

Chapter 2

DIAGNOSTIC QUALITY OF ECONOMIC, THEMATIC, AND SECTOR WORK



2.1 SCOPE OF THE REVIEW

Each CPS paper contained six to eight thematic assessments. In most cases, discussions in the main text were supplemented by a more detailed assessment in an appendix. For the five CPS papers reviewed, about three quarters of the thematic assessments were based on in-depth background studies carried out by ADB as part of CPS preparation. The country team survey

private sector development (PSD), as shown in Table 2. In addition to the main text, the review covers

- (i) two CPS appendixes (LAO and PNG) and five ADO chapters on growth;⁸
- (ii) four CPS appendixes (INO, LAO, UZB, and VIE) and three in-depth background studies (INO, UZB, and VIE) on poverty; and
- (iii) four CPS appendixes and four background studies (LAO, PNG, UZB, and VIE) on PSD.

Table 2. Thematic Assessments—Scope of the Review

Theme	INO	LAO	PNG	UZB	VIE
Growth	<ul style="list-style-type: none"> • CPS main text • ADO chapter 	<ul style="list-style-type: none"> • CPS main text • CPS appendix • ADO chapter 	<ul style="list-style-type: none"> • CPS main text • CPS appendix • ADO chapter 	<ul style="list-style-type: none"> • CPS main text • ADO chapter 	<ul style="list-style-type: none"> • CPS main text • ADO chapter
Poverty	<ul style="list-style-type: none"> • CPS main text • CPS appendix • Background poverty assessment 	<ul style="list-style-type: none"> • CPS main text • CPS appendix 	<ul style="list-style-type: none"> • CPS main text 	<ul style="list-style-type: none"> • CPS main text • CPS appendix • Background poverty assessment 	<ul style="list-style-type: none"> • CPS main text • CPS appendix • Background poverty assessment
Private Sector Development	<ul style="list-style-type: none"> • CPS main text 	<ul style="list-style-type: none"> • CPS main text • CPS appendix • Background private sector assessment 	<ul style="list-style-type: none"> • CPS main text • CPS appendix • Background private sector assessment 	<ul style="list-style-type: none"> • CPS main text • CPS appendix • Background private sector assessment 	<ul style="list-style-type: none"> • CPS main text • CPS appendix • Background private sector assessment

ADO = *Asian Development Outlook*, CPS = country partnership strategy, INO = Indonesia, LAO = Lao People's Democratic Republic, PNG = Papua New Guinea, UZB = Uzbekistan, VIE = Viet Nam

Source: Compiled by the Economics and Research Department.

indicated that when background studies were not carried out, thematic assessments relied mainly on information from other sources, including ETSW within ADB, ETSW by other development agencies, and other research and knowledge products. The review of thematic assessments in *Retro 2006* focuses on three topics—growth, poverty reduction, and

⁸ Because no in-depth background growth assessments were prepared during the CPS processes, ADO growth chapters were reviewed based on the limited evidence that ADO provided supporting information to develop the discussions on growth in the CPS papers. The ADO is prepared for a different audience and purpose, but is being assessed here in terms of its usefulness for preparing a growth assessment for a CPS paper.

The five CPS papers contained 28 sector road maps (Table 3). A typical sector road map consisted of (i) an introduction and background (or summary situation analysis), (ii) key issues and development challenges, (iii) government plans and policies, (iv) ADB's experience in the sector, (v) roles and/or activities of other development partners, (vi) ADB's sector assistance strategy, and (vii) implementation and monitoring. Some road maps also included an assessment of the capacity and approach to managing for development results in the sector, and links with other CPS outcomes.

2.2 GROWTH ASSESSMENTS

A. Assessment Framework

To ascertain the quality of growth assessments, *Retro 2006* follows the analytical framework outlined in *Retro 2005* (Table 4). A sound growth assessment should cover growth performance, growth drivers, macroeconomic management, constraints to growth, and growth outlook. Assessing growth performance involves describing indicators such as overall growth of gross domestic product (GDP) as well as

Table 3. Sector Road Maps—Scope of the Review

	INO	LAO	PNG	UZB	VIE	Total
Agriculture and Natural Resources	▲	▲	–	▲	▲	4
Education	▲	▲	–	▲	▲	4
Health	▲	▲	▲	▲	▲	5
Energy	▲	▲	–	–	▲	3
Transport and Communications	▲	▲	▲	▲	▲	5
Water Supply and Sanitation	▲	▲	–	▲	▲	4
Finance	▲	▲	–	–	▲	3
Total	7	7	2	5	7	28

▲ = present in the paper, – = not present, INO = Indonesia, LAO = Lao People's Democratic Republic, PNG = Papua New Guinea, UZB = Uzbekistan, VIE = Viet Nam

Source: Compiled by the Economics and Research Department.

Previous ADB assessments of quality-at-entry have questioned whether ADB is allocating an inordinately large amount of resources to undertaking country assessments.⁹ The answer to this probably depends on the quality of the assessments. A thematic assessment or sector road map will not be very useful if it does not properly diagnose the problems and does not propose useful interventions that could be integrated into sector and country operations. That is, the resources devoted to ETSW should be evaluated against the usefulness of the results of ETSW in informing ADB's strategy setting and choice of interventions.

⁹ One of the lessons learned from the review of the Nepal results-based CPS is to coordinate better the start date and sequencing of the country poverty analysis and the country assistance and program evaluation. Ideally, these diagnostics will be conducted 12 months prior to the CPS preparatory stage to improve their quality and usefulness and to reduce the need for some thematic assessments to be prepared separately for the CPS (ADB 2006c). ADB's stocktaking report on the results-based process also recommends guaranteeing appropriate resources and time for strengthening sector results orientation while exploring ways of reducing the heavy burden of the required assessments and analyses by maximizing the use of existing studies and assessments (ADB 2006d).

growth rates and shares of major production sectors (agriculture, industry, and services) and of key demand components (consumption, investment, and imports and exports). Growth drivers can be identified through accounting techniques that can decompose a country's growth into contributions by factors of production, demand components, production sectors, or regions (Box 1). Macroeconomic management can be examined by assessing the country's fiscal and monetary policies and indicators such as inflation, money supply, fiscal deficit, government debt, and external payments.

While growth performance and drivers indicate where growth occurred, the identification of the critical or binding constraints to growth is the key to setting the priorities of development strategies and plans. "[Development practitioners today] do not really know what cause economic growth," admitted François Bourguignon, Chief Economist at the World Bank, but "we do have a good sense of what are the main obstacles to growth and what are the conditions without which an economy can't grow" (Naim 2006). Identification and analysis of

Table 4. Framework for Growth Assessment

Topic	Key Question	Assessment Method
Growth Performance	How did the economy perform in recent years?	Describe growth indicators.
Growth Drivers	What were the underlying factors that drove growth?	Decompose growth into contributions by (i) production sectors, (ii) demand components, (iii) regions, and (iv) factors of production.
Macroeconomic Management	How effective was macroeconomic management in supporting growth and maintaining macroeconomic stability?	Discuss fiscal and monetary policies and external payment positions.
Growth Constraints	What are the binding constraints to growth?	Analyze the market and nonmarket failures that constrain growth.
Growth Outlook	What is the growth outlook?	Link the analysis of the identified constraints to the growth outlook and assess the prospect for growth.

Source: Compiled by the Economics and Research Department.

a country’s critical constraints to growth, or more broadly, to development, therefore provide the fundamental basis for operations of a development agency.

A country’s critical constraints to growth are country-specific conditions and factors—reflecting either *market* or *government failures* that restrict the country from realizing its development potential. At

Box 1. Growth Accounting

Growth accounting or decomposition provides a useful way to identify drivers of growth. Growth of gross domestic product (GDP) can be decomposed by factors of production, sources of demand, production sectors, or economic regions. Decomposition by factors of production attempts to decompose GDP growth into contributions by growth of labor, growth of capital, and growth of total factor productivity. This can be carried out by using the following equation:

$$G_Y = (W_K \cdot G_K) + (W_L \cdot G_L) + G_F$$

where G_Y is growth of GDP (or national income), W_K is share of capital income in GDP, G_K is growth rate of capital, W_L is share of labor income in GDP, G_L is growth rate of labor, and G_F is growth rate of total factor productivity. In practice, G_Y , G_K , G_L , W_K , and W_L can be estimated from the national accounts data and other statistical sources, while G_F is calculated as the residual. G_F , also called the Solow residual, is the portion of GDP growth not explained by changes in the standard factors of production, and it is often attributed to technological progress, knowledge spillovers, and efficiency gains due to factors such as policy and institutional reforms. Contributions by labor, capital, and total factor productivity to GDP growth can be expressed in absolute terms (percentage points), or relative terms (as a share to total GDP growth).

Decomposition by sources of demand attempts to decompose GDP growth into contributions by key demand components, including private consumption, private investment, government spending, and net exports, using the following formula:

$$G_Y = (G_C \cdot W_C) + (G_G \cdot W_G) + (G_I \cdot W_I) + (G_{X-M} \cdot W_{X-M})$$

where G_Y is growth rate of GDP, G_C is growth rate of private consumption, W_C is share of private consumption to GDP, G_G is growth rate of government spending, W_G is share of government spending to GDP, G_I is growth rate of private investment, W_I is share of private investment to GDP, G_{X-M} is growth rate of net exports, and W_{X-M} is share of net exports to GDP. All the variables in this formula can be estimated from the national accounts data. Contributions to GDP growth by each component can be expressed in absolute terms (percentage points) or relative terms (as a share to total GDP growth).

Growth can also be decomposed by production sectors or economic regions following the same procedure as for decomposition by sources of demand.

Source: Gillis et al. (1996).

an aggregate level, the constraints can be of a sectoral nature (e.g., poor financial intermediation, inadequate infrastructure, or energy shortages) or a thematic nature (e.g., poor macroeconomic management, weak governance, or inadequate institutional capacity).¹⁰ Analyses of the constraints should therefore be carried out with a conscious search for market and government failures, on which the rationale for public sector interventions and ADB assistance will rest. *Retro 2005* introduced the framework for growth diagnostics, which aims to identify the binding constraints to growth and appeared recently in the development economics literature (Hausmann, Rodrik, and Velasco 2005).

B. Diagnostic Quality of Growth Assessments

Unlike most other thematic assessments, growth assessments were often not based on in-depth background studies by ADB. Among the five CPS papers, no in-depth background study by ADB on growth was identified during the review, and only two—LAO and PNG—provided an appendix on growth assessment.¹¹ In the other three CPS papers, growth was only assessed with a few paragraphs in the main text. All the CPS team leaders indicated that ADB's existing ETSW on growth was inadequate and not comprehensive enough for CPS purposes. As a result, all five CPS papers required additional work on growth assessment, carried out either by staff consultants or by CPS team members. However, whether the CPS teams were able to produce comprehensive and adequate growth assessments within the required CPS preparation schedule cannot be directly observed because none of the additional work was published or cited. A total of 16 studies were cited as references in the growth assessments of the five CPS papers. Only four were produced by ADB, two of which are 2006 ADO chapters cited in the PNG and VIE CPS papers and the other two are evaluation reports by the Operations Evaluation Department (OED). This seems to confirm the perception revealed in the CPS country team survey that ADB's ETSW on economic growth was inadequate.

ADO country chapters provided useful information on growth, but that information is not sufficient for a CPS paper because ADO serves a different purpose; and even that information did not seem to have been fully used in the CPS papers. ADO country chapters provided reviews of performance, sources, and prospects of growth. They also discussed macroeconomic and structural policy issues of importance to accelerating and sustaining growth. In many ADO country chapters, decomposition of GDP growth was also often performed using the growth accounting method. However, the analysis in the chapters normally had a much shorter time horizon than that of a CPS paper. It is neither feasible nor appropriate for ADO country chapters, which have a semiannual frequency, to provide detailed growth diagnostics, which normally require a time horizon of 5–8 years. However, the review found that even such information as drivers and sources of past growth in ADO chapters was not always fully used in many growth assessments of the CPS papers.

Growth trends were generally adequately described, but the pictures of drivers of past growth were less clear. Most CPS papers provided generally adequate descriptions of growth trends, with the discussions often supported by relevant statistical indicators. However, the drivers of past growth were less clear, and growth decomposition was not commonly carried out to quantify the sources of growth. Among the five CPS papers, only the UZB CPS conducted the growth decomposition exercise to identify sources of growth on both supply and demand sides. The INO and VIE CPS papers did not go into detail on the drivers and sources of growth, probably due to the page limit as the two did not provide an appendix on growth. The LAO and PNG CPS papers provided good discussions on the growth of major production sectors, but not on the demand side or on factors of production.

The critical constraints to growth were often highlighted, but not backed up by supporting diagnostics. The review revealed conscious efforts to discuss the binding constraints to growth, but only the UZB discussion was backed up by diagnostics.¹²

¹⁰This definition is adopted from *Retro 2005* (ADB 2006a).

¹¹The PNG CPS paper appended a country economic overview.

¹²As indicated in the initiating paper, the UZB CPS paper applied a diagnostic approach, similar to that outlined in *Retro 2005*, to analyzing the constraints to private-sector-led growth.

The lack of systematic diagnostics often led to a laundry list of constraints to growth with neither supporting evidence nor prioritization. Further, discussions of the constraints to growth were not always in terms of market and/or nonmarket failures. Instead, a number of growth assessments presented short- and medium-term growth prospects of concerned countries, and discussed the risks to these prospects. Some of the risks (e.g., uncertainty over market access and bad investment climate) were related to market or nonmarket failures, which call for public intervention, while others (e.g., world price changes of major trade commodities) were not.

Growth assessment could be better used as a diagnostic tool to guide the formulation of ADB’s CPSs. The review of growth assessments in the main text and appendixes shows that, in many cases, these assessments were either not supported by in-depth background studies or could have made a better use of background studies available at the time of CPS preparation. The assessments presented in the CPS

papers could be improved in a number of areas, including the identification of a country’s critical or binding constraints to growth.

2.3 POVERTY ASSESSMENTS

A. Assessment Framework

A country poverty analysis provides a good starting point for a comprehensive examination of the constraints to and opportunities for poverty reduction in each country. The *Handbook on Poverty and Social Analysis* (ADB 2001a) provides guidance on how to conduct a country poverty analysis. Thus, ADB’s analytical framework for poverty analysis is clearly defined. In reviewing poverty assessments, *Retro 2006* generally follows this framework. Since the focus is on the diagnostic quality of ETSW underpinning CPS papers, *Retro 2006* looks only at poverty profiling, inequality profiling, and analysis of the causes of poverty and constraints to poverty reduction (Table 5).¹³

Table 5. Framework for Poverty Assessments

Topic	Key Question	Assessment Method
Poverty Profiling	<ul style="list-style-type: none"> Who are the poor and how poor are they? 	<ul style="list-style-type: none"> Choose the poverty line. Determine the incidence of income and nonincome poverty. Describe economic, social, and geographic characteristics of the poor. Describe the evolution of poverty and trends in poverty reduction.
Inequality Profiling	<ul style="list-style-type: none"> How are wealth and income distributed? What are the sources of inequality? How has inequality been evolving? 	<ul style="list-style-type: none"> Describe income and nonincome inequality. Decompose inequality by region or social group. Describe the evolution of inequality.
Causes of Poverty and Constraints to Poverty Reduction	<ul style="list-style-type: none"> Why are the poor poor? 	<ul style="list-style-type: none"> Analyze the causes of poverty. Identify the critical or binding constraints to reducing poverty in the market and nonmarket failure framework.

Source: Compiled by the Economics and Research Department.

¹³The CPS guidelines note that careful diagnosis of the development constraints at the national and sector level is essential for selectivity and focus. The guidelines specify that poverty assessments should examine trends in poverty reduction and assess the effectiveness of public policies and how the policies contributed to poverty reduction; analyze the main roots of poverty and major constraints to poverty reduction and Millennium Development Goal achievements; and cover income inequality (ADB 2007a).

Poverty profiling involves choosing a proper poverty line; determining poverty incidence; describing economic, social, and geographic characteristics of the poor; and describing the evolution of poverty. Inequality profiling requires assessing income and nonincome inequalities and discussing the sources and evolution of inequalities. A sound poverty assessment should also examine the causes of poverty, identify critical or binding constraints to poverty reduction, and highlight opportunities for reducing poverty.

B. Diagnostic Quality of Poverty Assessments

Four of the five CPS papers provided poverty assessment appendixes (INO, LAO, UZB, and VIE); three of these were supported by in-depth background poverty studies (INO, UZB, and VIE); see ADB (2006g and 2006h). The PNG CPS had no appendix on poverty. Overall, *Retro 2006* finds that the poverty assessments were more comprehensive than the growth assessments.

Income and nonincome poverty was generally well profiled. Most poverty assessments used well-defined national poverty lines, estimated on the basis of the minimum expenditure to meet the 2,100 calories per day per person requirement adjusted by nonfood expenditure. Some of the assessments also provided poverty incidence estimates using the \$1-a-day international poverty line for cross-country comparison. Both income poverty and nonincome poverty were well profiled, and the INO and VIE CPS papers provided good examples in this regard. In the INO CPS, income poverty was well discussed with poverty incidence benchmarked against the national poverty line. Nonincome poverty was also given adequate attention and analyzed in terms of meeting the Millennium Development Goals. Poverty profiling in the VIE poverty background study went beyond mere enumeration of indicators and discussions of recent trends by presenting more in-depth analysis (e.g., discussing the significance of the growth elasticity of poverty). Income poverty was discussed in terms of threshold consumption, food poverty, poverty line, and poverty incidence. Nonincome poverty was embedded in the discussion of poverty profile (e.g., school enrolment rates and health indicators for poor groups).

The analysis of income inequality, however, was of mixed quality. In some poverty assessments, income inequality was clearly analyzed. A good example was the INO CPS, with the background poverty study presenting and explaining inequality measures such as the Gini coefficient, income share of the poorest 40% and richest 20% of population, poverty gap index, and poverty severity index; how these changed over time; and regional patterns of inequality. For other CPS papers, the issue of income inequality was either not highlighted or inadequately examined. None of the poverty assessments reviewed, including the INO CPS paper, attempted to decompose overall inequality by different sources such as subregions and population subgroups, using decomposable inequality measures (Box 2).

Causes of poverty were discussed in all the poverty assessments, but sometimes they were mixed up with individual or household characteristics of the poor, from which it is difficult to infer policy implications. Causes of poverty broadly fall into three categories: (i) lack of growth and economic opportunities, which is in turn caused by the binding constraints to growth; (ii) inability to participate in the growth process due to lack of human capital and/or other productive assets such as land and credit, or other constraints reflecting market, institutional, or policy failures; and (iii) vulnerabilities due to lack of social safety nets. Among the five CPS papers, the LAO CPS discussed the causes of poverty along this framework in a clear and logical manner. The causes listed and discussed included remoteness and isolation; limited access to land; limited opportunities for broader rural development due to inadequate market access, poor distribution networks, low level of electrification, shadow rural financial markets, and a lack of all-weather roads; limited urban employment opportunities; weak human resources; and lack of social safety nets for coping with shocks. The quality of the analysis in other CPS papers was more varied. In the case of the VIE CPS, for example, the appendix on poverty assessment merely listed the perceived causes of poverty, from some of which (such as lack of land, capital, and labor; poor health; and harsh climate) it is difficult to infer policy implications. The UZB CPS appendix had no assessment of the causes of poverty. Moreover, the background poverty study carried out to support the UZB CPS preparation did not include an explicit identification of the causes of poverty.

Box 2. Some Common Measures of Inequality

There are broadly two types of measures of inequality in income or expenditure. One measures relative inequality, and the other measures absolute inequality. The former is more commonly used in applied economics, but the latter is also receiving increasing attention lately.

Measures of Relative Inequality

Relative inequality is a function of ratios of individual incomes to the mean. This implies that when incomes of all individuals are multiplied by a certain constant, inequality is unchanged. The most commonly used inequality measures, such as the Gini coefficient, Theil index, quantile ratio, and income (or expenditure) share of the poorest group, satisfy this so-called “scale independence axiom” and, therefore, are measures of relative inequality. There are also other properties that economists consider as desirable to possess as measures of relative inequality, including “population independence”, “transfer principle”, and “decomposability.” Population independence implies that the inequality of two populations with different sizes but the same distribution is identical. The transfer principle requires that transferring income from a richer person to a poorer one, without reversing their ranks in distribution, should lead to a fall in inequality. Decomposability means that it is possible to decompose inequality of a given population into inequality within each of its subgroups and between subgroups. However, not all the inequality measures satisfy these properties. Inequality measures also differ in their sensitivity to income differences at different points along the distribution.

The **Gini coefficient** is the most commonly used measure of relative inequality. Numerically, it can be computed as:

$$Gini = \frac{-(n+1)}{n} + \frac{2}{n^2 \mu} \sum_{i=1}^n i \cdot y_i$$

where y_i is income of individual i , μ is the mean income of the population, and n is the number of individuals in the population. The Gini coefficient ranges from zero, indicating perfect equality, to 1 (or 100 when expressed in percentage terms), indicating perfect inequality. The Gini coefficient is population independent, and satisfies the transfer principle. Another attractive feature of the Gini coefficient is that it can be graphically represented using the Lorenz curve, which maps the cumulative income share on the vertical axis against the distribution of the population on the horizontal axis. A major weakness of the Gini coefficient, however, is that it cannot be decomposed by population subgroups. The Gini coefficient gives larger weights to income changes closer to the mode of the distribution and smaller weights to changes closer to the tails.

The **Theil index** has gained popularity because it satisfies all the desirable properties described above. Numerically, the Theil Index (T) can be computed as:

$$T = \frac{1}{n} \sum_{i=1}^n \frac{y_i}{\mu} \left(\ln \left(\frac{y_i}{\mu} \right) \right)$$

where y_i is income of individual i , μ is the population mean income, and n is the number of individuals in the population. A particularly attractive feature of the Theil Index is that it can be decomposed by population subgroups, where subgroups can be defined by socioeconomic characteristics such as geographical location, nationality, or gender. Assuming that a population consists of h subgroups and the Theil Index of each subgroup is T_g , the overall inequality of the population, T , can be computed as:

$$T = \sum_{g=1}^h s_g T_g + \sum_{g=1}^h s_g (\ln(s_g / p_g))$$

where s_g is group g 's income share of the total income, and p_g is group g 's population share of the total population. The first summation is the average of the Theil Indexes of h subgroups weighted by income shares, and gives the component of overall inequality that is due to inequality within subgroups. The second summation is the Theil index calculated on the mean income of each subgroup, and hence gives the component of overall inequality that is due to between-group inequality. A major weakness of the Theil index is that, while it is equal to zero when the distribution is perfectly equal, it does not have an upper limit. However, it can be shown that the value of the Theil index is 1 for an inequality slightly above the

continued next page.

Box 2. continued.

equivalent to the frequently cited 80:20 distribution, that is, 80% of the wealth is owned by 20% of the population. The Theil index gives equal weight to income (or expenditure) changes across different locations of the distribution.

A common weakness of both the Gini coefficient and Theil index is that any transfer of income between two individuals has an impact on inequality, whether it takes place among the rich, among the poor, or between the rich and the poor. If a society is most concerned about the difference between the rich and poor, or the share of income of the people at the bottom, alternative measures can be used.

The quantile ratio is the ratio of the mean income (or expenditure) of the top group to the mean income (or expenditure) of the bottom group, with groups defined in terms of deciles, quintiles, or quartiles. By expressing the income of the rich as multiples of that of the poor, it is readily interpretable. The most commonly used quantile ratio is the 90/10 ratio, which is the mean income of the 90th percentile divided by the mean income of the 10th percentile. The quantile ratio is population-independent, and can be decomposed. In the case of the 90/10 ratio, for example, it could be expressed as the product of the 90/50 ratio and 50/10 ratio. This decomposition indicates to what extent the 90/10 ratio is driven by inequality at the top of the distribution versus inequality at the bottom end.

Income (or expenditure) share of the poorest group is the share of income (or expenditure) belonging to the poorest group of a population, where the poorest group can be defined in terms of deciles, quintiles, or quartiles.

Other measures of relative inequality that are less commonly used are logarithmic variance, coefficient of variation, and Atkinson's class of inequality measures.

Measures of Absolute Inequality

While, traditionally, relative inequality has been the focus of the study on income distribution, more recently, measuring absolute inequality is receiving increasing attention. This is partly due to the debate on the impact of globalization on inequality. As noted by Ravallion (2004), if using the relative concept, globalization only has had limited impact on inequality; but using the absolute concept, globalization has had very significant impact on inequality. Survey studies of public perceptions about relative vis-à-vis absolute inequality have also drawn attention to measuring absolute inequality. Absolute inequality measures look at the absolute differences in income or expenditure between rich and poor subgroups of a population, and they do not satisfy the scale independence axiom.

Sources: Cowell (1995), Ravallion (2004), and ADB (2007b).

Which causes of poverty are most serious or which constraints to poverty reduction are most critical were insufficiently analyzed for the poverty assessment. Although causes of poverty were listed in most cases, the discussion merely enumerated and explained the causes of poverty, rather than diagnosing which causes were most serious or which

constraints to poverty reduction were critical. This was true even for the LAO CPS, which contained a good discussion of the causes of poverty. This gap raises the question of to what extent poverty assessments provide country teams with useful insights and inputs in determining ADB's partnership strategies in the concerned DMCs.

2.4 PRIVATE SECTOR ASSESSMENTS

A. Assessment Framework

Private sector development is one of the thematic priorities under ADB’s *Enhanced Poverty Reduction Strategy* (ADB 2004b), the *Long-Term Strategic Framework (2001–2015)* (ADB 2001b), and the *Medium-Term Strategy II (2006–2008)* (ADB 2006i). ADB has articulated this strategic thrust twice to enhance its support for private sector operations. The initial articulation occurred when the first strategic framework, *Private Sector Development* (ADB 2000), was released, and the second was when *Private Sector Development: A Revised Strategic Framework* was issued (ADB 2006e). These two PSD strategic guidelines, however, are more relevant for lending and nonlending operations than for diagnostic work. In the absence of handbooks or guidelines for conducting private sector assessments (PSAs), *Retro 2006* used the following framework for assessing the diagnostic quality of PSAs, focusing on three

areas: (i) profile of the private sector, (ii) diagnosis of critical constraints to PSD, and (iii) assessment of prospects for PSD (Table 6).¹⁴

Private sector profiling is necessary to understand the private sector’s role in an economy and to provide an appropriate context for analyzing the issues and constraints it faces. Profiling the private sector may involve describing its size, structure, sector composition, and recent performance, as well as the factors driving or hindering its performance. Identifying the constraints to PSD requires examining the country’s climate and conditions for private investment and business. Profiling may describe the overall business environment, which consists of regulatory, policy, legal, and financial environments within which private companies operate. For transition economies, progress in privatizing state-owned companies could also be examined. Based on these analyses, the outlook and prospects for PSD may be assessed and policy recommendations made as a result.

Table 6. Framework for Private Sector Assessments

Topic	Key Questions	Assessment Method
Private Sector Profile	<ul style="list-style-type: none"> • What constitutes the private sector in the country? • How important is the private sector in the economy? 	<ul style="list-style-type: none"> • Characterize the private sector in terms of size and sector structure. • Discuss the importance of the private sector to the economy.
Constraints to PSD	<ul style="list-style-type: none"> • What are the constraints to doing business and private investment in the country? 	<ul style="list-style-type: none"> • Analyze the quality of regulatory, policy, legal, and financial environments within which private companies operate. • Identify the critical constraints to PSD, including through investment climate or costs of doing business surveys.
Prospects for PSD	<ul style="list-style-type: none"> • What are the prospects for PSD? 	<ul style="list-style-type: none"> • Analyze the emerging trends in PSD. • Link the analysis of these trends to the identified constraints and assess the prospects for PSD. • Suggest what governments could do to address market or institutional failures.

PSD = private sector development

Source: Compiled by the Economics and Research Department.

¹⁴This framework is only for the purpose of assessing the diagnostic quality of private sector assessments; it is not a recommended template for developing the full private sector road map.

B. Diagnostic Quality of Private Sector Assessments

Four of the five CPS papers (LAO, PNG, UZB, and VIE) had a PSD appendix, all supported by recent in-depth background studies. The INO CPS contained an appendix on private sector operations by ADB but no private sector assessment per se. An in-depth background study of PSD was also prepared for the INO CPS, but was not covered in this retrospective, because its existence was only revealed to ERD during an interdepartmental review of the draft *Retro 2006*.¹⁵

The background studies on private sector development generally were of good diagnostic quality. All the PSA background studies provided adequate profiles of the private sector and careful analysis of the factors constraining its development. The VIE study could be considered a good practice example, wherein the sector profiling included a clear definition of the private sector in the Viet Nam context and a good discussion of its macroeconomic context and links to poverty reduction. The private sector components—funding sources and sectoral and geographical locations—were well analyzed with updated data. The assessment of constraints to the development of small, medium, and micro enterprises and the private provision of physical infrastructure was also sufficiently diagnostic, with specific reforms suggested.

The diagnostic quality of the CPS appendices, however, did not appear as satisfactory as that of the background studies. There were noticeable differences in diagnostic quality between the background studies and the CPS appendices. First, the private sector profiles appeared inadequately summarized in the CPS appendices. It is generally difficult to infer from the discussion the basic underlying factors driving the performance of the private sector. Second, the identification of the critical constraints in the CPS appendices was less clear and not always consistent with the background studies. The UZB CPS appendix, for example, mainly discussed financial accessibility and industrial organizations as constraints to PSD, leaving unattended other

significant constraints identified by the background study such as punitive tax rates, inefficient tax administration, and macroeconomic instability. Such discrepancies between background studies and CPS appendices possibly reflect two problems. One is presentational—the CPS appendices failed to provide relevant details when summarizing the background studies' findings. The other problem may have to do with a divergence in opinions of the authors of the two documents—presumably the CPS appendices were mainly prepared by ADB staff and the background studies by consultants.

Nevertheless, findings from private sector assessments were reasonably well integrated into relevant sector road maps. Of the 28 sector road maps in the five CPS papers, over half addressed PSD issues. The most notable examples of integrating PSA findings were found in the financial sector and infrastructure sector road maps, as limited access to credit and poor infrastructure availability are almost universal constraints to PSD. In addition to financial access and infrastructure availability, a wide range of issues constrains PSD. These issues have to do with labor market regulations as well as trade and industrial regulations, and do not necessarily fall into the typical sectors in which ADB chooses to operate.¹⁶ In such cases, there was no place in the CPS to address these issues, but the VIE CPS was an exception. The VIE CPS included, in addition to an appendix on PSA, a separate road map discussing the policy and institutional framework for development of the private sector and small and medium enterprises and proposing specific interventions.

¹⁵The background study was not listed as a reference in the CPS paper or mentioned in the country team survey at the initial stage of the retrospective exercise.

¹⁶Although draft staff guidelines on the design of small and medium enterprise support projects were prepared in 2004, ADB does not require preparation of a strategy for the industry and trade sector (ADB 2005b).

Table 7. Diagnostic Framework for Sector Road Maps

Topic	Key Questions
Sector Performance—Impact, Outcomes, and Outputs	<ul style="list-style-type: none"> • How is the sector performing in terms of impact, outcomes, and outputs? • Is it underperforming compared to Millennium Development Goals, national targets, and international standards? • How important is the sector in the economy and in supporting growth and poverty reduction?
Sector Constraints	<p>If a sector is underperforming, what are the critical constraints:</p> <ul style="list-style-type: none"> • Lack of financing? • Weak institution? • Weak capacity? • Faulty policy? • Demand-side constraints?
Government Plan, Other Development Partners' Assistance, and ADB's Experiences	<ul style="list-style-type: none"> • How sound is the government's plan given the sector constraints identified? • How feasible is the government's plan given its capacity and budget? • How are other development partners supporting the government plan? • What is ADB's past experience in the sector?
ADB Strategy and Interventions	<ul style="list-style-type: none"> • What is the appropriate strategy for ADB? • What are the proper sequences of ADB interventions? • What are the proper modalities for ADB interventions?

ADB = Asian Development Bank.

Source: Compiled by the Economics and Research Department.

2.5 SECTOR ROAD MAPS

A. Assessment Framework

A well-prepared sector road map should provide sound sector diagnosis to identify the constraints to sector development; assess the government's sector development plan, other development partners' assistance to the sector, and ADB's sector experience and core competencies;¹⁷ and, on the basis of these, design relevant ADB interventions at the sector level (ADB 2007a). A sector road map also requires a results framework for monitoring and evaluation purposes. While all these are important components of a sector road map (Table 7), this retrospective focuses only on diagnosis of sector constraints.

The diagnosis of sector constraints could start by examining sector performance. If a sector is underperforming, it could be due to supply-side constraints, such as lack of financing; weak planning capacity; faulty policy; poor regulatory, governance, and accountability frameworks; and/or an adverse macroeconomic environment. Or, it could be due to demand-side constraints. Robust sector diagnosis is

¹⁷In this document, ADB's core competencies refer to ADB's capabilities that contribute to its uniqueness and distinctiveness as compared with other development partners.

essential to ensure that ADB assistance is targeted at the sector's critical constraints and leads to the maximum possible development impact.

B. Diagnostic Quality of Sector Road Maps

Sector performance in terms of impacts, outcomes, and outputs was generally well discussed, but the importance of the sector to relaxing the constraints to growth and poverty reduction could have been more clearly highlighted. Most sector road maps presented sector-specific indicators of impacts, outcomes, and outputs.¹⁸ Some road maps presented historical trends, future outlook, and international comparisons of these indicators. In this regard, the VIE CPS paper's education and health sector road maps and the INO CPS paper's energy sector road map provided good practice examples. Some road maps, mostly those for the agriculture sector, also discussed the sector's importance in the economy and in supporting growth and poverty reduction to reinforce the rationale for their selection for ADB interventions. In the LAO CPS, agriculture was selected for intervention for clear reasons: the

¹⁸The exceptions are the Indonesia financial sector and health sector and all UZB sectors, as these are integrated with the CPS results framework. In these results frameworks, the indicators of sector outcomes and impacts were discussed.

sector accounted for 50% of GDP, employed 80% of the total labor force, and was the primary source of livelihood for the poor. The INO CPS noted that the agriculture and natural resources sector was the backbone of economic growth, contributed about a quarter of GDP, and was the base for the largest segment of the Indonesian population and the poor. But this type of discussion was not presented in many other sector road maps. The findings give credence to recommendations of the stocktaking report (ADB 2006d) such as (i) to pursue more rigorous diagnostics for priority sectors to examine specific sector constraints, their causes, and their opportunities; and (ii) to ensure that sector selection is more firmly rooted in the analysis of development issues specific to the DMC, and that the sector road maps directly answer the most critical constraints.

In assessing sector constraints, the institutional arrangements, policy framework, and organizational capacity were not given adequate attention. Apart from lack of financing, a sector is often constrained by institutional, policy, or capacity weaknesses. Institutional weaknesses could arise from inappropriate ownership structure and ineffective regulatory framework; weaknesses in policy (such as excessive price subsidies) could lead to distortions of market incentives; and weaknesses in capacity could undermine the formulation of development plans and their effective implementation. These weaknesses often reflect either market or government failures. Overall, these aspects were often not adequately covered in many sector road maps, with notable exceptions. For example, the VIE water supply and sanitation (WSS) sector road map showed that limited community awareness and participation in planning and management of urban services constrained the efficient provision of urban infrastructure and WSS services, especially in small and medium-size towns. The UZB road sector road map explicitly identified government failures as evident in the gaps in regulations and policies. Similarly, the LAO WSS sector road map explicitly discussed government failures reflecting the absence of any clear legislative framework and weak capacity. The INO WSS sector road map adequately analyzed institutional failure in the light of issues related to decentralization (e.g., separation of ownership and management of local government utilities to increase their performance and accountability, as well as objective determination of tariff levels to support cost recovery).

Not all sector road maps looked at demand-side constraints. WSS sector road maps generally presented adequate analysis and discussions of demand-side factors, especially deficiencies of information. For instance, the analysis for LAO explained that because the importance of improved sanitation for the health of women and children was not well understood, local demand and household initiatives for improved sanitation were lacking. The UZB WSS sector analysis highlighted that the water problem was partly owing to the public's attitude, i.e., treating water as an inexhaustible and very cheap resource, which then leads to system losses, waste of scarce resources, and difficulties in collecting water bills. The VIE WSS road map clearly explained that one of the challenges for the sector was to change people's attitudes to investing in household sanitation facilities.

However, in the road maps of many other sectors, demand-side factors were often not examined. For example, four of the five CPS papers included education sector road maps that focused only on supply-side factors, such as school access and teaching quality. None analyzed demand-side constraints, such as sufficiency of parents' information on returns to education; whether the child labor market, on-farm work, migration opportunities, or household chores imposed very high opportunity costs on going to school; and whether there was gender bias in parental decisions on schooling. None of the four education sector road maps reviewed discussed the return to education for the country. The lack of discussions on demand-side constraints could weaken the justification for interventions that might be proposed in the future for providing more schools and teachers.

Sector road maps were based primarily on the report and recommendation of the President (RRP) and technical assistance (TA) papers. Table 8 shows that most citations in the sector road maps were documents produced by ADB, including RRP (42%); TA (20%); country assistance program evaluation, sector assistance program evaluation, country strategy and program update, project performance audit, and other ADB papers (8%),¹⁹ most of which were project-specific. The review found only one stand-alone sector study (ADB 2005c). Basing sector

¹⁹Non-ADB references were less frequently cited, with about one citation per sector road map on average.

Table 8. Supporting References Cited in the Sector Road Maps

References	INO	LAO	PNG	UZB	VIE	Total
Number of Sector Road Maps	7	7	2	5	7	28
Number of Citations in the Sector Road Maps	33	22	9	16	35	115
Of which...						
ADB RRP	15	9	0	9	15	48
ADB TA	2	8	1	3	9	23
ADB CAPE, SAPE, CSPU, PPAR	4	1	0	0	0	5
Other ADB publications	2	1	0	1	1	5
Non-ADB sources	10	3	8	3	10	34

ADB = Asian Development Bank, CAPE = country assistance program evaluation, CSPU = country strategy and program update, INO = Indonesia, LAO = Lao People's Democratic Republic, PNG = Papua New Guinea, PPAR = project/program performance audit report, SAPE = sector assistance program evaluation, UZB = Uzbekistan, VIE = Viet Nam

Source: Compiled by the Economics and Research Department.

road maps on project-specific documents could raise three concerns. One is the adequacy of sector assessments in project-specific documents. Second is the objectivity of the sector work conducted—even if the results of the sector work seem unbiased for the project, the analysis is susceptible to focusing too much on project-related aspects. The third concern is the difficulty of tracking this kind of sector work. An OED special study on ETSW in 2001 noted that the monitoring and evaluation framework for ETSW within ADB was not in place, and, as a result, data on the overall cost of ETSW, outputs, or impacts were not readily available (ADB 2001c).^{20, 21} *Retro 2006's* investigation of background sector work that supports the development of sector road maps confirms that this situation has not changed much.

Effective tracking systems for sector work are yet to be developed in most parts of ADB.

Sector work provides analytical inputs to the development of sector road maps. *Retro 2006* found it generally difficult to track how many background ETSW studies supported the development of the sector road maps. Securing copies of ETSW outputs often turned out to be challenging. The South Asia Department (SARD) pioneered a compilation of ETSW and can be considered a good practice example. SARD produced 103 ETSW products in 2005, not counting ADO chapters as well as country economic reports (ADB 2006f). Of these, 95 were country-specific—equivalent to 13.6 ETSW products per country per year. Resident missions produced 78% of the total, an average of 4.6 per professional staff, and the India Resident Mission alone accounted for 48% of the total, with each professional staff on average producing 9.8. The number of ETSW products was positively correlated with the size of country and sector operations. These ETSW products, in addition to external publications, helped to inform the preparation and design of ADB lending and nonlending operations and supported the development of CPS papers.

²⁰Despite the difficulty in defining, tracking, and evaluating sector work, or ETSW in general, significant ADB resources have been used to produce them. An OED study in 2001 estimated that 5–6% of professional staff time was devoted to economic sector work activities. In addition, direct staff consultant inputs of \$3 million to \$5 million and anywhere between \$30 million and \$50 million of TA resources were used for economic sector work tasks per year, accounting for roughly 15–25% of total TA resources (ADB 2001c).

²¹The Budget, Personnel, and Management Systems Department started compiling the number of non-TA ETSW products from 2003 to 2010 by originating department to track annual work accomplishments, plan, and budget requirements. It consulted the Regional and Sustainable Development Department and the Strategy and Policy Department regarding the base for the role as focal point to track ETSW and guide the data collection. Eventually, the Budget, Personnel, and Management Systems Department would like a more complete database (with author, sector/theme, and paper type) and to find a permanent custodian for the database.