

***Economic Analysis
Retrospective 2005***

**Key Findings
and Future Directions**

Economics and Research Department

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ADB

Objectives of Retro 2005

- To promote the use of rigorous economic analysis in CSPs and RRP.
- Three points of departure from previous Retros:
 - Inclusion of CSPs;
 - Introduction of a numerical rating system;
 - Explicit consideration of the concept of binding development constraints.

Why Include CSPs?

- Country-focus, identification of binding constraints to development, and linking such constraints to country strategies and programs are at the heart of ADB's ability to improve quality at entry.

Why Consider Binding Constraints?

- Central to problem diagnosis;
- Critical for establishing ADB's *raison d'être* in a DMC;
- Seamless interface between CSP and RRP.

What are Binding Development Constraints ?

- **Country-specific** conditions and factors—reflecting either *market failures* or *government failures*—that restrict the country from realizing its development potential.
 - At country level, binding constraints can be of a sectoral nature (e.g. poor financial intermediation, inadequate infrastructure, or energy shortages), or a thematic nature (e.g. poor economic management, weak governance, or inadequate institutional capacity).
 - At the sector level, binding constraints can mostly be classified into categories such as limited access to financing, low technological capability, weak policy/regulatory framework, governance issues, or incentive and information problems.

Three issues when interpreting the findings...

- **Documents Reviewed:** limited to the final documents, but actually the culmination of a year-long process of ERD reviews.
- **Root causes for weak economic analysis not investigated:** problems in ETSW and TA studies; failure to distill the findings of ETSW and TA studies; various constraints faced by country teams and project missions; or simply poor presentation.
- **Not a review of whether or not business processes and guidelines are followed.**

Economic Analysis in CSPs: Establishing Rationale

Goal	Objective	Attribute of analysis
CSP		
Establish relevance and responsiveness of ADB operations	To identify development challenges and binding constraints to growth and poverty reduction in a DMC	<ul style="list-style-type: none"> Country diagnosis in terms of economic, thematic, and sector assessments
	To assess the government development plan and implementation capacity in light of the country diagnosis	<ul style="list-style-type: none"> Assessment of government development plan or PRS
	To identify lessons learned—strengths and weaknesses—from ADB’s past performance in assisting the DMC	<ul style="list-style-type: none"> Assessment of ADB’s past performance
	To identify assistance activities of other aid agencies to establish the value-added of ADB operations, promote coordination, and avoid duplication	<ul style="list-style-type: none"> Assessment of donor coordination
	On the basis of the above assessments, to formulate ADB’s assistance strategy and program	<ul style="list-style-type: none"> ADB assistance strategy ADB assistance program

Rating Distribution by Attribute of Economic Analysis - CSPs

Attribute	Number of CSPs rated as				Mean score
	US (1)	PS (2)	GS (3)	FS (4)	
Country assessment	0	5	1	0	2.2
Government development plan	0	5	1	0	2.2
ADB's past performance	0	3	2	1	2.7
Assistance strategy	0	5	0	1	2.3
Assistance program	0	5	0	1	2.3

Main Findings on CSPs: Country Assessment

- Two major weaknesses

- Lack of systematic analysis of **binding constraints** to growth and poverty reduction.
- **Fragmented presentations** of economic, thematic, and sector assessments, making it difficult to tell coherent development stories of the concerned DMCs.

Main Findings on CSPs: Country Assessment - Specific Problems

- **Growth assessments:** the drivers of and binding constraints needs to be clearly identified, and the analysis of macroeconomic policy issues more forward-looking;
- **Poverty assessments:** did not lead to a better understanding of poverty trends, country-specific causes of poverty, constraints to poverty reduction, and income inequality;
- **Sector assessments:** sector constraints not systematically diagnosed.

Main Findings on CSPs: - Government Dev. Plan

- **Soundness of the plan:**
 - assessed, but the weaknesses in country diagnoses raise concerns over whether these assessments were adequately informed.
- **Feasibility of the plan:**
 - Both in terms of financial and institutional capacities, needs improvement

Main Findings on CSPs: - ADB's Past Assistance

- **Sector level experience:**
 - Analysis of lessons learned and problems ADB encountered at the sector level should be strengthened.
- **Development outcomes and impacts:**
 - In assessing the impact of ADB's past assistance, the CSPs mostly focused on lending volumes, numbers of projects, and project performance ratings; not on development outcomes and impacts

Main Findings on CSPs : ADB Strategy

- Lack of clear identification and explanation of the binding development constraints
- No clear demonstration of the linkages between the strategic focus of ADB assistance and binding development constraints
 - Difficult to judge whether the sector and thematic areas selected for ADB intervention were targeting the most urgent needs of the concerned countries

Main Findings on CSPs: ADB Program

- **Sector binding constraints**
 - Not clearly defined, making it difficult to assess economic rationale of proposed interventions.
 - The issue of sequentially relaxing binding constraints was often not highlighted.
- **General approach to the selection of operational instruments and lending modalities**
 - Not sufficiently discussed.
- **Details of planned projects or programs**
 - usually were not clearly spelled out, making assistance programs appear to be disconnected from the pipelines of planned interventions.



Economic Analysis in RRP: Economic Rationale and Viability

Goal	Objective	Attribute of analysis
RRP		
Validate economic rationale of ADB intervention	<ul style="list-style-type: none"> •To diagnose problems and identify constraints in a targeted sector •To establish justification for government intervention •To establish justification for ADB assistance 	Analysis of economic rationale
Assess economic viability of ADB intervention	To conduct economic analysis of project and sector loans	<ul style="list-style-type: none"> • Demand analysis • Alternatives analysis • Cost-benefit analysis • Sustainability analysis • Sensitivity/risk analysis
	To conduct broad economic and policy analysis of program loans	<ul style="list-style-type: none"> • Analysis of government reform plan/capacity • Program design • Determination of loan size • Assessment of benefits & impact of reforms • Risk assessment

Ratings for Project RRPs

Attribute	Number of RRPs rated as				Mean score
	US (1)	PS (2)	GS (3)	FS (4)	
Analysis of economic rationale	2	27	10	0	2.3
Demand analysis	8	15	15	1	2.4
Alternatives analysis	13	17	8	1	2.0
Cost-benefit analysis	2	4	25	8	3.2
Sustainability analysis	5	16	14	4	2.7
Sensitivity & risk analysis	1	18	18	2	2.7

	Analysis of economic Rationale	Demand analysis	Alternatives analysis	Cost-benefit analysis	Sustainability analysis	Sensitivity analysis
Agriculture & Natural Resources	63.6	9.0	9.0	72.7	45.4	45.4
Energy, Water Supply & Sanitation	62.5	50.0	50.0	100.0	50.0	50.0
Transport	61.5	76.9	23.0	92.3	53.9	53.9
Education & Health	28.6	14.3	14.3	71.4	28.6	57.1

Main Findings on Project RRPs

- **Economic Rationale:**
 - Problem diagnosis generally adequate, but justification for public sector intervention missing
 - Some were poor in justifying ADB's involvement in the project and choice of financing modality
- **Demand analysis:**
 - Weakest area, especially for agriculture and social sector projects
- **Alternatives analysis:**
 - Missing for many

Main Findings on Project RRP

- **Cost-benefit analysis:**
 - most satisfactory
- **Sustainability analysis:**
 - inadequate discussions on a project's fiscal implications and the government ability to meet the financial and institutional requirements.
- **Sensitivity and risk analysis:**
 - Mostly looking at scenarios of benefits or costs increasing or decreasing by certain percentages;
 - Very few performed risk analysis.

Ratings for Program Loan RRPs

Attribute	Number of RRPs rated as				Mean score
	US (1)	PS (2)	GS (3)	FS (4)	
Analysis of economic rationale	0	0	6	4	3.5
Government reform plan/capacity	0	2	8	0	2.8
Program design	0	1	4	5	3.4
Determination of loan size	3	2	5	0	2.2
Benefit and impact of reform	0	3	7	0	2.7
Risk assessment	0	1	9	0	2.9

Main Findings on Program Loan RRPs

- **Economic rationale:**
 - Generally adequate except the justification of ADB involvement could be better explained.
- **Government reform program and capacity:**
 - Weak, insufficient discussion
- **Program design:**
 - Discussion generally comprehensive and activities linked with the identified problems.

Main Findings on Program Loan RRPs

- **Determination of loan size:**
 - Weakest part. About half did not provide estimate of adjustment costs.
- **Benefit and impact of reform:**
 - Channels through which the benefits and impacts were to be achieved need to be identified.
- **Risk assessment:**
 - Weak in the discussion of risk mitigation.

Strengthening Quality at Entry: Future Directions

- Diagnostic approach in ETSW;
- Integrate key findings of ETSW in CSP in a coherent manner;
- Use diagnostic findings to critically assess government development plans;
- ADB's strengths and weaknesses determine what it will do and what it will not do;
- CSPs directly targeted at relaxing binding development constraints;
- Ensuring the quality-at-entry requires good economic analysis in CSPs as well as RRP.

ERD's Responses

- Accelerate reorientation of advisory services to early part of operational cycle;
- Pilot country-specific growth diagnostic studies;
- Methodological studies;
- Retrospective reviews;
- Learning programs.

Summary of Meeting with Regional Departments

- Broad support for findings of Retro;
- Partnership between ERD and RDs to pilot-test growth diagnostics;
- Partnership must be demand-driven;
- RDs would collectively determine on their next steps;
- ERD would brief CSP Team Leaders and RRP Mission Leaders of the retro findings.

Key Messages

- Robust ETSW should focus on identifying binding constraints;
- Key ETSW findings should be presented in CSP in an integrated manner;
- CSP should target relaxing constraints;
- CSP should establish rationale for projects;
- RRP should strengthen demand and least-cost analysis.

