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India: NABARD VII (Small Irrigation)

Ex-post evaluation

OECD Sector	24030 Financial intermediaries of the formal sector	
BMZ project number	1995 669 36	
Project-executing agency	National Bank for Agriculture and Rural Development	
Consultant	---	
Year of evaluation	**2002**	
	Project appraisal (planned)	**Ex-post evaluation (actual)**
Start of implementation	Q 3 1996	Q 4 2001
Financing, of which FC funds	EUR 17.4 million	EUR 17.4 million
Other institutions/donors involved	None	None
Performance rating	4	
• Significance / relevance	4	
• Effectiveness	4	
• Efficiency	4	

Brief Description, Overall Objective and Project Purposes with Indicators

The project comprises the extension of a credit line to the National Bank for Agriculture and Rural Development (NABARD) in the amount of EUR 17.4 million for the purpose of refinancing sub-loans granted by financial intermediaries to small agricultural enterprises for irrigation measures. The overall objective is to heighten agricultural production and to increase and stabilize income in rural areas. The purposes of the programme are improved credit supply for small agricultural enterprises and enhanced efficiency of NABARD and the participating financial intermediaries (cooperatives). The target group of the project primarily comprised small farmers in India with property of up to 2 ha who were to be selected according to NABARD's criteria for providing support. In order to achieve the programme purposes and the overall objective two indicators were defined.

- The share of units receiving financial support for which the real family income could either be ensured or increased one year after the loan-financed investment should be at least 80%.
- The repayment rates of cooperatives participating in the programme should improve by 2.5% annually assuming a minimum rate of 65% or, if the initial rate is already 80%, then it should at least remain constant.

Project conception / Major Deviations from the original Project Planning and their main Causes

At the time of the project appraisal the structural problems of the cooperative sector were regarded as critical since they led to non-sustainable credit supply in rural areas and, due to the losses that were incurred, placed a heavy burden on the national budget. Fundamental sector reforms were considered absolutely vital. With respect to NABARD as an apex refinancing institution for the banking system in rural regions, its double function as a source of refinance and as a supervisory authority, the loans it extends according to a supply-led approach, and the state guarantee for loan defaults were particularly criticized. Against this backdrop the “new definition of NABARD” and the implementation of sector reforms with the support of the World Bank were mentioned as prerequisites for sustainable agricultural financing. The following reform steps were considered essential to the system’s ability to survive on its own:

a) Complete deregulation of interest

b) Complete abolishment of target group lending

c) Complete abolishment of supply-led liquidity planning

d) Refinancing of the rural lending business via loans from commercial banks and bonds and thus the successive reduction of state-subsidized income (NABARD)

e) Extension of loans based on criteria for the creditworthiness of the borrowers instead of on the type of investment

In spite of the repeated approval of the reforms by the Indian government, thus far it has not initiated any concrete steps for their implementation. Owing to the sluggish reform process, since 1996 NABARD has no longer received support from the World Bank in the financial sector. Therefore, hopes for significant reforms in the cooperative sector have not been fulfilled to date.

Key Results of the Impact Analysis and Performance Rating

For NABARD, the financing of small irrigation projects has traditionally been an important area of activity. In the 1980s the share of financing for small irrigation projects was approximately 40%; currently it still accounts for 10.2% due to the diversification of the credit portfolio. In the months of June and July 1997 the FC funds financed a total of 8490 such projects under the realm of NABARD’s regular business activities. 83.6% of the FC funds flowed to the cooperative bank Uttar Pradesh Sahakari Gram Vikas Bank (UPSCARDB) in Uttar Pradesh, 12.3% to Maharashtra, 3.7% to Gujarat and 0.4% to Tamil Nadu. According to the respective local situation, diesel pumps, pipe pits, sprinkler systems etc. were financed. Only new projects received funds.

The key results of the impact analysis and samples tested by NABARD in Uttar Pradesh prior to the local ex-post evaluation were:

- Far more than 90% of the farmers receiving financing have less than 2 ha of land.

- The yield per hectare was able to be improved by up to 60% depending on the crops and region.

- The net family income rose in each case under examination owing to the improved yield; the higher costs were taken into consideration.

- The area of irrigated land was increased substantially as a result of the investments that were carried out.

Measured by the corresponding indicator, overall both the non-monetary goal and the overall objective have been achieved.

As regards the monetary goal, the target indicator for the repayment rates was formally met. Thus, UPSCARDB, for example, had a repayment rate of 79.7% at the beginning of the project, which it was able to increase to 86.2% by March 2001. However, from today's perspective the indicator agreed during the project appraisal offers only a limited amount of information on the programme purposes: the relatively good portfolio quality of the intermediaries involved is due less to the requirements of NABARD for the FC credit line but rather to the fact that with one exception, NABARD only involved those intermediaries in the credit line who satisfied the target indicator from the very beginning. As the sector reforms, deemed essential during the project appraisal, and a new definition of NABARD were practically not implemented, no significant improvements in the performance neither of the institutions involved nor of the overall system arose; none would have been able to be proven on the basis of the agreed indicator. At 65% on average, the repayment rate for the overall system remains unchanged at a low level.

The project's refinancing of small irrigation projects was a positive contribution to stabilizing and increasing the income of small farmers. Nevertheless, the project could not create new jobs as hoped because in most cases the work is performed within the family (category **SHA**). In India, taking out a loan has traditionally been a task for men. Women are not advantaged in the extension of loans and account for only a minimal percentage of the borrowers. Therefore, it cannot be attested that the project specifically supports gender equality (category **GO**). The promotion of environmental protection and resource conservation was not a project goal. Thus, we assign the project into category **URO**. In view of the lax execution of technical requirements and protective laws of the water utilities, water consumption by small irrigation projects is unnecessarily high and there is a danger that the groundwater resources are being overused. NABARD needs to take action in this regard.

In a summarized assessment of all future impacts and risks we have arrived at the following rating of the project's <u>developmental effectiveness</u>:

Measured by the agreed target indicators the project purposes have formally been met. Given the limited informative value of the indicators as mentioned above and the sector reforms, which have practically not been applied, the performance of the participating banks cannot be said to have improved and sustainable credit supply cannot be said to have been brought to rural areas. The limitation of the programme to relatively efficient cooperative banks ensured that the funds were put to effective use, but in light of the systemic weaknesses and the fungibility of the funds it could not help encourage sustainable credit supply. Therefore, overall we classify the project's **effectiveness** as **inadequate** (partial evaluation: rating 4).

The aspect of efficiency should be differentiated in the assessment. The effects of the financed project on the income of the target group can be judged as being relatively efficient. Our appraisal is negative with regard to NABARD and the cooperatives involved. Owing to the interweavement of the various institutional tasks at NABARD and taking the effective state guarantee for loan defaults into account, the efficiency of the institutions – measured on the operative level by the margin of need – and also their financial efficiency – measured in terms of their real RoA – are judged to be unsatisfactory. From a macroeconomic perspective the project's efficiency – with a volume of system losses accumulating annually of USD 500 million – is inadequate. Ultimately, despite its concentration on relatively efficient cooperative banks, the project helps encourage this inefficient, subsidized system. After taking these aspects into account, we also classify the project's **efficiency** overall as **inadequate** (partial evaluation: rating 4).

The project was able to achieve the defined overall objective and thus by all means had significant developmental effects. On the target group level the project's offer of long-term financing was principally a relevant contribution to resolving the main problem identified during the project appraisal. However, the subsequent reclassification of already approved loan applications to the FC credit line raises the question of the extent to which bottlenecks really existed in the credit supply to the small farmers in specific cases. Added to this is the fact that NABARD's financing policy – which continues to be supply-led only – and the strict financing conditions only meet the needs to a very limited degree. Beyond that the project hardly contributed at all to increasing the efficiency of existing irrigation systems, identified during the project appraisal as the key challenge which irrigation farming faces.

A look at the financial sector level reveals that the programme must be rated as having clearly insufficient significance. The reforms stated to be essential during the project appraisal were not initiated and are not expected to be introduced in the future, either. The hopes for successful implementation of a sector reform programme by the World Bank were not fulfilled, and the related risks were underestimated during the project appraisal. Ultimately the financial support of NABARD discouraged rather than encouraged pressure to reform, despite the lack of a serious willingness to reform.

Therefore, overall we classify the project's **significance** and **relevance** as inadequate (partial evaluation: rating 4).

In general the programme has an **inadequate degree of developmental effectiveness** (**rating 4**).

General Conclusions applicable to all Projects

The key issue raised by the project is whether and in what form an FC project should be carried out whose decisive precondition for long-lasting effectiveness is a functioning financial sector and which is characterized by extreme structural difficulties and scant desire to reform. The lesson that can be drawn from the project NABARD VII is that a project approach whose scope and concept cannot contribute to resolving these structural problems makes little sense. However, this does not mean that in principle no projects with such a constellation should be realized; rather, in a similar existing situation projects should be planned in such a way that, with corresponding complementary support, they begin to be structurally effective to a limited degree via demonstration effects in a segment that is able to be influenced – in this case by concentrating on a cooperative bank and pursuing a demand-led credit policy with adjusted technologies.

Legend

Developmentally successful: Ratings 1 to 3

rating 1	Very high or high degree of developmental effectiveness
rating 2	Satisfactory degree of developmental effectiveness
rating 3	Overall sufficient degree of developmental effectiveness

Developmental failures: Ratings 4 to 6

rating 4	Overall, no longer sufficient degree of developmental effectiveness
rating 5	Clearly insufficient degree of developmental effectiveness
rating 6	The project is a total failure

Criteria for the Evaluation of Project Success

The evaluation of a project's "developmental effectiveness" and its classification into one of the various levels of success described in more detail below during the final evaluation concentrate on the following fundamental questions:

- Are the **project objectives** reached to a sufficient degree (aspect of project **effectiveness**)?
- Does the project generate sufficient **significant developmental effects** (project **relevance** and **significance** measured by the achievement of the overall development-policy objective defined beforehand and its effects in political, institutional, socio-economic and socio-cultural as well as ecological terms)?
- Are the **funds/expenses** that were and are being employed/incurred to reach the objectives **appropriate** and how can the project's microeconomic and macroeconomic impact be measured (aspect of **efficiency** of the project concept)?
- To the extent that undesired **(side) effects** occur, are these tolerable?

We do not treat **sustainability**, a key aspect to consider for project evaluation, as a separate category of evaluation but instead as a cross-cutting element of all four fundamental questions on project success. A project is sustainable if the project-executing agency and/or the target group is able to continue to use the project facilities that have been built for a period of time that is, overall, adequate in economic terms or to carry on with the project activities on its own and generate positive results after the financial, organizational and/or technical support has come to an end.