

MANAGEMENT RESPONSE TO THE ANNUAL REPORT ON 2006 PORTFOLIO PERFORMANCE

On 19 September 2007, the Director General, Operations Evaluation Department (OED), received the following response from the Managing Director General on behalf of Management:

I. General Comments

1. The Annual Report on 2006 Portfolio Performance (the Report) provides a helpful overview of ADB's operations. We agree with the findings that portfolio performance has improved in several key respects in the recent past. We also appreciate OED's helpful suggestions to improve portfolio management further, so that these improvements are sustainable.

2. In particular, there has been a welcome improvement in disbursements from 2004 to 2006, by 25% (year-on-year average) for the loan portfolio as a whole. The executive summary of the Report attributes this better performance only to the increased share of program loans in the portfolio, but the body of the Report makes clear that this is only part of the story. Disbursements in project/sector loans (excluding program loans) have recorded average annual increases of 18% over the same period. We are working hard to maintain this recent pick-up in 2007 and for future years.

3. We also note that OED has evaluated as satisfactory the implementation of Management's *2005 Action Plan to Improve Loan and Technical Assistance Portfolio Performance* in response to OED's *2004 Annual Report on Loan and Technical Assistance Portfolio Performance*.

4. The structure and arrangement of the Report has become less descriptive and more analytical in the last 2 years, and we support this trend away from an accumulation of data towards a focus on issues. The inclusion of a portfolio theme (for this year the project/program performance report [PPR] system) is also helpful, although we suggest that, for future reports, OED should discuss the theme with other departments at an earlier stage, and certainly before the draft report is prepared. Nevertheless, we appreciate the constructive and consultative approach taken by OED in meeting with and listening to other departments before finalizing the Report. Our specific comments below are structured around the four key recommendations.

II. Specific Comments

5. **PPR System.** We fully agree with the need to upgrade and enhance the PPR system. We agree with much of the Report's analysis of the shortcomings of the current system, although the Report under-emphasizes the constraints imposed by the currently available information systems. As noted in the Report, the current PPR system is being comprehensively reviewed as part of the ADB-wide Project Processing and Portfolio Management (P3M) Project, which is already under way. P3M will replace PPR, the technical assistance performance report system, and other fragmented and poorly integrated legacy systems with enhanced, consistent, up-to-date, and user-friendly results-reporting at country, sector, and project level. P3M will include a thorough business process review and updating of Project Administration Instructions so that a modernized PPR system is an integral part of ADB's business processes for project administration.

6. The P3M Working Group (on which OED is represented) will take into consideration the useful suggestions in the Report to revamp the PPR system. At this point in the P3M process, it would be premature to reach conclusions on all of these suggestions. For example, Management is not yet convinced of the merit of the Report's recommendation for an index in the PPR to link the number of reported problems to the number of actions taken to resolve them. The key issue is the effectiveness of the remedial actions, rather than the number of actions taken. We accept the recommendation that the PPR system should be simplified by adopting relatively few tracking and monitoring indicators. More generally, Management also supports a thorough overhaul of the PPR system, which is why P3M is currently a very high priority exercise.

7. **Measure of Portfolio Health.** Quality of information and timeliness in PPR updates require frequent interaction with governments and executing agencies (EAs). Further project delegation to resident missions (RMs) and fielding regular project administration missions are resource-intensive. Management has committed under the *Work Program and Budget Framework 2008-2010* to further delegate project administration to RMs with a broad target of 43% of loan portfolio delegated to RMs by 2010 compared to 39% as of end 2006. Given local knowledge and proximity of RMs to developing member countries, we believe that this further delegation to RMs will bring about better quality of information and timeliness in PPR updates. The Strategy and Policy Department is currently undertaking a review of RM operations, which will include an assessment of the extent of sustainable delegation in project administration.

8. The Report notes that PPRs currently serve a dual function—as an early-warning tool for identifying and addressing projects/programs “at risk” and also as a measure of portfolio performance. In our view, the Report's clear-cut distinction between the PPR's two functions as a “management tool to steer the implementation process” and as a gauge of the “longer term state of health of the portfolio” is not particularly helpful; generally, these are two sides of the same coin. Management will consider during the P3M process the Report's recommendation that an alternate measure of portfolio health should be developed and PPR should be used only as an early warning device to help improve portfolio management. We regard this recommendation as a helpful input to the P3M process, but consider that it would be premature to take a final view at this stage.

9. **Design and Monitoring Frameworks.** ADB is committed to increase development effectiveness by embracing Managing for Development Results (MfDR). The design and monitoring framework (DMF) is the tool to ensure result-focused project design and management. Underlying MfDR and the DMF is a paradigm shift from monitoring inputs to performance management of outcomes and from preparing projects for developing member countries to jointly developing realistic projects and by doing so creating ownership management. This paradigm shift is far from completed in ADB and it is not surprising that the use of the tools—problem tree analysis and the DMF—require further improvement. Nevertheless, very substantial progress has been made in recent years.

10. The results of the most recently completed OED assessments (2000–2005) showed a steady improvement in the quality of DMFs for both loans and technical assistance (TA), albeit from unsatisfactory starting-points. As a comparable OED assessment of DMFs for loans and TAs approved in 2006 has not yet been completed, we would be reluctant to propose a new action plan for DMFs at this point. However, we accept the Report's recommendation that the Project Performance Management System Task Force should undertake a stock-taking of progress made and remaining issues.

This stock-taking should include consideration of some of the deficiencies in DMFs identified in the Report. The Task Force will also work on establishing closer linkages between DMFs and country partnership strategies (formerly country strategies and programs), through a more rigorous sector-level monitoring or outcome and impact indicators, along the lines of the work being carried out by the South Asia Department.

11. **Implementation Delays.** We agree that delays in the implementation of loans, TAs, and grant projects continue to be a problem. Start-up delays from loan approval to loan signing and finally to loan effectiveness averaged about 17 months over the last 5 years compared to average implementation delays at about 18 months over the same period. Reducing start-up delays would significantly reduce the average implementation period. Although loan signing and subsequently making the loan effective is sometimes outside the control of the EA, proactive advance contracting actions would often compensate for some of these delays. These would require the EA to have the implementation capacity to undertake advance actions. ADB's recent increased focus on project readiness filters, including procurement capacity assessments and preparation of procurement plans during project processing, will reduce implementation delays over time.

12. We agree that implementation schedules for new projects should be realistic and should be carefully evaluated by both ADB and the borrower to reflect implementation experience. In some cases, project extensions become necessary when unanticipated problems arise during implementation. Nevertheless, rigorous upfront screening of proposed implementation schedules, together with the enhanced use of project readiness filters and advanced procurement planning requirements, will lead to improvements.