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Agenda Item 6

IFAD'S FRAMEWORK FOR  
DEFINING PROJECT IMPLEMENTATION PERIODS  
AND EXTENSION OF LOAN CLOSING DATES

I. BACKGROUND

1. As a follow-up to IFAD's plan for the formulation of operational policies and procedures, which was contained in the document EB 96/57/R.31, during the year management has examined the issues involved in defining project implementation periods and extension of loan closing dates. In-house reviews were initiated to assess the Fund's past experience in dealing with the subject matter, with a view to finding out whether the current procedures are appropriate to the continuously changing conditions for the development of IFAD-type projects. While in many aspects the current procedures remain valid, it became clear that adjustments are needed in some areas in order to provide staff with better operational guidance. In the light of such a judgement, and since all the actions are of an operational nature within the authority of the President, management has decided to amend some aspects of the current procedures, which will be presented in Part III below.

2. This document has been prepared to inform the Executive Board of IFAD's progress in the follow-up to its formulation of operational procedures in this area. Part II contains a summary of the current procedures for defining project implementation periods and extension of closing dates. Part III outlines the adjustments in the operational procedures on the basis of past practice. An annex provides a review of IFAD's past experience in handling the issues in question.

II. CURRENT PROCEDURES

3. IFAD's procedures for defining project implementation periods and extension of loan closing dates are elaborated in the Loan and Grant Administration Manual, which was issued in September 1994. Similar to the approaches of other international financial institutions (IFIs), IFAD's project implementation period represents the best estimate of the time required for the physical execution of project activities, and it is made during appraisal. Based on this estimate, a project completion date for marking the termination of physical implementation is agreed upon between IFAD and the borrower at loan negotiations and recorded in the Loan Agreement.

4. The loan closing date, which stands for the last date by which the borrower should complete withdrawals from the loan account, is also established at loan negotiations and specified in the Loan Agreement. This date is normally set six to twelve months after the anticipated project completion date, depending on the nature of the project. For projects that are relatively straightforward, a six-month interval between the above-mentioned two dates is normally sufficient. For complex projects with multiple implementing agencies, a nine or twelve-month lag is always preferable. The interval allowed between project completion and loan closing dates is intended to ensure sufficient time for submission of final withdrawal applications after the completion of physical implementation.

5. At the closing date, IFAD may terminate the right of the borrower to withdraw funds from the loan account and, by notice to the borrower, may cancel any amount of the loan remaining unwithdrawn. However IFAD may also extend the closing date where delays related to project implementation have occurred, either by IFAD's own initiative or at the request of the borrower. IFAD's decision to approve the extension of a loan closing date is based on the assessment carried out by the cooperating institution (CI), six months prior to the closing date, confirming that the project remains viable, the overall performance of the borrower and the project executing agency is satisfactory, and the extension is likely to lead to successful completion. The CI's assessment should give specific consideration to the following aspects: (a) factors causing delayed project implementation; (b) additional time needed for completing the project and consolidating its achievements; (c) any special action required by the borrower or IFAD to ensure completion within the extension period; and (d) any action required to bring a non-complying borrower into compliance with loan covenants.

6. Extension of the loan closing date is normally authorized for one year at a time. In exceptional circumstances where a longer period is clearly warranted, extension may be made for up to two or, in rare cases, three years.

7. The loan closing date is not allowed to be extended for the purpose of using cost savings, financing unforeseen project expenditures, or permitting disbursements that require a change in project description. Extension is also not authorized where the borrower is not in compliance with covenants of the Loan Agreement or while a loan is under suspension. In the latter case, however, based on the CI recommendation, IFAD can opt for either: (a) keeping the loan open informally until the suspension is lifted, after which a formal extension may be considered; or (b) closing the loan.

### III. MANAGEMENT DECISIONS ON OPERATIONAL PROCEDURES

8. Management has decided to introduce the following adjustments into the current operational procedures. These adjustments supersede the relevant provisions of the current procedures.

#### Defining Project Implementation Periods

9. Length of Implementation Periods<sup>1/</sup>. The reference implementation period for an "e" or "f" type project<sup>1/</sup> will be six years. The implementation period for a "c" type project<sup>1/</sup> will be established consensually by IFAD, the cofinancier(s) and the borrower. A much greater emphasis will be placed on effective and timely implementation. In this connection, project design will need to ensure better and realistic implementation planning, taking into account available implementation capacity. A vigorous process of portfolio management will be instituted to closely monitor the performance of project implementation, so as to ensure the initiation of follow-up actions in a timely and effective manner.

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<sup>1/</sup> This framework will be complemented by the policy framework for programme lending, which will be developed in the near future.

<sup>2/</sup> The "e" type project refers to a project initiated and exclusively financed by IFAD. The "f" type project refers to a project initiated by IFAD and cofinanced by other donor(s).

<sup>3/</sup> The "c" type project refers to a project initiated by another financial institution and cofinanced by IFAD.

10. Commencement. In order to count a real period of effective implementation, the project implementation period will commence on the date of loan effectiveness. In case the conditions of effectiveness are not met two years after loan signing, follow-up actions will be initiated in collaboration with the government, in order to either meet the conditions in a short period of time or to cancel the loan immediately.

#### Extension of Loan Closing Dates

11. Conditions for Extension. Extension of a loan closing date will be accepted in exceptional cases, instead of being of a routine nature. The project controller will need to demonstrate that serious efforts have been made by IFAD, the CI and the borrower to address the factors affecting project performance. Extension will be granted only when there has been an active management of the portfolio, and on the basis of sound planning for actions during the extension period and of the borrower's strong commitment and assurances for improvements. Efforts will be made to avoid the need for further extensions when planning for the initial extension. The criteria stipulated by IFAD's current policy on extension of loan closing dates are valid, but improvements are needed in the application. Explicit and quantifiable criteria will be used to justify the proposal of extension, such as: satisfactory physical and financial progress, adequate targeting of the rural poor vis-a-vis the original estimates, evidence of satisfactory project organization and financial management performance, sufficient local funds, etc.

12. Cumulative Length, Number of Extensions and Disbursement after Closing Date. The cumulative length of extension of a loan closing date for a given project will be limited to three years. Since extension will be treated as an exception, the number of extensions granted for a given project will be kept to the fewest possible. Therefore the forward action plan for extension should contain elements to minimize the need for further extensions. No disbursement may be made after the closing date, and any amount of the loan remaining unwithdrawn beyond such a date will be cancelled.

13. Cases for Which No Extension of Closing Dates should be Made. Extension of loan closing dates will not be made in the following circumstances: (a) where funds remain, mainly because the project objectives were not reached due to over-optimistic design, or because devaluation of local currency or unforeseen cofinancing made it possible to implement the project with fewer IFAD funds; (b) where an extension has been previously granted and the targets set for physical progress and loan disbursement over that extension period have not been realized; and (c) in case of non-compliance of loan covenants by the borrower.

14. For "c" and "f" type projects, IFAD will coordinate with the cofinancier(s) to reach a decision on the extension of loan closing dates.

#### Loan Cancellation

15. The overall strategy on loan cancellations covers the full project development cycle: more emphasis at the project design stage will be given to early start-up and 'implementability' of a project; better in-house quality control will improve project planning, including more precise costing of projects. Efforts will also be made to fully activate the potential of beneficiary participation, government involvement and the use of in-country resource groups, so as to achieve a higher level of local commitment to project implementation. At the same time, country portfolio review and project reformulation will be used to manage loan cancellation. A "portfolio clean-up" in which the partial

cancellation of loans will play an important part will be undertaken over the next two years. This is particularly true for those projects nearing the end of their implementation periods. During the exercise, project controllers will review and present the status of portfolios and actions to enhance their performance. Beyond this time frame, loan cancellations will be carefully managed by the regular loan portfolio management process.

## REVIEW OF IFAD'S EXPERIENCE IN DEFINING PROJECT IMPLEMENTATION PERIODS AND EXTENSION OF LOAN CLOSING DATES

### I. INTRODUCTION

1. IFAD's current procedures for defining project implementation periods and extension of loan closing dates are elaborated in the Loan and Grant Administration Manual, which was issued in September 1994. A summary of these procedures is provided in Part II of the main text. It is obvious that the implementation period of IFAD-type projects must be defined realistically to ensure that the impact of its support to the rural poor can be maximized without sacrificing institutional efficiency and effectiveness. Clear criteria are also needed for the extension of the loan closing date, so that the incidence of loan extensions can be contained at a reasonable level. The following paragraphs will present IFAD's past experience in the application of the set procedures. They are intended to serve as a basis for identifying gaps and emerging issues that may stimulate suggestions for adjustments.

### II. THE PAST PRACTICE

#### Trends in Setting Project Implementation Periods

2. IFAD currently has a total project portfolio of 442 projects, 190 of which, financed by 193 loans, had already been closed by mid-1996. The designed implementation period of projects in the entire portfolio averages 6.7 years, with a minimum of 4.5 years for programme loans and a maximum of 7.1 years for settlement projects. For the 190 closed projects, the average designed implementation period was 5.7 years, while the actually realized period was 7.6 years, representing a delay of almost two years. On average, IFAD's earlier projects had a designed implementation period shorter than the later ones.

3. During the initial years of its operations, IFAD was heavily dependent on the pipeline of other financial institutions, notably the World Bank, for project development. Up to 1984, the "c" type constituted about half of the projects approved by the Executive Board. As a result, the implementation period of IFAD projects was essentially influenced by those of the cofinanciers, who normally set the implementation period at about five years. This time frame was also established in the conviction, prevalent in those years, that loans could be disbursed at a higher rate in the earlier years of project implementation.

4. The mid-1980s represented an important milestone for IFAD operations. The shift in priorities of other major financial institutions, and the need for sharpening focus on the issue of rural poverty, prompted IFAD to look at new ways of project development, so as to genuinely address the constraints of the rural poor. Both "e" and "f" type projects have come to dominate the project portfolio since 1985. Based on its initial experience in targeting the rural poor, IFAD started to place more emphasis on process-based interventions such as grass-roots capacity-building and beneficiary participation. These interventions, by definition, entailed longer implementation periods. Parallel to the above-mentioned development, the macro-economic and sectoral environment for implementing rural poverty alleviation projects in borrowing countries, particularly the poorest ones, gradually deteriorated. This had a negative impact on the performance of externally-financed agricultural development projects as a whole. The cumulative effect of these circumstances led to a gradual expansion of the project implementation period to 7-8 years.

### Extension of Loan Closing Dates and the Consequences

5. Out of the 190 closed projects mentioned above, 154 projects financed by 157 loans experienced extension of loan closing dates, ranging from one to six times. The overall results have been mixed: 17 loans that had low or moderate disbursement at the original closing date made remarkable and continuous progress during the extension period; 22 loans, although they had been granted many extensions (3-6 times), obviously failed to achieve the targets expected at the time of approving the various extensions. For the remaining loans, 71 were promptly closed after 1-2 extensions, either by reaching the expected physical and/or disbursement targets or in the anticipation that expected targets could never be efficiently and sustainably achieved; the other 47 loans managed to reach a relatively high disbursement rate after significant time overruns resulted from more extensions (3-6 times).

6. Extension of loan closing dates, in cases of delays in implementation, is not always avoidable. Past experience reveals that, when well programmed and implemented, projects under extension of loan closing dates can yield very positive effects in terms of reaching the designed objectives and generating the expected, if not stronger, impact on beneficiaries. However, a high incidence and long period of extension tend to have negative effects in the following ways: (a) undermining the overall performance of project portfolio management, reflected in increased portfolio size resulting from more underperforming projects, inadequate forward planning for extension and lack of effective implementation follow-up over the extension period; (b) unnecessarily tying up IFAD's committable resources, which otherwise could be used to support other projects in the same country or other countries; (c) increasing the cost of development activities related to project staff, CI services for additional supervision, incremental workload for IFAD staff, etc.; and (d) possibly encouraging inadequate project design and underperformance.

### Disbursement Performance

7. Variation Among Project Types. The disbursement profile is normally regarded as a major indicator of the lending institution's performance and the borrowing country's capacity in project implementation. IFAD's past analyses indicate that disbursement performance is considerably dependent on the type or nature of a project:

- Conventional credit projects (i.e., projects focusing on provision of credit lines) can have a faster disbursement pace than loans for other types of projects and have the highest possibility of reaching full disbursement within a relatively short period. However, projects aiming at establishing financial services for the rural poor require longer time for implementation, and consequently disburse slowly.
- Livestock projects, if well conceived, can also be disbursed at a fast pace because of the straightforwardness of project structure. On the other hand, projects aimed at natural resource management such as rangeland conservation entail longer implementation periods and slower disbursement pace.
- Agricultural development projects are more complex and difficult to implement than narrowly-focused projects. For rural development projects, the implementation progress may be slowed by the time-consuming process of promoting beneficiary participation. Thus loans for agricultural and rural development may disburse at a slow pace and need a longer period to reach the expected targets.
- For irrigation projects, loan disbursement usually starts slowly because of the time needed for establishing water users' associations, as well as for infrastructure design and tendering. Implementation of irrigation projects may also suffer from underestimated costs and problems associated with delays in land acquisition, etc.
- Loans for research and extension projects are disbursed even more slowly, because considerable time is needed for the training of extension staff, carrying out applied

research, and achieving changes in thought and practices. Sometimes project design tends to underestimate these difficulties.

8. Regional Variation. The variation of disbursement performance between regions is not very significant. On average, the projects in Asia have a slightly faster disbursement pace, followed by Africa, Latin America and the Caribbean, and the Near East and North Africa. Countries with lower absorptive and weaker institutional capacity tend to have a slow disbursement pace.

#### Loan Cancellation

9. Delayed or imperfect project implementation may lead to loan cancellation. During 1993-96, for instance, almost two thirds of the cancelled loans were due to implementation-related factors. These factors included, among others, slow implementation pace, procurement delays, inadequate counterpart funds, and project organizational and management problems. The remaining one third were the result of causes such as civil unrest, natural disaster, devaluation, etc.

#### Factors Affecting the Realization of Designed Project Implementation Periods

10. Delays related to project implementation are the most significant factor causing the invalidity of designed project implementation periods. Implementation delays can be caused by two groups of factors: (a) macro-level factors: political instability and a poor security situation; impact of structural adjustment and macro-economic imbalance, such as arrears and lack of counterpart funds; lengthy process of legislative approval; shift in government priorities; poor inter-agency coordination; and delays in concluding cofinancing arrangements; and (b) project-level factors: poor project management and operations; late involvement of project managers in the project development cycle; high turnover of project staff; and over-optimistic and/or complex design without adequate appreciation of the local institutional capacity and the implementation pace of project activities. In addition, the start-up time also has a bearing on the duration of this period, because there is always an interval between loan signing and the actual start-up of implementation to allow for fulfilment of conditions for loan effectiveness. Such time lags have a negative impact on the completion of project implementation within the originally expected time frame, particularly among the poorer borrowing countries where the capacity for pre-financing implementation is generally limited.

#### Past Efforts to Improve Project Quality

11. New Project Cycle. The re-engineered project development cycle was introduced on a pilot basis in late 1995. The new cycle builds on the positive features of the previous one by adding the flexibility to facilitate higher quality operations in the field, while simultaneously addressing weaknesses in the previous process. It highlights, among other measures, the importance of promoting local ownership of projects with a view to ensuring adequate project performance. Although the effect of positive changes will take time to realize fully, some initial signs of improvement are already in sight.

12. Better Correlation Between Design and Implementation. Greater attention has been paid to areas where improvements could be made. Some of the conditions traditionally stipulated for loan effectiveness are now dealt with during loan negotiations. The Special Operations Facility, which was initially introduced under the Special Programme for Sub-Saharan African Countries Affected by Drought and Desertification, continues to be used as a tool to ensure smoother project start-up. Efforts have been made to involve national staff in the process of project formulation to the extent possible.

13. Supervision and Monitoring. IFAD has further strengthened its collaboration and interaction with CIs, so that the quality of supervision could be improved and, where necessary, follow-up actions of implementation support could be initiated in a timely and appropriate manner. At the same time, Periodic Loan Portfolio Review (PLPR) has been used as an essential instrument for monitoring the performance of projects, particularly problem ones, which usually involve the issue of the implementation period and extension of the loan closing date. In this regard, the deployment of the Project Portfolio Management System (PPMS), as announced by the President on 24 January 1997, represents a major IFAD effort in search of effective management tools for monitoring and improving project implementation.

### III. CONCLUDING REMARKS

#### Project Implementation Period

14. It has been conventional wisdom that the project implementation period should refer to the actual and uninterrupted time frame for the physical implementation of designed project activities. The time needed for actions leading to the start of implementation should preferably not be counted as part of the implementation period. While the establishment of a time frame for project implementation is quite straightforward, the realization of the designed period can be undermined by various factors. These include, for instance, over-optimistic design, delayed start-up, and slowed implementation resulting from various difficulties. In this regard, IFAD-type projects may encounter more difficulties than general agricultural projects, due to IFAD's emphasis on innovation, targeting and beneficiary participation, as well as to the local conditions of the project areas. IFAD's project implementation period should be defined realistically, giving due consideration to the various factors that may have an important bearing on achieving project targets within the designed time frame.

15. The experience of IFAD and other financial institutions shows that neither a shorter nor longer implementation period is demonstrably right or wrong. The yardstick should be whether the designed project targets can be smoothly achieved in the established period, while simultaneously demonstrating IFAD's efficiency and effectiveness in carrying out its operations. The latter aspect is of particular relevance to the reality of IFAD, because its role and significance in world rural poverty alleviation largely depend on the "design and implementation of innovative, cost-effective and replicable programmes with sustainable impact" as affirmed in IFAD's Vision.

16. Improvements can obviously be made in current IFAD practice in defining the project implementation period. It is important to ensure realistic design and better-quality implementation, so that designed project targets can be achieved within the set time frame. There is a need for developing projects that are compatible with local conditions and the local institutional capacity, in particular, so as to enhance the 'implementability' of designed activities. Smoother project start-up and implementation are also likely to be realized by closer and more proactive interaction with government authorities, possibly through exploring alternative solutions to the various delays. In addition, it appears desirable that the project implementation period begin at the time of loan effectiveness, because this date officially signifies the start of availability to the project of IFAD financing.

#### Extension of Loan Closing Dates

17. Extension of loan closing dates is often the result of delays in project implementation. Past experience demonstrates that the outcome of extension is largely dependent on the quality of forward planning for the extension period and the level of local commitment to continued project implementation. Successful implementation of the plans for extension can enhance the access of the rural poor to project benefits. However, improvement is needed in the application of the current policy on extension of loan closing dates. It is preferable that such extensions should be subject to explicit and quantifiable criteria, based on realistic planning.

#### Loan Cancellation

18. Loan cancellation policy is closely interrelated with that for the extension of loan closing dates. Past experience indicates that loan cancellation appears to be the preferable option where a project has been constantly underperforming as a result of either macro-level or project-level factors - whether extension has been made or not. Prompt loan cancellation, partial or full, enables IFAD to free funds that cannot be used in a sustainable manner, and that it will otherwise be obligated to keep in liquid form.