

ASIAN DEVELOPMENT BANK

R-Paper

**COOPERATION WITH JAPAN
JAPAN FUND FOR POVERTY REDUCTION**

April 2000

ABBREVIATIONS

DMC	-	Developing Member Country
JFPR	-	Japan Fund for Poverty Reduction
SDF	-	Social Development Fund

NOTE

In this report, "\$" refers to US dollars and ¥ refers to Japanese yen.

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I. INTRODUCTION

1. Asia has developed over the last three decades in a way that has been referred to as a miracle. This benefited many poor people and reduced the extent of poverty significantly in many countries. But the number of poor people has not been decreasing fast enough. There are still some 900 million people, nearly two-thirds of the world's poor living in Asia. The adverse impact of the recent financial crisis that initially hit the poor in East and Southeast Asia, and then spread to other parts of the Asian and Pacific Region, has not only slowed the pace of poverty reduction, but also resulted in a considerable increase in the number of the poor.

2. In 1999, as a part of a plan to assist the crisis-affected countries in Asia, the Government of Japan (the Government) supported the Asian Currency Crisis Support Facility administered by the Asian Development Bank (ADB). Economic recovery has begun in some countries in the Region. But it will take quite some time before the fruits of economic recovery reach those people who are most severely hit by the financial crisis and socially vulnerable, and still increasing number of poor people in the Region need urgent assistance.

3. ADB has always had a prior concern to reduce poverty in the Region and has played an important role in helping to reduce poverty. But poverty persists, Asia remains the center of the world's concern for poverty reduction, and this has prompted ADB to adopt poverty reduction as its overarching goal. To achieve this goal, ADB prepared a new *Poverty Reduction Strategy*¹ that was unanimously approved by the Board of Directors on 9 November 1999. The strategy is based on three pillars: promoting pro-poor growth, social development, and good governance.

4. ADB will reorient projects so they have more impact on poverty reduction, investing more in essential services for the poor, and especially for vulnerable groups who were most severely hit by the financial crisis, including women and children. Future projects will be designed to either accelerate pro-poor growth or to focus directly on reducing poverty. All these new initiatives, which are aimed at addressing the most urgent task of reducing poverty, will require swift implementation with innovative approaches.

5. The Government, in recognition that fighting poverty in the Region that has been affected by the financial crisis, is an urgent task of ADB, is prepared to make available a contribution of 10 billion Japanese yen (approximately US\$90 million) for the Japan Fund for Poverty Reduction (JFPR) in the year 2000 to ADB. This contribution is viewed by the Government as both urgent and limited in duration. The contribution will finance, on a grant basis, activities that specifically target the poor.

6. This paper outlines the proposed cooperation arrangements between the Government and ADB concerning the initial contribution of ¥10 billion and any further contribution by the Government to the JFPR.

II. OBJECTIVES AND SCOPE

A. Objectives

7. The JFPR will support innovative poverty reduction and related social development activities that can add substantive value to ADB financed projects.² ADB Developing Member

¹ R179-99, *The Poverty Reduction Strategy of the Asian Development Bank*, October 1999.

² ADB financed projects include program loans, sector loans, and project loans.

Countries (DMCs) that have been adversely affected, either directly or indirectly, by the recent financial crisis will be eligible for the JFPR. The JFPR will have the following objectives:

- (i) Support well-targeted poverty reduction and social development activities that have a direct impact on the poor and on socially or economically excluded or vulnerable groups,
- (ii) Stimulate the self-help capacities of the poor,
- (iii) Stimulate widespread stakeholder participation at the community level, and
- (iv) Provide a systematic impact on DMCs' operations and approaches towards sustainable poverty reduction.

8. The JFPR, because of grant financing and the range of activities it supports, will significantly add to the variety and effectiveness of the arsenal available to ADB for addressing poverty reduction concerns in DMCs.

9. To maximize the impact on poverty reduction, JFPR financed activities will be compatible with and complementary to country operational strategies, partnership agreements, and country assistance plans.

B. Scope

10. The JFPR will finance activities which are aimed directly at poverty reduction, and provide innovative and demonstrative impacts on poverty reduction. JFPR financed activities should have strong relation to and enhance effectiveness of ADB financed projects. Typical types of activities to be covered will be as follows.

1. Provision of Basic Economic and Social Services

11. The JFPR could finance small-scale basic economic and social services to the poor, including community level water supply and sanitation, small clinics, local product market facilities, skill training centers, and so on. Pilot-testing type of activities, which could then be replicated on large scale future ADF financed projects, will be included. Innovative and demonstrative approaches for basic economic and social services provided by community initiatives would be given priority.

2. Supporting Social Development Funds

12. The JFPR could also support social development fund (SDF) activities. SDFs are innovative instruments that channel funding to small-scale projects targeted to benefit the poor and communities that are otherwise excluded from access to jobs and essential social and economic infrastructure. Activities supported by JFPR financed SDFs could include community level infrastructure, such as schools, clinics, and water supply and sanitation; and targeted programs for child nutrition, reproductive health, skill training, microfinance, which add great value to poverty reduction in ADB financed projects.

3. Supporting NGOs' Activities for Poverty Reduction and Social Development

13. The JFPR could finance nongovernment organization (NGO) activities that support poverty reduction and social development. NGOs are important agents supporting change and development in most DMCs. These organizations can assist processing in a participatory manner, facilitating community involvement in project implementation, and capacity building at the grassroots level. NGOs can also play an important role in monitoring project progress and in increasing the accountability of public sector agencies. However, NGOs often lack the resources and/or technical capacity needed to perform all these tasks effectively. To broaden impact and enhance various development finance schemes, JFPR support for NGOs would be linked to ADB financed projects.

4. Project Supporting Activities:

14. Other possible areas of JFPR assistance are in capacity building for local government, and for community-based organizations. The JFPR could also provide support to local NGOs for the purpose of design, implementation, monitoring, and evaluation; and the testing of pilot activities in conjunction with ADB financed projects. Activities that are especially innovative and demonstrative would likely be prioritized. These activities would differ from technical assistance financed by other sources in that they will specifically target the poor, and they could be previously untested.

15. Examples of activities that might be considered for JFPR financing are presented in Appendix 1.

16. To make this grant scheme more effective, outcomes of activities should be monitored and the results should be fed back to DMCs' poverty reduction operations. Monitoring and evaluation methods of JFPR contributed activity's impact on poverty reduction should be well designed for each activity.

C. Executing Agency

17. JFPR executing agencies will, in principle, be DMC central and local governments and public institutions. Expenditures arising from JFPR funded activities will be paid in accordance with ADB's standard procedure for disbursements. Although central and local governments and public institutions are expected to be the executing agencies, activities to be financed by the JFPR will likely be managed and maintained by communities. Active participation of communities in activity design, implementation, monitoring, and evaluation is essential to the success of JFPR financed activities.

D. Project Cost

18. Given the extensive demand for activities and investments in support of poverty reduction, JFPR financed activities are likely to be spread throughout the Region. As activities to be financed by the JFPR will not be stand-alone projects but will enhance ADB financed projects, JFPR financed activities are likely to be relatively small compared to ADB financed projects.

19. Beneficiary ownership and associated commitment is essential to the successful outcome of JFPR activities. However, as the scheme specifically targets the poor, any

beneficiary cost sharing is expected to be limited, and would in most cases be in the form of in-kind contributions such as locally available materials and labor. In addition, as one of the salient features of the grant scheme is its intended financing of innovative and pilot projects, it would be quite difficult to identify an appropriate cost sharing level prior to the implementation of the JFPR. Therefore, the cost sharing level of individual activities will be determined on a case-by-case basis.

E. Coordination with Civil Society

20. The poverty reduction activities to be financed by the JFPR will be spread all over the region and over a variety of sectors and sub-sectors. Input from civil society will be essential for the effective implementation of this scheme. ADB will make the necessary efforts to obtain input and feedback from civil society for design, implementation, and evaluation of each activity.

III. IMPLEMENTATION ARRANGEMENTS

21. As an administrator of the JFPR, ADB will ensure that all applicable ADB policies would govern each JFPR financed activity.

A. Processing Procedures

22. Activities will be prepared and proposed by relevant operational and other departments in cooperation with beneficiary communities, and NGOs or other organizations as relevant. Programs Departments including resident missions will coordinate the no objection and processing of each proposal with DMC governments. Departments/Offices concerned will forward proposals to the Strategy and Policy Department, Poverty Reduction Unit (PRU) for consideration and advice. Upon clearance by PRU, Departments/Offices concerned will forward the proposals to the Office of Co-Financing Operations (OCO) for submission to the Government for approval. After Government approval, the proposals will then be forwarded through the relevant operational Vice President to the President for approval or for Board consideration.

23. Board approval for the proposed activity will be required for all activities for which JFPR financing exceeds \$1.0 million, while the President will be authorized to approve all activities for which JFPR financing is \$1.0 million or below. All proposed activities approved by the President will be circulated to the Board for information. Among other considerations, the Board will review likely impact of JFPR financing on ADB financed projects.

24. Following approval of the proposed activity, ADB, on behalf of the Government, will enter into a JFPR assistance letter of agreement with the executing agency to channel such portion of the proceeds of the JFPR as shall be required to carry out the approved activity.

25. It is expected that the World Bank will operate a similar fund, financed by the Government.³ Coordination between ADB and the World Bank with respect to each such fund will be carried out.

³ The budget of the Government for fiscal year 2000 also includes similar contribution to the World Bank.

B. Procurement

26. ADB will review and approve all relevant actions undertaken by executing agencies associated with the JFPR (i.e., recruitment of consultants, procurement of goods and services, and disbursement) in accordance with established procedures. In cases where ADB itself recruit consultants, all relevant procedures governing such recruitment will be followed.

27. The recruitment of consultants will also be carried out in accordance with ADB's *Guidelines on the Use of Consultants* as amended from time to time. Procurement of goods and services will also be carried out in accordance with ADB's *Guidelines for Procurement* as amended from time to time.

C. Monitoring and Evaluation

28. ADB will monitor and evaluate JFPR financed activities in the same manner as all other ADB financed projects and in accordance with established ADB procedures.

29. ADB will prepare an annual report on the evaluation of activities financed by the JFPR that will be submitted to the Government.

IV. JFPR ADMINISTRATION ARRANGEMENTS

A. Contribution and Bank Account

30. The proposed contribution of ¥10 billion will be made available to ADB upon the signing of the Arrangement Establishing the Japan Poverty Reduction Fund (the Arrangement). The Arrangement is in Appendix 2. At its discretion, the Government may provide additional resources to the JFPR. The Government will deposit its initial contribution (and any successive contributions) to the JFPR into an account with the Bank of Japan in the name of ADB. Interest earned on such amount will be used for the purpose of JFPR.

B. Administration Cost

31. The JFPR would be administered by ADB. For administering the JFPR, ADB may use part of the JFPR (together with any interest earned thereon) to cover the direct and identifiable costs⁴ incurred in the administration of the JFPR including monitoring and evaluation.

C. Records and Accounts

32. ADB will maintain records and accounts in accordance with its normal procedures to show expenditures financed by the JFPR. ADB will arrange to provide the Government with periodic reports on the utilization of the JFPR and the activities financed by the JFPR. ADB will maintain records and accounts of the JFPR, and such records and accounts will be audited annually by independent auditors.

⁴ A new service charge structure proposed by R68-00 *Review of Service Charges for the Administration of Grant Cofinancing from Bilateral Sources* was approved on 7 March 2000. However, JFPR financed activities have different characteristics from the modalities specified in the review, i.e., a channel financing agreement and letter of agreement that deal with stand-alone or attached technical assistance and components of loan projects. Accordingly, the new service charge structure proposed in the review will not apply to JFPR.

D. Termination and Residual Funds

33. If and when the purpose of the JFPR is considered to have been fulfilled, and the arrangements of the JFPR terminate, the use of any residual funds including investment income of such funds will be determined in consultation between the Government and ADB.

V. CONCLUSION

34. The proposed Japan Fund for Poverty Reduction will support poverty reduction and social development activities in DMCs. The JFPR will add significantly to the effectiveness of ADB projects and programs and the implementation of ADB's Poverty Reduction Strategy.

VI. RECOMMENDATION

35. It is recommended that the Board approve (i) the acceptance by ADB of the proposed fund, to be called Japan Fund for Poverty Reduction, as a new trust fund; and (ii) the administration of the Fund in accordance with the provisions set forth in this paper and in the letter from the Government of Japan to the President of ADB appended hereto.

APPENDIXES

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EXAMPLES OF POTENTIAL ACTIVITIES

A. Provision of Basic Economic and Social Services

1. **Basic Education.** The Project, Basic Education (Girls) Project, in Lao People's Democratic Republic, will help expand access and improve retention by (i) providing educational facilities in primary education in 50 districts, and strengthen capacities at the central and provincial levels to plan, manage, and implement school construction and school development programs; and (ii) promoting community participation in school management to increase the enrollment and retention of children, particularly girls, in primary schools. The Japan Fund for Poverty Reduction (JFPR) could support the project by providing commuting facilities, water supply and sanitation facilities, and basic healthcare equipment for each school.

2. **Agriculture and Rural Development.** A proposed ADB project in southern Philippines will finance labor-intensive upgrading of farm to market roads, communal irrigation, and drinking water in poor municipalities to increase the income of small farmers and reach food security in the country. The project is demand driven and local government led and uses for monitoring and evaluation a creative cooperation with NGOs. The farm to market roads open up agricultural potential areas in remote and poor villages mostly in the uplands of a municipality. However, the project does not provide livelihood and sustainable income generation activities for poor households outside of agriculture. The JFPR could provide this additionality, and, thus make with a distinguished new component, a pro poor investment project, such as local product market facilities, specifically targeted towards the providing new income means for the poor.

B. Supporting Social Development Funds

3. **Basic Skills Training.** This project in Cambodia aims to assist in developing skills training programs for the growing service industry and for the delivery of basic health services, and to equip groups of disadvantaged and displaced people with income-generating skills. Since training was to be provided in actual production enterprises, a National Training Fund was created to reimburse these enterprises. A JFPR matching grant contribution to the training fund could greatly accelerate its utilization. It is especially worth noting that in the women's sewing and embroidery training program, the buildings and machines procured under the loan were little used because of a lack of consumables such as thread and cloth. A small grant of less than \$100 per training center per annum could dramatically increase the effectiveness of the program.

4. **Skills Development and Small Enterprise Fund.** In Papua New Guinea, ADB is supporting a project that improves the income earning opportunities of the un- and underemployed through skills training, jointly financed by the government, NGOs, private training institutes, and the beneficiaries. A Skills Development Small Enterprise Fund is set up the interests of which is used to finance on a sustainable basis training in three pilot projects. A grant contribution from the JFPR could provide trainees supporting programs and other incentives for targeting the poor.

5. **Sanitation, Public Health and Environment Improvement.** In Kiribati, an ADB financed project aims at improving the quality and availability of safe drinking water, rehabilitate and expand sewerage and sanitation systems and promote hygiene and sanitation through better solid waste management. One feature of this project, which would be specifically useful for JFPR contribution, is the creation, through an NGO network, of a fund to help households building their own dry-pit sealed toilets to protect the water lens from being polluted through leakage. Another component, where JFPR support would make a difference is the promotion of hygiene campaigns in the neighborhood through NGOs.

C. Supporting NGOs' Activities for Poverty Reduction and Social Development

6. **Community and Local Government Development.** The ADB is currently supporting a project with local governments and communities in Indonesia. Local governments and communities will identify and implement small-scale infrastructure projects using labor intensive techniques to generate employment opportunities and expand access of the poor to economic and social services. The participation of civil society is critical for the success of the project. The JFPR could support NGO activities in the project's 35 to 50 districts. This would promote (i) monitoring of individual sub-projects by the public, (ii) dissemination of information on local development activities and issues, and (iii) knowledge of conflict resolution, which has become increasingly important as Indonesia moves to a more open and democratic system of governance.

D. Project Supporting Activities:

7. **Community-Based Infrastructure Services.** A proposed ADB project in the Kyrgyz Republic covers elected local governments in the southern part of the country, where about 60 percent of residents are poor. The project will provide basic infrastructure services, such as (i) safe, adequate, and reliable piped water supply services; (ii) sanitation facilities, and (iii) flood control, drainage facilities, and improvement of local roads. In addition, the project will improve health and hygiene education, water quality surveillance, and facilitate greater local government responsibility for basic social services. The JFPR could directly support the project through financing capacity building of 600 village level local governments to better operation and maintain the basic infrastructure services provided by the Project.

DRAFT ARRANGEMENT

_____2000

Mr. Tadao Chino
President
Asian Development Bank

Dear Mr. President:

I have the honor to refer to the discussions between the Government of Japan (the Government) and the Asian Development Bank (ADB) with regard to cooperation between them in the process of promoting poverty reduction in developing member countries (DMCs) of ADB.

Majority of the world's poor live in Asia, and the negative impact of the recent financial crisis that initially hit the poor in East and Southeast Asia, and then spread to other parts of the Asian and Pacific Region, caused a worsening of poverty in the Region. In 1999, as part of a plan to assist the crisis-affected countries in Asia, the Government supported the Asian Currency Crisis Support Facility (ACCSF), which is administered by ADB. Economic recovery has begun in some crisis-affected countries. But it will take quite some time before the fruits of economic recovery reach those people who are most severely hit by the financial crisis and socially vulnerable, and still increasing number of poor people in the Region need urgent assistance.

In this connection, I have the honor to inform you that the Government intends to make available to ADB funds in the amount of ten billion yen (¥10 billion) on a grant basis during the Government's fiscal year 2000, for the financing of activities that specifically target the poor in Asia. Concerning the provision of the Japan Fund for Poverty Reduction (the Fund), I have the honor to propose the following arrangements:

1. The Government will appoint ADB as Administrator of the Fund. The appointment will come into effect upon the entry into force of these proposed arrangements. The Government will provide, in accordance with the budget and relevant laws and regulations of Japan, the above-mentioned grant funds to ADB in its capacity as Administrator.

2. The Fund will be made available under the following terms and conditions:

(1) The objective of the Fund is to support innovative poverty reduction and social development activities that can add substantive value to ADB-financed projects. DMCs of ADB that have been adversely affected, directly or indirectly, by the recent financial crisis will be eligible for the Fund. Accordingly, the Fund will be utilized for the following purposes:

(a) support well-targeted poverty reduction and social development activities that have a direct impact on the poor and on socially or economically excluded or vulnerable groups;

- (b) stimulate self-help capacity of the poor and broad stakeholder participation at community level; and
- (c) provide a systematic impact on operations and approaches of the DMCs towards sustainable poverty reduction.

(2) Within the general objective, the Fund will finance activities, which (a) are aimed directly at poverty reduction; (b) provide innovative and demonstrable impacts on poverty reduction; and (c) have strong relation to and enhance the effectiveness of ADB financed projects. Typical types of activities to be covered will be as follows:

- (a) provision of basic economic and social services to the poor, including pilot-testing type of activities, such as community level water supply and sanitation, small clinics, local product market facilities, and skills training centers;
- (b) supporting social development funds that channel funding to small-scale programs such as child nutrition, reproductive health, skill training, and microfinance, which are targeted to benefit the poor and communities that are otherwise excluded from access to jobs and essential services;
- (c) supporting non-government organization (NGO) activities for poverty reduction and social development, through assisting NGOs in processing projects in a participatory manner, facilitating community involvement in project implementation, capacity building at the grassroots level, and monitoring project progress; and
- (d) capacity building for local government, community-based organizations, and local NGOs for the purpose of designing, implementing, monitoring and evaluating projects and testing of pilot activities in conjunction with ADB financed projects.

(3) In the implementation of the Fund, ADB will monitor the outcomes of each activity covered by the Fund so that the results are fed back to DMCs' poverty reduction operations. Monitoring and evaluation of each activity's impact on poverty reduction will be suitably designed by ADB.

(4) Recipients of the Fund will in principle be central and local governments, as well as public sector institutions of DMCs. Expenditures arising from activities financed under the Fund will be paid in accordance with ADB's standard procedures for disbursements. Activities financed by the Fund are expected to be managed and maintained by communities, and active participation of communities in design, implementation, monitoring, and evaluation is essential.

(5) As ADB identifies specific activities for financing under the Fund, ADB will, at such intervals as agreed with the Government, provide to the Government for approval a list of such activities, their outlines, the amounts of the proposed assistance, and the proposed items of expenditure to be financed.

(6) As poverty reduction activities financed by the Fund will be spread all over the Region and over various sectors, input from civil society is needed for effective implementation. ADB will make efforts to obtain input and feedback from civil society for activity design, implementation, and evaluation.

(7) As the World Bank will operate a similar fund, financed by the Government, there will be close coordination between ADB and the World Bank with respect to each such fund.

(8) The Fund will be used to finance foreign exchange or local currency expenditures for goods, services and consultants which will be procured or supplied from ADB member countries, in accordance with procedures and practices consistent with the applicable ADB guidelines. ADB will ensure that the procurement of goods and services provided under the activities to be financed under the Fund are carried out in accordance with ADB's *Guidelines for Procurement*, as amended from time to time. ADB will ensure that the consulting services to be financed under the Fund are engaged in accordance with ADB's *Guidelines on the Use of Consultants*, as amended from time to time. The Government shall use reasonable endeavors to make available to ADB information concerning expertise available in Japan, and will assist ADB in the identification of suitable Japanese individuals, firms and institutions to help implement activities financed by the Fund.

(9) ADB will, as Administrator, enter into an agreement or agreements, as appropriate, with the recipient government and/or the concerned executing agency in connection with the provision of individual financial assistance out of the Fund.

(10) ADB will (a) be responsible for the administration of each agreement referred to in paragraph 2(9) above; (b) carry out such administration in accordance with its normal practices and standards and with the same degree of care as it uses in the administration of its own funds and have no further responsibility to the Government in respect thereof; and (c) may enter into such agreements, and do any and all such acts and things, as may be necessary or appropriate to accomplish fully the foregoing.

(11) ADB will be responsible for the appraisal and negotiation with the recipients of the scope and content of the activities referred to in paragraphs 2(1) and 2(2) above.

(12) Supervision and evaluation of the activities to be financed under the Fund will be the responsibility of, and will be carried out by, ADB. ADB will make available to the Government at six-month intervals, beginning six months after the entry into force of these proposed arrangements, a summary of progress on all activities financed by the Fund. ADB will also make available to the Government an annual report on the evaluation of activities financed by the Fund. ADB will invite the Government to participate, at its option, and with the prior consent of the recipient concerned, in the supervision and evaluation missions carried out by ADB.

(13) The Government will make payment of the Fund into an account (the Account) in the name of ADB at the Bank of Japan. An amount of ten billion yen (¥10 billion), for the Government's fiscal year 2000, will be paid promptly after the entry into force of these proposed arrangements.

(14) ADB may invest and reinvest the funds in the Account pending their disbursement to the relevant recipients. ADB will exercise the same care in investing these funds as it does for its own account. Interest earned will be used for the purpose of the Fund.

(15) ADB may use part of the Fund (together with any interest earned thereon) to cover the direct and identifiable costs incurred in the administration of the Fund including monitoring and evaluation.

(16) ADB will (a) maintain separate records and accounts in respect of the funds deposited in and withdrawn from the Account; (b) cause such accounts and records to be audited and certified by external auditors for each fiscal year of ADB that funds remain in the Account; and (c) furnish a copy of the report of such audit to the Government.

3. These arrangements shall remain in force until terminated by either the Government or ADB upon three months prior written notice to the other party. If these arrangements are terminated,

- (1) such termination will not affect any commitment under existing activities and ADB may continue to make withdrawals from the Account in respect of such activities (including withdrawals for related costs of ADB) as if these arrangements had not been so terminated; and
- (2) the use of any residual funds, including investment income of the Fund, will be determined in consultation between the Government and ADB.

4. From time to time, at the request of either party, the Government and ADB will consult with each other on matters arising out of the present arrangements. Moreover, ADB will promptly inform the Government of major changes or developments affecting the activities financed out of the Fund, including, inter alia, amendments to agreements; reallocation of funds; suspension, termination or cancellation of disbursements; and of any event which interferes, or threatens to interfere, with the successful implementation of such activities.

I have further the honor to propose that the present note and your confirmation of the foregoing arrangements shall be regarded as constituting an agreement between the Government and ADB, which will enter into force on the date of your confirmation.

Sincerely yours,

Naoyuki Shinohara
Executive Director for Japan

