cotton and wheat are the dominant crops in Uzbekistan and they currently take up the dominant share of land resources. Still, the area devoted to horticulture has been increasing steadily. In 2010, an additional 240 thousand hectares of land was reassigned to horticultural production under new government policies. Despite its small footprint, the economic impact of the fruit and vegetables subsector is large, accounting for 50 percent of the value of crop output and over 35 percent of export earnings.

The agro-climatic conditions that support horticulture in Uzbekistan are found in very few places and are the foundation of the subsector. In addition, steady economic growth over the last 10 years (including an 8.1 percent GDP growth rate reported in the third quarter of 2012), supplemented by strong population increase (at an annual rate of 2.7 percent) has resulted in an expanding domestic market for horticultural goods. Moreover, during the next decades, continued growth in income, population and urbanization are expected, sustaining a growing domestic demand for horticultural goods. As in other countries, an increase in domestic incomes in Uzbekistan has been accompanied by a shift in the Uzbek dietary preferences that favors horticulture. Uzbekistan is also well positioned to take advantage of the large and growing markets for horticultural products in Russia, Kazakhstan and other countries.

The farm structure in Uzbekistan has gone through a series of changes following independence. The reforms began with the restructuring of state and collective farms established during the Soviet era. Between 1990 and 1998, the state farms were converted into various economic entities, mainly lease-based collective farms. In 1998, the former state and collective farms were converted into cooperative farms (shirkats), where the production assets were managed by families. In 2002 the Government began a conversion of shirkats into private farms. Agricultural land is also held in the form of dehkan farms, small-scale operations largely based on household labor. Citizens living in rural areas are entitled to small inheritable household plots. As of 2010, they occupied about 13 percent of irrigated arable land and produced 63 percent of gross agricultural output (State Statistics Committee of the Republic of Uzbekistan, 2010).

Beginning from 2004, a lease-based land use system was introduced for all forms of farming entities, except for dehkan farms. Land plots are allocated to farmers on long-term lease for 49 years, with the minimum area for cotton and grain farms set at 30 hectares, and horticulture farms set at 5 hectares. Starting in 2006, 'agri-firms' were established within the horticultural subsector. Agri-firms are non-government associations and private firms that participate in the distribution and processing of fruit and vegetables; occasionally they have evolved into vertically integrated trading or processing firms that also operate private farms. As of 2012, there were 267 agri-firms in Uzbekistan.

In 2008, 2009 and 2010, selective land leases for unprofitable farms and farms where state resources were misused were revoked and farm land optimization was implemented by administrative measures. The number of private farms declined by 70 percent, and the average size of land plots increased from 27 hectares to 80 hectares. More recently, the Government has converted selected cotton-and-wheat farms into horticultural farms. For example, in late 2011 more than 500 private wheat and cotton farms concentrated in 25 districts were converted to farms specializing in horticulture.

Horticulture in Uzbekistan has also been a crucial for policy experiments in Uzbekistan. Most arable land in Uzbekistan is planted to grains and cotton, and these subsectors operate under a different set of policies. With the exception of what is produced on small dehkan plots, most field crops and orchards are situated on public lands operated by private farms under long-term leases. In the case of grains and cotton, private farmers are given a production quota under the terms of the lease and, in exchange, are given a guaranteed market and price for their production and receive support in the form of delivered inputs. In contrast, dehkan farmers growing any crop and private farms specializing in horticulture are given greater choice about what they produce and how they produce it. The Government has supported the subsector in many important ways, but has adopted a special set of policies for the horticulture subsector that rely on private investment, and private input and output markets.

At the same time, the Government has provided considerable indirect support to the sector by building high quality research institutes to support research in new varieties, as well as research in field and post-harvest technologies. Strong research institutions have helped sustain productivity growth in the horticulture subsector. Research related to fruit trees, grapes and wine making is managed by the Schroeder Institute, which has operated for 70 years. The Institute has branches in each region of the country, and has a well-established production and research capacity. Research on horticultural field crops, including melons and potatoes is managed by the Uzbek Research

Institute for Vegetables, Melons and Potatoes (RIVMP). The RIVMP is also a long-standing research center, having been established in 1933. The Government has also helped ease shortages for new planting materials and eased import duties and taxes on machinery and advanced irrigation inputs.

The cotton sector in Uzbekistan has come under intense international scrutiny. Although Uzbekistan has signed the ILO conventions on child and forced labor and has adopted pertinent national legislation, children and adults are reportedly forcibly mobilized to pick cotton. The World Bank recognizes the seriousness and complexity of the forced labor issue in Uzbekistan, and believes that the most effective way it can address the issue is to use a holistic approach through (i) continuous country dialogue and collaboration with international agencies and donors; (ii) sector policy dialogue and program interventions; and (iii) specific project interventions. The Bank is collaborating with the UN and other development partners in an active dialogue with the Uzbekistan government on the child/forced labor concerns. As the proposed project supports the development of the lucrative horticulture sector, it is expected to contribute to a diversification away from cotton production. Nonetheless, the Bank will continue working with the Government of Uzbekistan, to agree on the adoption of appropriate measures to address the issue of child and forced labor in this proposed project.

Relationship to CAS

The interventions of the recently prepared Country Partnership Strategy (CPS) focus, among others, on two key challenges: (a) diversifying agriculture away from cotton and wheat into other high value crops such as fruit and vegetables; and (b) intensifying agricultural yields and productivity. The proposed Horticulture Development Pilot Project will focus on crops other than cotton, as well as analytical and advisory activities to develop a horticulture strategy.

The project also builds on recommendations from a recent Horticulture Policy Note for Uzbekistan Strengthening the Horticulture Value Chain (ACS4703). The first set of recommendations is aimed at improving farm productivity. Although the recommendations are based on a review of the horticultural sector, many relate to the agricultural sector in general. They include recommendations for: (i) protecting genetic resources and continuing the country's strong commitment to catalog genetic material; (ii) restoring land and improving water resource management; (iii) sustaining domestic improvements in production technologies; (iv) finding innovative ways to deliver extension services; (v) sustaining support for new private investments; (vi) expanding the successful program of granting farmers greater autonomy; and (vii) facilitating land markets. A second set of recommendations aims to support high-value export markets. These include: (i) strengthening support for quality and food safety standards; (ii) building a brand for Uzbek horticulture; (iii) continuing to support private access to quality and productivity enhancing equipment; and (iv) continuing on-going efforts to remove obstacles to foreign direct investment in the sector. A final set of recommendations is aimed at eliminating unintended incentives that encourage the use of informal, low-valued market chains. These include: (i) eliminating export restrictions on horticultural produce; (ii) easing restriction on the use of foreign currencies in trade; (iii) dropping the revenue tax on farm products; and (iv) promoting competition by bring more firms into the formal export chain.

Broadly, the activities detailed in this document are designed to advance the first productivity constraints and enhance markets and to build-up an understanding of best policy practices among stakeholders by drawing on the experience of countries with strong horticulture subsectors and

thriving agricultural sectors.

The proposed project also complements efforts at the IFC. The IFC recently signed a Financial Advisory Services Agreements with two state-owned companies under the Ministry of Foreign Economic Relations, Investment and Trade (Uzmarkazimpex and Uzprommashimpex) to attract investors/operators to finance, build, own and operate a portfolio of six (6) refrigerated warehouses in Uzbekistan. The total planned capacity of warehouses is 21,100 MT. Appropriate sites have been identified in Djizzak, Samarkand, Fergana, Bukhara, Kashkadarya and Surkhandarya regions. The investment requirement is estimated at about USD 31 million. The proposed project private beneficiaries can benefit from the IFC initiated cold storages services in the same project areas.

Also, IFC plans to sign an agreement with the Hamkorbank to help build its capacity to finance agricultural investments. Under the agreement, IFC will provide training on agricultural lending, assist in developing a client database, and help the bank expand agri-lending through on-the-job training. The proposed project Participating Financial Institutions can benefit from the IFC advisory project to provide better services to the project beneficiaries.

II. Proposed Development Objective(s)

Proposed Development Objective(s) (From PCN)

The development objective of the proposed project is to strengthen the horticulture subsector by: i) facilitating investments along the value chain in order to improve productivity on the farm, improve quality and reduce post-harvest loss, and reduce food safety hazards; ii) improving the flow of information about best practices on farm and along the value chain; iii) facilitating the adoption of a supportive policy framework for the subsector.

Key Results (From PCN)

Success of the project will be monitored against the following key results indicators:

- i. Increased investment on the farm and along the marketing chain consistent with objective component i;
- ii. Increased research and outreach activities by public agricultural research centers and public-private associations;
- iii. The development of improved mandatory quality and safety standards in Uzbekistan that comply with international standards (i.e. IPPC, CODEX, ISO, HACCP, GMP, GAP); and the development of voluntary industry standards that facilitate the expansion of exports, through the establishment of standardized operation procedures, certification program and on farm quality assurance;
- iv. Increased opportunities for policy makers and stakeholders to learn about and discuss the relevance for Uzbekistan of policies that have been effective in other countries.

III. Preliminary Description

Concept Description

The area to be covered by the project was discussed with the Ministry of Agriculture and Water Resources and it was tentatively agreed to include the following five regions: Tashkent, Jizzak,

Samarkand, Kashkadarya, Andijan, Fergana and Namangan. The project is proposed to be implemented over a 6-year period, and will include three components as described below.

Component 1: Agricultural Support Services - Providing Public Goods

As discussed in the Horticulture Policy Note for Uzbekistan Strengthening the Horticulture Value Chain, Uzbekistan's horticultural sector has grown rapidly, fueled by growing domestic and export demand, and by rates of on-farm profits that are high relative to alternative crops. The rapid expansion has brought with it a new set of market participants on the farm and along the marketing chain, straining the capacity of existing institutions. The general market for agricultural input and output services is less extensive than in similar-sized agricultural sectors elsewhere. This is in part because the governance structures of dehqan and private farms growing horticultural produce are different from those under which private wheat and cotton farms operate. Grain and cotton producers occupy 84 percent of the arable land in Uzbekistan and are given production quotas by the state, and are supplied with pesticides and fertilizer. In contrast dehqan farmers make their own arrangements for purchasing fertilizers, pesticides, machinery, planting materials, etc. and organize the sale of their outputs.

As a consequence, agricultural input and output markets are not fully mature in Uzbekistan and the large number of farmers growing horticultural subsector for the first time are unfamiliar with many of the technical aspects of growing the crop and with market-reliant activities. Entrepreneurs entering to provide inputs or down-stream services lack experience as well for many of the same reasons. All of this creates a knowledge gap, which current institutions are unable to close in a timely way.

The public institution responsible for developing and disseminating new biological and mechanical technologies are well respected as centers of excellence, but the rapid expansion of the sector has brought challenges there as well. The scale and variety of threats from pests and disease has increased rapidly with the import of planting material and the expansion of cultivated areas. Moreover, it is important for the research centers to fully document the genetic material present in the traditional local varieties of fruit and vegetables and to document and preserve the genetic material present in Uzbek forests, since these may be the building blocks for improving future varieties.

To respond to the above challenges, the following set of activities is proposed to be included in this component component in order to strengthened two research institutes:

- Provide assistance to assure improved planting materials, disease and pest identification and soils tests by supporting labs and training personnel
- Identify and document genetic material available in the wild and material found in local varieties non-commercial varieties
- Develop the capacity to map pests and diseases as outbreaks occur in order to coordinate actions to stem related crop losses
- Support demonstration farms and media-based mechanisms for disseminating information about mechanical and biological on-farm technologies, including information about varieties, irrigation, greenhouses and post-harvest equipment
- Develop modular training programs for farmers and traders for all areas, including storage, post-harvest handling, packing and marketing, and food hazard controls

- Develop and disseminate basic materials to help farms manage the business-side of farming, including basic information on record keeping, marketing, and business plans.
- Explore and disseminate information about alternative energy technologies, including solar energy and energy based on agricultural by-products
- Support study tours for leading farmers

The following set of activities would be funded in order to strengthen the public-private institutions that facilitate agricultural input and output markets:

- Build the capacity of voluntary associations along the value chain with the goal of drawing up quality standards, codes of conduct, and organizing marketing campaigns, drawing on the successful experiences of other countries
- Improve market information, including price information gathering and reporting, about domestic regional markets and destination markets in Russia and the Ukraine
- Undertake market studies of potentially interesting fruit and vegetable markets for Uzbek producers to help farmers improve profitability;
- Undertake market-channel studies identifying bottlenecks and opportunities for new private sector investments (e.g. collection points for processors, new packaging, new crops, etc.)
- Provide technical support in marketing via publications of articles, video and coordinated events at demonstration plots with information about packing, volume, quality and food safety requirements along various marketing channels.
- Participate in national and international trade shows for fruit and vegetable stakeholders to promote investments and exports, and to improve quality of production, marketing and investment decisions.
- Establish opportunities for stakeholders and policy makers to learn from countries with advanced horticultural subsectors about successful policies

As discussed in the Policy Note, food safety hazards often emerge as marketing chains become more complex and these pose a public health threat to domestic consumers. In addition, quality and food safety assurances become increasingly important in export destination markets. In recent years, supermarkets, fast-food restaurants and other buyers of horticultural products impose their own private-sector standards on suppliers in order to protect their reputation and core business. To date, Uzbekistan's horticultural exports, especially exports to Russia, have grown rapidly because of their high quality and early availability. However, the ability of Uzbek exporters to penetrate high end markets may become more limited because of weak food hazard controls, as Russia implements its obligations under the WTO and as supermarkets and restaurants capture a larger share of the produce market.

For example, more than 90% of Uzbekistan's fresh produce has been traditionally sold in Russia and not many of these fruits and vegetables have entered supermarket chains due to inadequate packaging, sorting and grading of produce. In Russia supermarkets are winning in competition with traditional open markets and thus, the size of Russian market for produce from Uzbekistan has decreased twofold in the past five years, while local production continued growing.

Furthermore, a study prepared under the Bank-financed Central Asia One Health Project in 2011 identified a number of recommendations to strengthen the national food safety structure controls and reduce the risk of food borne diseases. The recommendations and conclusions are divided into

three sections: legislative framework, administrative and institutional structures and operational aspects of the food chain. Implementation of these recommendations will be important for improved food safety and public health in Uzbekistan, and for enhanced export potential of horticulture products.

The following set of activities would be financed under this component to protect local consumers should be protected from unsafe products and improve their access to higher quality products. They would also help farmers, processors and traders manage their reputational risks and improve the image of Uzbek produce outside of the country, thereby improving access to the most attractive marketing channels.

- o Assist developing good production and handling practices according to GlobalGAP, HACCP and other internationally recognized food safety systems;
- o Help Uzstandart translate into Uzbek various international fruit & vegetable quality requirements;
- o Develop manuals of quality and packaging requirements for various products in various countries where products from Uzbekistan are or could be sold.
- o Work with private-public voluntary associations to gather and disseminate information about private-sector standards in domestic and destination markets

Component 2: Facilitating Private Investment - Access to Credit

While knowledge gaps contribute to many problems along the horticulture market chain, private sector investments are often required to solve the problems. By way of example, it is estimated that over 30% of vegetable and fruit crops are wasted due to lack of proper storage and the inability to process crops that do not find their way into fresh produce markets. Although there is no data to show the total capacity of the country's cold storage, field visits suggest that the majority of the horticulture farmers, mainly dehkan farmers, do not have access to the modern post harvest pre-cooling and cold storage facilities. Fresh farm produce cannot maximum its shelf life without pre-cooling after harvest even the transportation with refrigerator is available for export market.

The agro-business sector in Uzbekistan remains constrained by the lack of capital in general, but investment capital in particular. Whereas the banking sector has in recent years registered significant gains in the availability of short-term lending resources, long term resources remain limited. Demand for agricultural financial services is high and is not currently being sufficiently met. Consequently, banks and leasing companies still need long-term funds in order to respond to investment demands from their clients.

The objective of the Access to Credit component is to enhance access to financial services for agribusinesses operating in Uzbekistan's horticulture sector, in particular towards enhanced competitiveness of the sector, improved quality and food safety standards, and establishment of market linkages. The component would finance such investments as new cultivar, seeds/seedlings, water-saving irrigation facilities (such as drip irrigation), cold storage and other cold chain facilities, and value added handling/processing equipment and facilities. The project will build on the experience gained during RE SP II which has achieved sizeable results with provision of financial services to Uzbekistan's agricultural enterprises. RESP II also supported capacity building of the participating banks to improve their skills in appraising agriculture-related investment loans.

The component would further expand the access to the investment financing through additional lending resources for use by banks and leasing companies for on-lending agribusiness. The project would also support introduction of new financial products to support value chain development in the sector.

Line of Credit for Banks and Leasing Companies. This sub-component will finance investment activities, principally for enterprises operating in the horticultural sector, through qualifying commercial banks and leasing companies. The current needs of agribusinesses for financing far exceed the long-term funds available to commercial banks, as shown by the high demand for investment funds under RESP II. Particularly, attention will be focused on investments supporting the enhanced competitiveness of the sector, access to new technologies, value addition in the sector, and improved market access through establishment of market linkages. In addition, the project would introduce a range of innovative structured finance products, to support development of market linkages and value chains. These products are expected to take the focus of the financial sector off the traditional forms of collateral, help agribusinesses borrow to deliver under signed contracts, and develop relationships between farmers, agro-processors, wholesalers, retailers, etc.

Similar to RESP II, the Credit Line will be extended through qualified commercial banks and leasing companies, the Participating Financial Institutions (PFIs). A PFI will be a commercial bank or a leasing company selected on the basis of a set of PFI Eligibility Criteria, which include compliance with banking laws and prudential norms and regulations, maintenance of a healthy financial status and sound lending policies and procedures. The credit line will be open to all interested commercial banks which qualify through the due diligence process. Leasing companies are also encouraged to undergo the due diligence procedure, as leasing arrangements may be more attractive than loans in some cases due to lesser collateral requirements. An operational manual for the credit line (similar to the Rural Enterprise Investment Regulations under the RESP II) will set forth the eligibility criteria for PFIs, sub-borrowers and sub-projects to be financed and the procedures for all parties involved in the implementation of the credit line.

Capacity building program for Financial Institutions. Given the novelty of the non-traditional financial products to support value chain development, the project will implement a capacity building program for the financial institutions involved in the project. The PFIs will receive training on applicability of the new financial products in lending to agriculture, assessing the suitability and effectiveness of these new financial products, and on mitigation of the related risks. The PFIs will receive hands-on training in practical application of the new financial products through long-term (resident) TA, training and a study tour to a country with a developed agricultural finance system and application of value chain finance in agriculture.

Component 3: Project Management

The component will be focused on strengthening the MAWR's and RRA's capacity for Project management, monitoring and evaluation through the provision of goods, consultant services, Training, and financing of Incremental Operating Costs. This component will (i) support operation of the RRA, and finance overall project management, as well as contract administration, procurement, and financial management; and (iii) establish a robust performance based Management Information System (MIS) and arrange for data collection and reporting on key performance output and impact indicators, through baseline surveys, participatory assessments, mid-term review and final evaluation.

IV. Safeguard Policies that might apply

Safeguard Policies Triggered by the Project	Yes	No	TBD
Environmental Assessment OP/BP 4.01	x		
Natural Habitats OP/BP 4.04			x
Forests OP/BP 4.36		x	
Pest Management OP 4.09	x		
Physical Cultural Resources OP/BP 4.11		x	
Indigenous Peoples OP/BP 4.10		x	
Involuntary Resettlement OP/BP 4.12		x	
Safety of Dams OP/BP 4.37		x	
Projects on International Waterways OP/BP 7.50		x	
Projects in Disputed Areas OP/BP 7.60		x	

V. Financing (in USD Million)

Total Project Cost:	160.00	Total Bank Financing:	150.00
Financing Gap:	0.00		
Financing Source			Amount
Borrower			10.00
International Bank for Reconstruction and Development			150.00
Total			160.00

VI. Contact point**World Bank**

Contact: Dilshod Khidirov
 Title: Senior Rural Development Specialist
 Tel: 5771+255
 Email: dkhidirov@worldbank.org

Borrower/Client/Recipient

Name: Ministry of Finance
 Contact: Mr. Jamshid Kuchkarov
 Title: Deputy Minister
 Tel: (998 71) 233-7073, 139-1132
 Email: JKuchkarov@mf.uz

Implementing Agencies

Name: Rural Restructuring Agency
 Contact: Nasriddin Najimov
 Title: General Director

Tel: /Fax: (998-712) 371-657
Email: resp_sks_uz@slider.sks.uz

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VII. For more information contact:

The InfoShop
The World Bank
1818 H Street, NW
Washington, D.C. 20433
Telephone: (202) 458-4500
Fax: (202) 522-1500
Web: <http://www.worldbank.org/infoshop>

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