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Auditor General

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AUDIT REPORT
AGRICULTURE SECTOR
USAID/PERU

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Area Auditor General Latin American
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I INTRODUCTION

The Office of the Area Auditor General, Latin America, has made an audit of the active Loans and Grants in the agriculture sector under the United States Agency for International Development bilateral economic assistance program to the Government of Peru (GOP).

The purpose of the audit was to evaluate progress being made on program activities and to review the effectiveness of implementation and resources utilization.

II BACKGROUND AND SCOPE

Peru is at a critical juncture in its development. It is a country attempting to consolidate 10 years of revolutionary change, moving toward a more open democratic political system, and trying to deal with a deepening economic crisis which is rapidly eroding the Peruvian standard of living. The U.S. assistance program has a vital role to play in helping to create the conditions for long-term growth and equality in Peruvian society.

The current situation of Peru is a marked contrast to the climate of hope which many felt when the Revolutionary Government announced and began to implement a sweeping program of social and economic reform 10 years ago. Then, the government carried out rapidly and without violence one of the most massive agrarian reform in the history of Latin America. Today, the government lacks the resources to make the agrarian reform work, or to deal with the bulk of rural poverty which was never touched by the reform measures. The performance of the agricultural sector, with a few notable exceptions, has been poor for the past 10 to 15 years.

The strategy paper prepared by the Mission for FY 1979 has principal focus on the sierra poor, secondary focus on the migrating poor (ceja de selva development and the urban slums), and a third focus on institutional innovation and reform. Within the agriculture sector priorities are as follows:

1. Improving farm productivity in the sierra is the crucial first step to ameliorating Peru's most severe poverty. The largest portion of AID financing will be concentrated in efforts to:
 - Increase food output on small to medium sized farms. These farms can absorb the majority of sierra surplus labor and dampen the flow of migration to coastal cities. Major increases in small-scale, on-farm investments are required. U.S. assistance is vital.
 - Help rebuild the structure of institutional services to agriculture. It will be difficult to reach the poorest rural Peruvians and affect productivity without improving institutional channels which have deteriorated badly in recent years.
 - Target in on identifiable groups within the sierra which stand at the bottom of the list of all the poverty indicators. Mission activities to improve high pastures and Andean livestock and to organize community nutrition programs will aim at these hard-to-reach groups.

- Target in on identifiable groups within the sierra which stand at the bottom of the list of all the poverty indicators. Mission activities to improve high pastures and Andean livestock and to organize community nutrition programs will aim at these hard-to-reach groups.
- Test the feasibility of and help apply appropriate rural technologies.

2. Creating off-farm employment in the sierra is essential to a broad attack on the programs of landlessness, underemployment and income maldistribution. The Mission will assist through:

- Programs to stimulate small business, especially agriculture-related enterprises, in the private and cooperative sectors.

3. Exploiting the agricultural potential of the ceja de selva affords Peru one of its few opportunities for easing the severe land tenure constraints of the sierra over the longer terms. AID will be involved through:

- Building basic infrastructure to make commercial agriculture possible.
- Upgrading the capacity of market towns in the ceja de selva to better serve their agricultural hinterlands and provide off farm employment for sierra migrants.

The agriculture sector assessment has identified the target groups on the basis of land tenure and rural organization. The development requirements include the revitalization of government institutions serving agriculture, assistance in small farmer organizations, land use planning, on-farm capital investment and appropriate rural technology. The major areas of proposed and actual agriculture sector assistance follow:

1. Research and Extension - Both research and extension are weak in farm management/production economics. There are two active projects, Project 0143, Campesino Para-Technician Training and Operational Program Grant (OPG)-0179, Campesino Training. The Mission plans a loan/grant program in research and extension for Fiscal Year 1980.

2. Small Farmer Organization - Loan No. 058, Agriculture Cooperative Federation Development is assisting the second-level farmer organizations. However, the majority of sierra farmers fall outside the organizations and must be grouped together to receive government services and to market their output more effectively. The USAID plans to provide grant funds for technical assistance to the Ministry of Agriculture (MOA), and, through OPG's, to experimental small farmer organizations in the sierra.

3. Agricultural Inputs

Improvement of Seed Multiplication and Distribution

Peruvian agriculture needs an orderly, self-sustaining system for improved seed production and distribution. Research and extension are inadequate without a plentiful source of improved seed for farmers to grow. Currently improved seed is often not available at planting time. Project 0149, Corn and Soybean Production on Small Farms is providing research assistance for the two crops. In the future the Mission will provide the MOA with a program of technical assistance for analyzing existing seed multiplication and distribution sub-systems, resulting in recommendations for improving the institutional and financial aspects of the structure.

Irrigation and Other On-Farm Investments

One of the principal basis of increased farm productivity in the sierra is the application of irrigation water. Considerable potential also appears to exist for capital investment through land leveling, drainage, reforestation, etc. Loan 059, Improved Water and Land Use in the Sierra is providing assistance in these areas. Future plans contemplate technical assistance to the MOA in on-farm capital investment activity, training for cooperative personnel and MOA technicians to improve their ability to identify on-farm investment opportunities and a study of private sector cooperative banking channels for on-farm investment.

Improved Breeding Stock

Severe decapitalization of breeding stock has taken place in the sierra. The USAID plans to study the problem of sierra breeding stock, to provide technical assistance to the MOA in the improvement of pastures and to provide technical assistance in improved management of alpaca and llama herds.

4. Off-Farm Employment Generation - There are presently two projects which generate off-farm employment. Project 0144, Fresh Water Fisheries Development and Loan 060, Rural Development Agribusiness Fund.

5. Ceja de Selva Regional Development - Loan 061, Sub-Tropical Lands Development is financing certain infrastructure to open the high jungle to more intensive cultivation.

6. Appropriate Rural Technology - The USAID is exploring unconventional technologies for potential benefit to the rural poor, as well as the more conventional technologies that deal with government research and extension. Project 0150, Use of Treated Sewage for Irrigation is an on-going pilot effort.

The scope of audit included a review of four loans (\$52 million) and seven grant projects (\$3.0 million). We examined project files, held discussions with project personnel, made visits to implementing agencies, inspected project sites, made a limited review of supporting financial records and performed such other procedures considered necessary to meet the objectives of the audit. The financial cut-off date was March 31, 1979, but project implementation was covered in some cases through May 31, 1979.

III SUMMARY

The review disclosed that AID assistance programs under the Agriculture Sector in Peru are within the U.S. country strategy plan. Most projects are slow in getting started and behind in planned implementation. The prime reasons for this are shortfalls in GOP counterpart support for projects and the constant changing of GOP implementing agencies. The economic situation in Peru is poor and as a result the GOP has had to make budget cuts for all of its agencies. Once projects do get underway, project results are usually successful. Project monitorship by the USAID in most cases is good although the implementation of two projects, Sub-Tropical Lands Development and the Soy and Corn Production on Small Farms have been delayed because of the late filling by AID/W of project personnel. Also we feel that the Fresh Water Fisheries Project has inadequate monitorship.

Following is a summary of projects reviewed under the Agriculture Sector. Details are contained in Part IV, Findings and Recommendations section of the report.

The Agriculture Cooperative Federation Development Loan is about 18 months behind in planned implementation. Delays in the approval of development plans and changes in implementing agencies have been the primary reasons for slow implementation of this project (see page 8).

The implementation of the Water and Land Use in the Sierra Loan is behind schedule because irrigation sub-project studies were late getting started. An advisor under a technical assistance contract was not performing satisfactorily because of a lack of Spanish language capability. A required audit of the technical assistance contract has not been performed (see page 11).

The Rural Development Agribusiness Fund Loan was slow getting started because of credit institutions unfamiliarity with procedures necessary to process sub-loans. However, as these credit institutions become familiar with these procedures, processing of sub-loans is expected to improve (see page 14).

Loan conditions precedent have not all been met and thus implementation of the Sub-Tropical Lands Development Project Loan has not started. The late designation of the Project Manager position by AID/W has contributed to the slowness by the borrower in meeting conditions precedent (see page 15).

The Campesino Para-Technician Training Project, although slow in starting, has progressed satisfactorily and the first stage of the project has been completed (see page 16).

Implementation of Fresh Water Fisheries Development in the Department of Ancash has not been satisfactory. Inadequate GOP project management, lack of counterpart funds for construction and operating expenses, administrative problems between GOP agencies and inadequate training of operating personnel have contributed to the poor performance of this project. Deficiencies were also noted in the use of project commodities (see page 18).

The Soy and Corn Production on Small Farms Project, delayed in getting started, has made progress since the arrival of a U.S. contracting team. GOP budget cuts have slowed project progress (see page 23).

The use of Treated Sewage for Irrigation Project is now progressing satisfactorily after delays in construction of the irrigation infrastructure. A production loan to the cooperative whose members are cultivating the project site has not been made because the agreement between two GOP agencies has not been consummated (see page 25).

The initial state of the On-Farm Water Management project went well. However, funds for the continuance of the project are being held up because a completed required evaluation by the GOP has not been approved (see page 28).

The activities of the first phase of the Campesino Training operational program grant are completed. The project is in its second phase. Required baseline data for project evaluation has not been submitted to the USAID (see page 30).

Ten of 11 Special Development Projects in the Agricultural Sector were successful. The one project failure was found to be economically unfeasible (see page 30).

I. Project No. 527-0170, On-Farm Water Management

1. Background

On December 29, 1977 the USAID entered into a Project Agreement with the GOP to improve on-farm water management practices among small farmers in order to increase production. The project will be implemented by a Utah State University contracting team working with the Ministry of Agriculture's Directorate General of Water (DGE) technicians in conducting systematic research of soil, plant and water interrelationships for major Peruvian food crops, demonstrating the effects of improved water management practices on water use and crop production, and developing irrigation system designs that optimize water application according to soil type, fertilizer utilization and crop.

AID's contribution to the project is being provided in increments, with the initial grant of \$189,000 financed under Project Agreement No. 1, December 29, 1977. Project Agreement No. 2, March 30, 1979, makes an additional grant increment of \$191,000 available. Subsequent increments will be subject to availability of funds and to the mutual agreement of USAID and the GOP. As of March 31, 1979, the status of funds was:

<u>Project Agreement No. 1</u>	<u>Obligations</u>	<u>Accruals</u>	<u>Unliquidated Balance</u>
Contract	\$164,000	\$127,540	\$36,460
Commodities	14,547	14,541	6
Participants	5,453	-	5,453
Other	<u>5,000</u>	<u>670</u>	<u>4,330</u>
Total	<u>\$189,000</u>	<u>\$142,751</u>	<u>\$46,249</u>

The final contribution date is June 30, 1979. Project Agreement No. 2 with a project assistance completion date of September 30, 1981, provides funds as follows:

Contract	\$175,600
Commodities	5,000
Participants	7,700
Other Costs	<u>2,700</u>
Total	<u>\$191,000</u>

The project contribution of the Ministry of Agriculture includes administrative and technical personnel, agricultural machinery, vehicles, laboratory facilities, office space with secretaries and operating expenses for the operation of the Project Research/Demonstration Farm sites as well as facilities and materials for bulletin publication.

2. Implementation

The first year of project implementation went well. Research and demonstration farms were established in three locations. Six in-depth water-soil-plant interaction research studies were conducted. Some 60 applied research-demonstration studies were performed. A national irrigation manual was prepared, eight extension type bulletins were prepared and five farmer field days were held. Five students are writing their thesis on varying aspects of the project. Numerous students, professionals, Ministry of Agriculture personnel, farmer organizations and private individuals received informal training at the three research/demonstration sites.

An irrigation engineer and an agronomist are providing technical assistance to the project through a contract with Utah State University. Most of the project funds have been used to support the contracting team. In addition, project funds were used to procure a vehicle, and testing and demonstration equipment.

None of the funds earmarked for participant training have been spent because the contractor has not found any suitable Peruvian technicians to receive short-term training.

A project evaluation, following guidelines established by the USAID, was made in April 1979 by personnel from the National Planning Office. The evaluation was not submitted to the USAID. As of May 18, 1979 the evaluation had not been approved on the GOP side. As a result there are no project funds available from Project Agreement No. 2, and project activity has been reduced. The agreement provides that an evaluation must be made of project accomplishments before funds can be considered as available for other activities. The USAID should determine why there has been a delay in approving the project evaluation. If the evaluation concluded that project implementation has been satisfactory the National Planning Office should immediately approve the evaluation.

Recommendation No. 7

USAID/Peru should obtain a copy of the evaluation and in conjunction with the National Planning Office determine if project objectives were met. If project objectives have been met, the USAID, in agreement with the GOP should proceed in implementing Project Agreement No. 2.

On January 23, 1979, by decree law, the National Institute for Agriculture Research (INIA) became the GOP implementing agency for the project. While there have been problems in the organization and functioning at the INIA, the Utah State University contracting team believes the new organization will be better for on-farm water management activities because the Directorate of Soil and Water under the INIA now has total counterpart responsibilities.

Counterpart funds for operating expenses have been limited but INIA is supposed to get an allocation of P.L. 480, Title I generated local currency in June 1979. The USAID is continually following-up on this matter.

J. Project No. 527-0179 - Campesino Training

1. Background

This Operational Program Grant was executed February 8, 1978 in the amount of \$100,000. The purpose of the grant is to increase agricultural production and productivity for approximately 2,500 independent, small farmers and their families in selected areas of the Peruvian sierra and ceja de selva through a pilot training program. The project is to be carried out in two phases. The first phase (approximately six months) will entail selection of trainers and technical advisors, diagnosis of needs and training required, and preparation of appropriate instructional materials. The second phase (18-24 months) will entail training farmers in approximately 200 short-term courses in subject areas relevant to the independent, small farmers' needs, including not limited to, livestock and poultry care, crop and food storage, animal nutrition, seed selection, fertilizer application, and food handling and preparation.

At the end of the project, instructional packages will be compiled and made available to GOP, private and international institutions interested in helping Peru's poor, small farmers.

The project is to be implemented by the GOP Instituto Peruano de Fomento Educativo (IPFE). IPFE will use its own staff as well as outside professionals for implementing the project.

The financial status of the project at March 31, 1979 was:

	<u>Obligated</u>	<u>Expenditures</u>	<u>Unliquidated Balance</u>
Other Costs (Training)	\$ 59,092	\$32,134	\$26,958
Commodities	<u>40,908</u>	<u>36,894</u>	<u>4,014</u>
Total	<u><u>\$100,000</u></u>	<u><u>\$69,028</u></u>	<u><u>\$30,972</u></u>

This phase of the project completion date is August 30, 1979. Subject to the availability of funds and the mutual agreement of the parties, AID will provide additional funds in FY 1979 to finance the activities remaining to complete the project.

SUMMARY OF AGRICULTURE SECTOR LOANS
As of March 31, 1979

<u>Loan Title and Number</u>	<u>Authorized</u>	<u>Disbursed</u>	<u>Available Balance</u>
Agriculture Cooperative Federations Development, 527-T-058	\$ 7,000,000	\$ 395,195	\$ 6,604,805
Water and Land Use in the Sierra, 527-T-059	11,000,000	1,329,636	9,670,364
Rural Development Agribusiness Fund, 527-T-060	15,000,000	363,880	14,636,120
Sub-Tropical Lands Development, 527-T-061	<u>19,000,000</u>	<u>21,505</u>	<u>18,978,495</u>
Total	<u>\$52,000,000</u>	<u>\$2,110,216</u>	<u>\$49,889,784</u>

SUMMARY OF AGRICULTURE SECTOR GRANTS
As of March 31, 1979

<u>Grant Title and Number</u>	<u>Obligations</u>	<u>Accrued Expenditures</u>	<u>Unliquidated Balance</u>
Campesino Para-Technician Training, 527-0143	\$ 100,000	\$ 97,168	\$ 2,832
Fresh Water Fisheries Development in the Department of Ancash, 527-0144	465,000	225,969	239,031
Soy and Corn Production on Small Farms, 527-0149	1,875,000	965,428	909,572
Use of Treated Sewage for Irrigation, 527-0150	200,000	153,166	46,834
On-Farm Water Management, 527-0179	189,000	142,751	46,249
Campesino Training, 527-0179	100,000	69,028	30,972
Special Development Project Activities, 527-0061	<u>33,928</u>	<u>23,928</u>	<u>10,000</u>
Total	<u>\$2,962,928</u>	<u>\$1,677,438</u>	<u>\$1,285,490</u>

LISTING OF RECOMMENDATIONS

Recommendation No. 1

USAID/Peru request Plan MERIS to have an interim financial audit made of the contractor ATA-CLASS.

Recommendation No. 2

USAID/Peru request ORDENOR-CENTRO to train the Huaraz laboratory employee in the use of the equipment.

Recommendation No. 3

USAID/Peru provide the Colorado State University contracting team with timely status reports of project events.

Recommendation No. 4

USAID/Peru assure the Tioga Motor Home Demonstration Unit in Huaraz is used for project purposes and if not successful request a refund of \$17,153 from the GOP for the cost of the Tioga Motor Home.

Recommendation No. 5

USAID/Peru should request the ORDETAM Project Manager to indicate to the farmer the crops that are prohibited and establish an inspection system to assure compliance with the law.

Recommendation No. 6

USAID/Peru request the GOP to determine which agency, the Ministry of Agriculture or ORDETAM, will sign the loan agreement with the Agrarian Bank.

Recommendation No. 7

USAID/Peru should obtain a copy of the evaluation and in conjunction with the National Planning Office determine if project objectives were met. If project objectives have been met, the USAID, in agreement with the GOP should proceed in implementing Project Agreement No. 2.

Recommendation No. 8

USAID/Peru request IPFE to obtain baseline data for measuring project results.

REPORT RECIPIENTS

	<u>Copies</u>
Deputy Administrator, AID/W	1
Assistant Administrator - Bureau for Latin America and the Caribbean (LAC), AID/W	1
Mission Director, USAID/Peru	5
Country Officer, ARA/AND/P, AID/W	1
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