

Appendixes

Appendix 1: Abstract of ADF I–V Report¹

The Asian Development Fund (ADF) I–V portfolio comprised 488 projects totaling \$11.2 billion. ADF resources were transferred to developing member countries (DMCs) mainly through projects. During ADF V, however, programs became a significant lending modality, accounting for about 26% of ADF V total lending as the Asian Development Bank (ADB) put greater emphasis on policy dialogue to support policy reforms in the DMCs at the macro and sector levels.

The allocation of ADF resources focused on DMCs with the lowest per capita gross national product (the main eligibility criterion during the period) including Bangladesh, Nepal, Pakistan, and Sri Lanka, which accounted for 76% of the total loan amount and the Pacific Islands economies, which received 4% of resources. Most of ADF I–V resources (about 47%) went to agriculture, particularly to irrigation and rural development, because of the heavy economic dependence on this sector and the fact that the majority of the population, especially the poor, lived in rural areas. Significant allocations were also provided to energy (16%), social infrastructure (13%), and transport and communications (11%). This allocation pattern reflected ADB's general strategy during the period, which relied mainly on economic growth to reduce poverty, but with greater attention given to the social dimensions in ADF IV–V.

Based on project and program performance audit reports rating, project performance was mixed. Of the 290 projects evaluated, 45% were rated generally successful, 43% partly successful, and 12% unsuccessful. Statistically significant differences in average performance ratings of projects were noted between Group A and Group B DMCs in favor of the latter, with physical infrastructure projects performing better than agriculture and social infrastructure projects. Among lending modalities, projects performed significantly better than programs and development finance institution credit lines, while sector loans were on a par with the overall average. In the 15 years between 1976 and 1991, there was a steady decline in the proportion of projects rated unsuccessful. However, the proportion of projects rated partly successful increased more (from 42%

in 1976–1978 to 50% in 1987–1991) than those rated generally successful (ranging from 42% to 44% during the same period). This suggests that there is still room for improvement in the efficient use of scarce concessional resources.

On the whole, the ADF I–V operations may be considered satisfactory. There were real achievements but there were also gaps between expectations and results. Projects designed to enhance the DMCs' productive capacity, such as those in energy, transport and communications, and irrigation, promoted economic growth. Indirectly, they contributed to poverty reduction. On the other hand, projects designed to directly reduce poverty through increased employment and income opportunities, as well as those designed to enhance the general well-being of the poor, while making positive contributions to these objectives, generally produced results below expectations. Lessons learned have been or are being considered in the design and implementation of subsequent projects. The lessons include the need for thorough project preparation considering not only the technical and financial aspects, but the local culture as well; the need for real beneficiary participation to develop a sense of ownership of the project; the need to enhance the capability of ADB staff to deal with stakeholders at the grassroots level; the need to thoroughly assess the capability of the executing agency to match the requirements of the project and to remedy the gap, if any, through appropriate technical assistance; the need for long-term commitment to a sector or subsector in providing assistance; the need for vigilance to ensure transparency and accountability in project management; and the importance of a policy environment supportive of the project.

Conclusions

Despite being the fastest growing region in the world during the past three decades, Asia and the Pacific still has the largest number of the world's poor people. While the proportion of poor relative to the total population has been declining, their absolute

¹ ADB. 2001. *A Review of the Asian Development Fund I–V Operations*. Manila.

number has been growing. The People's Republic of China and India, which have the biggest proportion of the region's poor, do not have access to ADF resources. The rationale for ADF—providing concessionary terms to meet the needs of the poorest in the region—continues to be valid. Experience in implementing ADF I–V provides insights that can help make future ADF operations more effective in addressing the poverty problem.

Growth of Contributed Resources

During the first five commitment periods, contributed resources grew, though at a decelerating rate. The growth occurred in absolute amount, percentage of the contributing countries' gross national product (except for ADF V), and share in the aggregate net resource flows to the borrowing DMCs. While the share of the ADF in the aggregate net resource flows to the borrowing DMCs increased, the share remained small in relation to the total official development assistance.

Focus

Based on the allocation pattern of ADF I–V, focus was achieved at the level of DMCs and of sectors and subsectors within the DMCs, and to some extent at the level of regions. What was not evident, however, was focus in terms of target beneficiaries. The portion of the ADF portfolio allocated for direct poverty reduction projects should concentrate on well-selected target beneficiaries and should provide continuing assistance. Sector indicators or milestones need to be better specified. A review of the appraisal reports and project and program performance audit reports reveals that in most of the ADF

I–V projects, the target beneficiaries were not clearly defined. Although social dimensions began to be integrated into projects toward the end of ADF V, the targeting of beneficiaries—who, where, and how many of the poor were expected to benefit—remained unclear for most projects.

Overall Project Impacts

Consistent with ADB's development strategy during ADF I–V period, a significant part of ADF resources was invested in physical infrastructure projects designed to enhance the DMCs' productive capacity to achieve economic growth. Given the high success rates of these projects, the most significant impact of ADF I–V operations was in helping promote economic growth, particularly in Lao People's Democratic Republic, Myanmar, Nepal, Pakistan, and to some extent in Bangladesh and Sri Lanka, thus indirectly contributing to poverty reduction in these DMCs. On the other hand, projects designed to have a direct impact on the poor, in terms of employment and income generation and enhanced well-being, had mixed results. While projects in the education, irrigation and rural development, and forestry subsectors and multisector projects showed above average performance, those in other sectors (livestock, fisheries, industrial crops, agricultural support services, urban development and housing, water supply and sanitation, health and population, and development finance) generally fell below expectations. Other noteworthy impacts of ADF I–V were contributions, albeit limited, to strengthening the institutional capacity of the executing agencies and promoting policy environments in DMCs.

Appendix 2: Evaluation Approach and Methods

This report evaluates the performance of Asian Development Fund (ADF) VI–VII against the stated objectives, covering 318 projects and \$12 billion in loans, approved during February 1992–December 2000. As of December 2002, 135 of these projects had been completed, and project completion reports (PCRs) with ratings were available for 102 of them.¹

Evaluation Methods

This report is based on the PCRs and other evaluative material on file, reviews of special evaluation studies conducted by the Asian Development Bank (ADB) during this period, including thematic evaluations and country assistance program evaluations, interviews with staff at ADB headquarters and government representatives in developing member countries (DMCs), field interviews with participants and beneficiaries for a sample of projects, and observations and other direct data collection for a sample of projects. Focus group discussions were held in the field and at ADB headquarters, and working papers circulated in advance of the drafting of this main report.

Data Sources and Sampling

Tables A2.1 and A2.2 provide information on the projects approved under ADF VI–VII. The former

disaggregates the information by strategic development objective (SDO) and the latter, by sector. Balancing samples to reflect the distributions by SDO and sector was complex. Most of the projects had growth as a primary SDO but in ADF VII, poverty reduction projects became increasingly important. In terms of sectors, projects in the agriculture and natural resources and social sectors dominated ADF VI–VII, accounting for over 60% of the lending during this period. These factors contributed to balancing and weighing the sample, especially the selection of country case studies.

The appropriate type of data collection and the appropriate sample to be examined varied by issue. In some cases, data was examined for all 318 projects approved during ADF VI–VII, for example, in regard to the lending mix or overall resource allocation. In other cases, issues could be examined on the basis of a smaller sample. Where this was methodologically adequate, it was also economical. Several such samples were used in the report. For example, where the issue related to a particular sec-

¹ Two additional PCRs were available for emergency loans—Loan 1171-COO(SF): *Emergency Telecommunications Rehabilitation Project* and Loan 1218-RMI(SF): *Emergency Typhoon Rehabilitation Assistance Project*—which were not required to be rated in the PCRs.

Table A2.1: Number and Loan Amount of ADF VI–VII Projects (approved and completed,^a by primary SDO)

Primary SDO	Projects Approved				Projects Completed				% Completed	
	No.	%	Amount (\$ million)	%	No.	%	Amount (\$ million)	%	No.	Amount (\$ million)
Economic Growth	159	50	6,907	57	93	67	3,499	76	58	51
Human Development	87	27	2,830	24	31	23	917	20	36	32
Poverty Reduction	40	13	1,188	10	6	5	97	2	15	8
Women in Development	8	3	251	6	1	1	5	0	13	2
Environment	24	8	843	2	4	5	104	2	17	13
Total	318	100	12,018	100	135	100	4,622	100	42	39

ADF = Asian Development Fund, SDO = strategic development objective.

^aAs of 30 December 2002.

Note: Figures may not add up to total because of rounding.

Source: Asian Development Bank's Loan Financial Information System.

Table A2.2: Number and Loan Amount of ADF VI–VII Projects (approved and completed,^a by sector)

Sector	Projects Approved				Projects Completed				% Completed	
	No.	%	Amount (\$ million)	%	No.	%	Amount (\$ million)	%	No.	Amount (\$ million)
Agriculture and Natural Resources	99	31	3,359	28	32	23	957	21	32	23
Energy	28	9	1,429	12	12	9	417	9	43	30
Governance, Finance, Trade, and Industry	24	8	720	6	17	13	543	11	71	72
Infrastructure	45	14	2,581	21	24	18	1,243	27	53	41
Social Sectors	99	31	3,352	28	34	25	1,022	22	34	24
Others	23	7	578	5	16	12	438	9	70	76
Total	318	100	12,018	100	135	100	4,620	100	42	34

ADF = Asian Development Fund.

Note: Figures may not add up to total because of rounding.

^aAs of 30 December 2002.

Source: Asian Development Bank's Loan Financial Information System.

Table A2.3: Completed ADF VI–VII Projects, by Sector (as of 30 December 2002)

Sector	Projects Completed		Random Sample of Completed Projects		Selected Case Studies	
	No.	Amount (\$ million)	No.	Amount (\$ million)	No.	Amount (\$ million)
Agriculture and Natural Resources	32	957	5	125	3	186
Energy	12	417	3	66	1	30
Governance, Finance, Trade, and Industry	17	543	6	168	3	68
Infrastructure	24	1,243	5	429	1	50
Social Sectors	34	1,022	12	303	4	74
Others	16	438	4	205	0	0
Total	135	4,620	35	1,296	12	408

ADF = Asian Development Fund.

Source: Asian Development Bank's Loan Financial Information System.

tor or a particular SDO or a particular type of DMC, then the appropriate sample was usually either all projects in that group, or all completed projects in the group. When women in development (WID) issues were assessed, all 8 WID projects were examined, 1 completed and 7 ongoing, for which WID was the primary SDO. The same procedure was followed for issues related to sectors, lending modality, or country groups. In general, there were three samples of projects used in this report (Table A2.3):

- (i) A stratified random sample of projects drawn from the whole population of 336, weighted by loan amount. Stratification, in this case, was by sector to ensure that the issue was examined in all sectors;
- (ii) A random sample of 35 of the 135 completed projects; and
- (iii) A sample of 12 case study projects.

The five SDOs were economic growth, human development, poverty reduction, WID, and environ-

mental protection and natural resource management. In terms of loan amount, most projects listed economic growth as the primary SDO (50%), followed by human development (27%) and poverty reduction (12%) (Table A2.1).

The SDO analysis is carried out in several ways in this report, including reviews of the whole population of ADF VI–VII projects, stratified random samples of completed projects, and case studies in the sample of five DMCs selected for this report.

The criteria for selecting the DMC sample included eligibility group, size of portfolio, and region. If the Operations Evaluation Department had completed a country assistance program evaluation, or had one under way simultaneously with this report, then this was taken into consideration in selecting the sample. Finally, it was attempted to cover a range of country situations, from landlocked to small island, from large multilingual states to small homogeneous states, and to include both transition economies and well-established market economies. No sample can fully capture the whole range of variation, but these five DMCs, supplemented by the wider samples of projects discussed, were considered representative for the purposes of this report (Table A2.4).

Table A2.4: Sample of Developing Member Countries

Eligibility Group	Region	Country	Project Portfolio	Type of Economy
A	East and Central Asia	Kyrgyz Republic	Medium	Transition Market
	Pacific	Vanuatu, Samoa	Small	
B1	Mekong	Viet Nam	Large	Transition Market
	South Asia	Sri Lanka	Large	

Appendix 3: Matrix of ADF VI–VII Commitments

Commitment	Actions and Progress To Date
<p>1. Stimulating Growth and Improving Poverty Impacts</p> <ul style="list-style-type: none"> Donors to the Asian Development Fund (ADF) VI–VII urged the Asian Development Bank (ADB) to use these funds in support of broad-based economic growth and the development of market economies. They also encouraged ADB to take a balanced approach to efforts to stimulate growth while including poverty reduction measures and investments to the social sectors. 	<p>Many ADF-recipient developing member countries (DMCs) grew relatively slowly over the past decade and were vulnerable to external shocks. ADF was a small part of the public finances of most DMCs, and looking for a clear statistical relationship between ADF and changes in gross domestic product would, in most cases, be difficult if not impossible. From the economic analysis of completed projects, the economic internal rate of return was on average more than 20%, well above ADB's minimum level of 12%. ADB helped address the principal obstacles to growth, such as weak legal and regulatory frameworks, and lack of private sector involvement and competition, through its program lending modality. Three factors proved to be essential for success: (i) understanding the country context and incorporating lessons learned in subsequent projects, (ii) providing inputs that were critical for growth and development, and (iii) designing projects that supported the government reform strategy.</p>
<p>2. Human Development</p> <p><i>ADF VI</i></p> <ul style="list-style-type: none"> Assistance for population activities should be expanded. Priority areas for ADB support should include family planning and maternal-child health care, information-education-communications, research in contraceptive methods, demographic analysis, and training. <p><i>ADF VII</i></p> <ul style="list-style-type: none"> Increase investments in human capital, especially education, vocational training and health, and increased and sustainable access for the poor to social infrastructure—especially primary health care, family planning, preventive public health measures such as access to clean water and sanitation. 	<p>One of the biggest changes in the social sectors has been the way projects are designed. After 1995, more attention was given to developing investments in conjunction with sector policies needed to support the investments; that is, projects became broader, addressing more complex issues, often including components that supported sector reforms and involving additional executing or implementing agencies. The emphasis shifted considerably during ADF VI–VII, away from projects with substantial population planning components toward a broader human development focus. Investments increased in the three main areas of human development projects: education, health, and urban development.</p>
<p>3. Poverty</p> <p><i>ADF VI</i></p> <ul style="list-style-type: none"> Increase coordination with national strategies and policies and activities for poverty reduction. <p><i>ADF VII</i></p> <ul style="list-style-type: none"> Improve poverty-targeted investments including the gender dimensions of poverty. Increase participation and coordination through nongovernment organizations (NGOs) and other grassroots level organizations to provide assistance to the most disadvantaged groups. Intensify efforts to address poverty and social inequality in countries including efforts to reach the poorest and most disadvantaged segments of society. Adopt a policy on poverty reduction. 	<p>Poverty reduction has been mainstreamed in ADB's operations. Coordination with national poverty strategies improved with the introduction of poverty reduction partnership agreements. ADB has, however, been slow to develop a strategic orientation toward poverty reduction. Therefore, poverty reduction efforts were concentrated in a few sectors. This resulted in some gaps in the reach of ADF-supported poverty reduction projects: (i) no primary poverty reduction project was targeted directly at the urban poor; (ii) 11 of 26 borrowers in ADF VI–VII had no projects that were primarily for poverty reduction; and (iii) ADF VI–VII did not reach the largest populations of poor people, in the People's Republic of China and India, comprising about 80% of the poor in the region. Secondary poverty reduction activities showed broader efforts, especially in the social sectors, infrastructure, and special assistance and emergency lending, reflecting the increasing attention to poverty reduction in project design. Of the projects approved during this period, 39% included primary or secondary poverty reduction efforts.</p>
<p>4. Women in Development (WID) and Gender and Development</p> <p><i>ADF VI</i></p> <ul style="list-style-type: none"> Ensure that gender issues are more systematically addressed in all programs and projects. Pay greater attention to the effects of ADB projects on women. Prepare a strategic plan of action that includes recommendations on integrating WID issues into planning and implementation of programs and projects; the allocation of appropriate resources, including staff resources; and training of professional and senior level staff. The plan should guide ADB in implementation of its policy on WID. Implement WID activities more fully by considering WID aspects at every stage of the programming and project cycles and ensure that women are targeted much more effectively in operations, both as donors and beneficiaries. 	<p>WID lending was very low during 1992–2000, partly because of the “donor congestion” in this area. It appears that having WID as an SDO and expanding it subsequently into GAD made little difference to the ADF project portfolio. Although sensitivity to gender issues improved, there is little evidence that ADB's portfolio was substantially more favorable to women at the end of ADF VI–VII than it was at the beginning. To mainstream gender issues in projects, ADB adopted the GAD policy in 1998. There is no adequate empirical basis yet for concluding the effectiveness of the GAD policy in this report. A full evaluation of its results is scheduled for 2004, 6 years after the policy was adopted. By then, there should be a more solid basis for assessing the impact of the GAD framework.</p>

ADF VII

- Reinforce efforts to improve the status of women by increasing lending to targeted WID projects, further mainstreaming gender considerations in all operations, and deepening ADB's understanding of gender issues.
- Increase lending to targeted WID projects and mainstream gender considerations in all operations.

5. Environment*ADF VI*

- Strengthen the environmental expertise available in ADB.
- Greater participation by affected groups and local NGOs in the environmental impact assessment process.
- Greater disclosure on all projects having a significant impact on the environment.
- Expand support to the forestry sector, particularly for the protection of tropical forest resources.

ADF VII

- Increase environmental lending in six priority areas: (i) pollution control in the industry and power sectors, (ii) environmental improvement in the urban areas, (iii) environmentally sound tropical forest management and conservation of biological diversity, (iv) interlinked poverty reduction and environmental improvement, (v) agriculture, and (vi) institution building and human resource development.
- Continue to strengthen the capability of borrowers, from both public and private sectors, on environmental impact assessment and other aspects of environmental planning and management.
- Conduct policy dialogue and integrate environmental considerations in country strategy and country programming exercises.

6. Program Lending

- Support policy adjustments that contribute to growth and benefit the poor.
- Strengthen policy analysis and, where reforms are needed, advocate the necessary policy changes.
- Support sectoral policy reforms and institution building that are consistent with a sustainable macroeconomic framework.

7. Planning Processes*ADF VI*

- Use strategic planning to introduce a more goal-oriented perspective in operations and ensure that crosscutting activities are properly focused and coordinated.
- Country strategies should be more operationally focused and strategically framed to support operations in a medium- to long-term perspective.

ADB has made advances in expanding and clarifying its policies for environmental and social concerns. Primary ADF lending for environmental protection and natural resource management during 1992–2000 was below expectations. However, ADB has supported some useful environmental and natural resource management work, but on a small scale. Greater public participation has helped enhance the design, operation, and monitoring of mitigation measures. Identification of major project impacts improved as environmental impact assessments and consultations with affected persons were made mandatory. Among the major reasons for these advances were (i) the strong emphasis given to social and environmental objectives in ADB's Medium-Term Strategic Framework (1995–1998), (ii) increased hiring of new ADB staff with skills in the social and environmental fields, and (iii) formulation of policies that provide guidance for improving the social and environmental design of projects in general.

ADF programs have addressed poverty issues usually through adjustments related to the implementation of policies such as rationalization of subsidies for food, utilities, or social services. An OED study on program lending noted that, in general, programs met their immediate targets. Total disbursements for completed programs were only 9% below the approved loan amounts. Although ambitious, containing a large number of conditions within a tight time frame, nearly all program conditions were met. Most programs took longer than planned to complete. Second tranche releases were often delayed from a planned 1–2 years into a third year, and not infrequently beyond. Many of these findings have been validated in this review of ADF-assisted programs.

Programs in the ADF VI period tended to have too many conditions, did not prioritize reforms, and sometimes lacked clear policy objectives. Learning from these early experiences, later programs under ADF VII had a stronger sector focus with program objectives prioritized and more clearly defined. The introduction of the sector development program combining investment components and policy actions has allowed greater flexibility for a more comprehensive reform package.

Some programs were of a high quality, establishing innovative models for reform and addressing some of the pressing issues in the Asian region such as privatization and industrial development, improving governance, and agriculture reform. The Asian and Russian financial crises blunted the impact of some of the program lending as the volatility of capital flows to emerging markets strained DMC fiscal management and the ability to implement difficult reforms. Program lending has had, and will continue to have, high relevance to the needs of DMCs, and has been moderately effective in supporting substantive legislative and policy changes.

One area where ADB made the greatest progress as an institution is in the strategic planning processes. The strategic framework that has been implemented directs planning and has articulated clear objectives. These objectives have been translated into country-based strategies in the country operational strategy, country assistance plan, and currently, country strategy and program documents. Crosscut-

Commitment	Actions and Progress To Date
<p><i>ADF VII</i></p> <ul style="list-style-type: none"> ● Make country strategies more analytical and selective. ● Broaden the consultation process in the preparation of country strategies and programs to encompass other concerned groups in the country such as local community groups and NGOs. ● Conduct a skills inventory within ADB to help identify comparative strengths and how resources can be reallocated to meet new challenges, such as improving public sector management and governance. ● Increase aid coordination encompassing multilateral as well as bilateral agencies. 	<p>ting activities have been clearly identified and developed into thematic objectives. In addition, the consultation process has expanded to encompass NGOs and other concerned stakeholders and aid coordination with multilateral and bilateral agencies has improved. The impact of these efforts has been felt in the design and implementation of projects. The result is that the reorientation of the institution has been successfully communicated from the planning and strategy level to the delivery of projects.</p>
<p>8. Improving Project Quality and Performance</p>	
<p><i>ADF VI</i></p> <ul style="list-style-type: none"> ● Improve the quality of projects by examining procedures for preparation, implementation, and supervision of projects. 	<p>In the ADF VI–VII period, there was a major overhaul of ADB’s project processing systems and procedures. Changes were instituted at the entry, processing, and postevaluation levels. There are clear indications that performance of projects implemented over the past 9 years has improved. In line with ADF recommendations, project selection, design, and implementation have become significantly more focused on impact, with more staff efforts directed toward incorporating policy and thematic content. The system does have some limitations and requires high-quality staff input to ensure its effectiveness.</p>
<p><i>ADF VII</i></p> <ul style="list-style-type: none"> ● Incorporate the development of monitorable and measurable performance indicators and annual performance assessments. ● Continue focusing on project quality and development impact of operations. 	
<p>9. Country Graduation</p>	
<ul style="list-style-type: none"> ● While recognizing that graduation from ADF was a complex and sensitive subject, donors emphasized that it needed to be addressed early to ensure that any changes in eligibility resulting from such a review would be relevant to ADF VII lending allocations. They, therefore, urged ADB to submit proposals to the Board of Directors for a graduation policy within 1 year of ADF VII becoming effective. 	<p>A graduation policy was adopted in 1998. The policy has been effective in facilitating country progression through ADF to ordinary capital resources. Further assessments are needed to identify and establish transparent trigger mechanisms for DMC progression and graduation. Evidence is less clear that this policy has been as effective in providing the basis for efficient access and eligibility mechanism to ensure that ADF reaches the poorest in the region.</p>
<p>10. ADF Allocation</p>	
<p><i>ADF VII</i></p> <ul style="list-style-type: none"> ● Allocation systems should ensure that scarce concessional resources are carefully targeted at those countries and projects where they are most urgently needed and most likely to be used effectively. Donors urged ADB to introduce a more formal allocation system, strengthening the link to more rigorous performance evaluation based on measurable indicators. 	<p>The process of moving to a formal, performance-based ADF allocation system was well under way during the ADF VI–VII period although the policy was officially adopted in 2001. ADF allocations during the ADF VI–VII period were based on less formal process of assessing DMC needs. Allocations under ADF VII were found to be efficient as they were in line with the indicative allocations under the formula proposed in the performance-based allocation policy.</p>

Appendix 4: Classifying Projects by Strategic Development Objective

In 1993, the Asian Development Bank (ADB) developed guidelines for classifying public sector projects and programs (see table). Each loan was allowed only one primary strategic development objective (SDO). In most cases, there was one secondary development objective as well, although in a few cases there were two. Classification was a sequential decision-making process. If a loan qualified as women in development, that was its assigned primary SDO. If not, it might be classified as poverty reduction, human development, or environment/natural resource management. If the loan did not meet the criteria for any of these four SDOs, it was classified as economic growth. There were no specific criteria for classification as economic growth. At the same time, the country focus and country strategies of ADB were strengthened. Project selection became partly a matter of achieving the SDOs and partly a matter of country-specific considerations. The SDO loan classification guidelines were revised and clarified in 1995. However, the essential criteria for loan classification remained the same. Governance, which toward the end of ADF VII, was to assume equal status with the other SDOs, was not yet mentioned in the 1995 guidelines. In 1998, ADB adopted a poverty reduction strategy. Poverty reduction became ADB's overarching objective and the other four SDOs were changed to themes rather than objectives.

ADF VI–VII Criteria for Loan Project Classification

Strategic Development Objective	Criteria During ADF VI–VII
Economic Growth	<p>Primary: No criteria. Residual after all other classifications.</p> <p>Secondary: None.</p>
Human Development	<p>Primary: Does not fit the women in development criteria, but more than 50% of project expenditures are targeted to education, health, population planning, water supply, sanitation, housing, and other basic human needs.</p> <p>Secondary: Less than 50% but more than 20% of expenditures.</p>
Poverty Reduction	<p>Primary: Two thirds of beneficiaries are poor, or more than 50% of expenditures are targeted to the poor.</p> <p>Secondary: One third of beneficiaries are poor, or more than 20% of expenditures are targeted to the poor, excluding mitigation of adverse effects caused by the project.</p>
Women in Development	<p>Primary: Two thirds of the beneficiaries are women, or more than 50% of expenditures are targeted specifically to benefit women.</p> <p>Secondary: One third of the beneficiaries are women, or less than 50% but more than 20% of expenditures are targeted specifically to benefit women.</p>
Environmental Protection and Natural Resource Management	<p>Primary: More than 50% of project expenditures are targeted to protect, improve, or conserve natural and environmental resources.</p> <p>Secondary: Less than 50% but more than 20% of project expenditures are for such purposes.</p>

Appendix 5: Progress on Millennium Development Goals

Goal/Indicator	South Asia		Mekong		ECA		SEA		Pacific		PRC		India	
	1990 ^a	2000 ^a	1990 ^a	2000 ^a	1990 ^a	2000 ^a	1990 ^a	2000 ^a	1990 ^a	2000 ^a	1990 ^a	2000 ^a	1990 ^a	2000 ^a
Goal 1: Eradicate extreme poverty and hunger														
● Prevalence of underweight children (under 5 years), % ^b	47.0	43.0	38.0	44.0	10.0	12.0	36.0	31.0	26.0	21.0	21.0	16.0	63.0	53.0
Goal 2: Achieve universal primary education														
● Literacy rate of 15-24 years, % ^c	67.2	67.6	66.5	79.8	88.4	99.4	96.4	93.6	76.9	75.9	95.1	91.7	65.2	68.4
Goal 3: Promote gender equality and empower women														
● Proportion of seats held by women in national parliament, % ^d	4.0	5.0	10.0	19.0	6.0	6.0	12.0	11.0	2.0	3.0	21.0	22.0	7.0	9.0
Goal 4: Reduce child mortality														
● Under-five mortality rate (per 1,000 live births)	120.0	82.0	109.0	93.0	79.0	71.0	79.0	44.0	59.0	48.0	49.0	40.0	123.0	96.0
● Infant mortality rate (per 1,000 live births) ^e	70.6	52.9	86.7	69.2	40.6	28.5	45.5	36.3	43.1	32.9	38.0	32.0	80.0	69.2
● Proportion of 1-year old children immunized against measles, %	72.0	76.0	50.0	73.0	86.0	93.0	72.0	75.0	59.0	78.0	98.0	90.0	56.0	50.0
Goal 5: Improve maternal health														
● Maternal mortality rate (per 100,000 live births) ^f	596.0	430.0	570.0	445.0	125.0	81.0	465.0	355.0	415.0	124.0	95.0	60.0	550.0	440.0
● Proportion of births attended by skilled health personnel, % of totals	38.5	34.3	53.3	55.5	69.3	93.3	42.5	56.0	74.1	82.3	51.0	67.0	34.0	43.0
Goal 6: Combat HIV/AIDS, malaria, and other diseases														
● Contraceptive prevalence rate (% of women aged 15-49) ^h	25.4	43.2	30.0	40.8	45.6	64.0	47.0	51.8	28.1	29.8	71.0	91.0	45.0	51.8
Goal 7: Ensure environmental sustainability														
● Proportion of population with sustainable access to improved water source, % ⁱ	69.0	85.0	42.0	41.0	66.0	75.0	79.0	82.0	75.0	78.0	71.0	75.0	68.0	88.0
● Proportion of population with access to improved sanitation, % ^j	21.0	56.0	26.0	46.0	76.0	82.0	68.0	75.0	66.0	69.0	24.0	38.0	13.0	31.0

ADF = Asian Development Fund, ECA = East and Central Asia, PRC = People's Republic of China, SEA = Southeast Asia.

^aData refer to most recent year available nearest to the year indicated in the column heading.

^bData available only for Kiribati (2000 only), Mongolia (1990 only), Papua New Guinea, Solomon Islands, and Vanuatu. 2000 data not available for Tajikistan.

^cPacific data for Papua New Guinea and Samoa only. Data not available for Bhutan, Kyrgyz, and Kazakhstan.

^d2000 data not available for Cook Islands, Marshall Islands, Tonga, and Tuvalu. 1990 data not available for Cook Islands, Federated States of Micronesia, Papua New Guinea, and Tuvalu.

^eData not available for Cook Islands, Marshall Islands, and Tuvalu.

^fData available only for Papua New Guinea, Samoa, Vanuatu and Solomon Islands (2000). 1990 data not available for Maldives.

^g2000 data not available for Bhutan, Cook Islands, Kiribati, Lao People's Democratic Republic, Maldives, Mongolia, Samoa, and Tuvalu. 1990 data available only for Mongolia and Kazakhstan, and not available for Marshall Islands and Tuvalu.

^h2000 data not available for Bhutan, Maldives, and Tonga. 1990 data not available for Maldives.

ⁱ1990 data available only for Mongolia; and not available for Cambodia, Federated States of Micronesia, and Tuvalu.

^j1990 data available only for Mongolia; and not available for Bhutan, Federated States of Micronesia, Papua New Guinea, Solomon Islands, and Tuvalu.

Sources: World Bank. 2001. *World Development Indicators*, CD-ROM. World Bank. *World Development Indicators*. Available: <http://www.worldbank.org/data>. United Nations. *United Nations Statistics*. Available: <http://www.unstats.un.org>. United Nations Development Programme. *Human Development Report*, various issues.

Appendix 6: Case Studies on Growth—Kyrgyz Republic

Corporate Governance and Enterprise Reform Program¹

This \$40 million program loan, along with an associated \$4 million technical assistance (TA) loan, was approved in 1997 and was the Asian Development Bank's (ADB) first program to focus explicitly on the issue of enterprise governance. The Program was launched in recognition of the fact that the Kyrgyz Government's otherwise reasonably successful corporatization and privatization, which were intended to facilitate the country's transition from Soviet-era central planning to a market economy, had not markedly improved enterprise efficiency. At the core of the problem was the need to establish the structures of modern corporate governance to more clearly define the rights and responsibilities of owners, managers, creditors, suppliers, and other enterprise stakeholders and to provide mechanisms to enforce governance principles and practices, which would create incentives for enterprise managers to improve efficiency within a rapidly opening economy.

The Program was designed to promote economic growth by eliminating constraints to improved efficiency within the enterprise sector by supporting reforms to (i) develop and institutionalize governance principles and practices, (ii) develop local expertise and capacity, (iii) elevate stakeholder awareness and understanding, (iv) impose financial discipline by eliminating budgetary support for state-owned enterprises, (v) prevent the creation of trade barriers and other impediments to competition, (vi) strengthen the legal framework for insolvency to enforce accountability and expedite the redeployment of assets from nonviable enterprises, and (vii) improve transparency by promoting the adoption of international accounting standards. In addition, the Program supported unemployment benefits and retraining for retrenched workers.

Under ADB's evaluation methodology, the Program was rated highly successful.² It was highly relevant. It addressed binding constraints to improved enterprise performance and was an essential component of the Government's overall development strategy. The Program was highly efficacious, and broadly successful in meeting the targets established by its logical framework. It was

highly efficient. By leveraging work being done in other sectors by ADB and using existing political requirements to enforce compliance with performance targets, the Program benefited from an efficiency of process. In addition, by bringing together a portfolio of reforms under one programmatic umbrella, the Program had greater impact than would have been achieved had individual reforms been pursued in isolation. It was likely to be sustainable. While the governance framework has been institutionalized, concerns regarding the Program's ultimate contribution to improved enterprise performance arise from (i) systemic weaknesses in the legal system; (ii) chronic tax evasion, which creates incentives for reduced, rather than increased, transparency in financial and operational reporting by enterprises; and (iii) ingrained rent seeking by some officials involved in tax collection, business licensing and regulation, and the judiciary. In terms of institutional development, the Program made substantial progress by reforming essential governance-related laws and regulations, inculcating norms and practices, developing local capacity, and changing the participatory attitudes of stakeholders.

The essential question for the Program—which illuminates a key lesson for future similar operations—is whether the governance framework it provided will actually lead to improved governance practices and ultimately to improved profitability and growth. For governance incentives to be meaningful, they must be reinforced by mechanisms of enforcement. While the basic transformation of incentives and attitudes envisaged under the Program has begun, the Program's ultimate success still hinges on the Government's sustained commitment to further reforms, the most important of which include addressing weaknesses within the legal sys-

¹ Loan 1546-KGZ(SF): *Corporate Governance and Enterprise Reform Program*, for \$40 million, approved on 25 September 1997. This case study was prepared independently by an international consultant, Mr. Christopher Bender. The full report is available at the Operations Evaluation Department (OED) web site—http://www.adb.org/documents/studies/corporate_governance_enterprise/corporate_governance.pdf.

² ADB. 2000. *Program Completion Report on the Corporate Governance and Enterprise Reform Program*. Manila.

tem, limiting undue political interference in the activities of private enterprises, strengthening institutional efforts to eliminate rent seeking, and promoting the development of the financial sector to enable it to play a disciplinary role in allocating investment capital.

The Program represents the first structured approach taken by any of the Central Asian republics to address the problems of enterprise governance. Although some work remains before the governance foundation developed by the Program will be finished—particularly with regard to harmonization of the legal framework—the Program can be credited with a number of accomplishments, including especially (i) providing a governance framework at a time when such a framework was crucially needed, (ii) substantially elevating the awareness of public officials, enterprise managers, shareholders, and the general public of the importance of corporate governance and the right of stakeholders to demand fiduciary responsibility from enterprise managers, and (iii) creating an institution (in the form of the Corporate Development Center) to continue the work of promoting improved governance beyond the existence of the Program and empowering the institution by placing it under the supervision of the Prime Minister's office. These were essential and valuable contributions.

Not surprisingly, the lessons to be learned from the Program's achievements are similar to those that can be learned from other successful projects, including the recognition that for development projects to produce useful outputs, they must be (i) designed to meet meaningful and attainable objectives, such as removing a known and binding constraint to growth (which was the essential objective of the Program); (ii) supported by adequate TA, with a strong emphasis on building local capacity; and (iii) actively embraced as a developmental priority by the borrower. Local ownership over the project is essential. The Program also demonstrates (i) the merits of an umbrella approach to reforming complex public policy issues (particularly those that involve large public education components and require the active cooperation and support of a number of governmental agencies and ministries); and (ii) the importance of identifying the proper executing agency to ensure the project receives both sufficient political support, as well as sufficient political attention. Finally, the Program highlights the importance of promoting policies that relax government-imposed distortions to market efficiency. This is particularly important in transition economies where the role of the state often remains inextricably intertwined with the activities of the ostensibly private economy.

The most important question yet to be asked, however, is whether the governance framework the Program provided will actually lead to improved governance practices by enterprise managers and, ultimately, to improved profitability and economic

growth. As stated earlier, the framework of modern corporate governance in any market economy establishes the incentives for enterprise managers to act as fiduciaries for the benefit of all of the owners of the enterprises they manage. For these incentives to be meaningful, however, they must be reinforced by mechanisms of enforcement, such as (i) the active and informed participation of shareholders in the governance process, (ii) the presence of competition and the absence of undue political interference in the activities of private enterprises, (iii) the disciplinary effectiveness of banks and the capital markets in allocating investment capital to profitable enterprises in preference to enterprises incapable of generating meaningful economic returns, and (iv) the existence of an efficient and impartial legal system to adjudicate claims and enforce accountability of enterprise directors and managers. Effective enforcement, in turn, depends on (i) the existence of acceptable standards for financial and operational reporting; and (ii) the transparency and impartiality of public officials, particularly those involved in tax collection, business licensing, and the judiciary.

The fundamental transformation of incentives and attitudes—as well as the basic change in the relationship between the state and enterprises—envisaged by the Program has yet to take place in the Kyrgyz Republic. This is largely because the mechanisms of governance enforcement remain underdeveloped. This weakness would impede the improvement of governance practices in the absence of further reforms. While some constraints to improved governance are structural and can be resolved in time with TA and targeted investment, the most important constraints can only be eliminated by the application of concerted political will. The Government must be committed to enforcing the governance requirements contained in the model corporate charter (and, now, in the proposed Joint Stock Company Law) even when the enforcement of these requirements may not be in its own financial or political interests.

In addition, the Government must recognize that the financial performance of joint-stock companies (JSCs) in which the Government remains the dominant shareholder will fall short of expectations as long as the Government's objective function includes conflicting objectives, such as job creation, and the Government tolerates poor financial performance by existing managers because their appointment reflects political patronage. While steps can be taken to improve the governance of such enterprises, the Government should eventually privatize them.

The effectiveness of the financial sector in encouraging improved governance will remain limited as long as enterprises do not view banks or the capital market as viable sources of investment capital. This problem is, to a large degree, self-reinforcing, as investors will remain reluctant to provide capital

as long as enterprises fail to disclose accurate and reliable financial data and managers fail to establish track records for acting in the interest of shareholders. The Government should continue to support development of the financial sector.

The objective of improving the governance practices of enterprise managers and efficiently and equitably restructuring or liquidating insolvent enterprises will be handicapped as long as governance standards cannot be enforced in the court system, either because of political interference or corruption. The Government should continue to support the reform of the judiciary.

The imposition of governance requirements—such as the production of timely and reliable financial statements—will not result in anticipated outcomes as long as enterprise managers have no practical reasons for complying with them. This is particularly evident when applied to the disclosure of financial data by enterprises that are successfully evading taxes. The State Tax Inspectorate should require the submission with tax filings of financial statements that follow international accounting standards. The Government should take steps to curb tax evasion and limit rent seeking by revenue collectors.

In addition to supporting these measures—privatization, financial sector reform, and judiciary reform—the aid community can help by supporting programs to (i) strengthen public governance (including, especially the curtailing of rent-seeking behavior by public officials involved in tax collection, business licensing and regulation, and the judiciary); (ii) strengthen financial sector governance (particularly with regard to limiting insider lending, improving auditing, and imposing meaningful civil penalties in the case of malfeasance); and (iii) facilitate enterprise restructuring (particularly with regard to improving the human capital of enterprise managers).

These issues appear to be adequately addressed in the design of the ongoing follow-on program.³

Power and District Heating Rehabilitation Project⁴

Reliable and efficient power and heat infrastructure is a basic requirement for macroeconomic stabilization and economic growth. ADB's strategy was to (i) support economic transition through improved energy supply reliability; (ii) enable savings in fuel imports; (iii) strengthen institutions and develop human resources in the power and heat sector; and (iv) promote policy reforms, including, in particular, tariff adjustment and energy sector legislation. This Project was a step forward in this direction.

The unbundling of Kyrgyz Energy into seven separate JSCs only in 2001 has made evaluation of the Project more difficult as many financial and operational divisions are still being sorted out. All the JSCs seem to be managed well from an operational view. The financial and commercial aspects

are more problematic. There appears to be a real difficulty in keeping meaningful accounts and lack of knowledge in most cases of international accounting standards. Commercial functions have presented more difficulties in making the adjustments required in the transition from a managed economy and should be monitored in the future.

The Kyrgyz Government has faced a number of difficulties in implementing the Project, including a severe financial crisis in 1998 and as a result was not able to provide required counterpart funding in a timely manner. The persistent level of poverty in the country continues to make it difficult socially to increase tariffs for energy consumption to levels that will make the energy sector financially viable. This is an area that should be emphasized to give consumers more incentive to conserve energy and to force more efficient choice in the use of energy types. Tariff increases are also essential to provide the energy sector with sufficient funding to assure long-term sustainability.

Various resolutions have been introduced to provide energy subsidy vouchers to low-income people, allowing overall energy tariffs to be increased. This approach would recognize the cost of providing electric power and heat to low-income citizens as a social cost rather than placing the financial burden on the energy sector as it does now.

ADB should follow events in the Kyrgyz Republic to ensure that energy tariffs continue to be increased. ADB must also monitor the safe storage of the replacement pipe for the Bishkek District Heating System to ensure that it is kept secure and installed on a reasonable schedule.

While many problems remain in the energy sector, the major short-term emphasis for both funding and TA should be in improvement of the low-voltage distribution networks. Most of the infrastructure of the four JSCs involved in distribution is old, obsolete, and in need of repair. Frequent outages persist and system losses including theft of electric power are estimated to exceed 35%. The Kyrgyz Republic should be encouraged to strengthen and enforce the energy law as regards the theft of energy.

In retrospect, the Project could have been better designed initially by including funds and TA for both the low voltage distribution network and for the international grid control system, which is located in Uzbekistan and controls the distribution of electric power among the participating states of Kazakhstan, Kyrgyz Republic, and Uzbekistan.

³ Loan 1860-KGZ(SF): *Second Phase of the Corporate Governance and Enterprise Reform Program*, for \$35 million, approved on 22 November 2001.

⁴ Loan 1443-KGZ(SF): *Power and District Heating Rehabilitation Project*, for \$30 million, approved on 6 June 1996. This case study was prepared independently by an international consultant, Mr. Ben Boyd. The full report is available at the OED web site—http://www.adb.org/documents/studies/power_heating_kgz/power_heating_project.pdf.

Future lending projects, which require counterpart funding, should also contain contingency plans for the possibility that these funds may not be available as promised.

Road Rehabilitation⁵

Soon after independence from the former Soviet Union in 1991, the Government identified the rehabilitation of the Bishkek-Osh road as the highest priority in the transport sector. That road connects two disparate regions of the country—the southern region containing the most fertile land in central Asia, the Fergana Valley, and the north industry corridor. The degradation of this road, which goes through the high mountain passes and valleys, has slowed commerce and increased transportation costs.

This Project, supported by \$50 million from ADF, was one of ADB's first ones in the Kyrgyz Republic and the first in the road sector. The Project was launched to rehabilitate about 135 kilometers (km) of key sections of the Bishkek-Osh road and provide equipment to improve maintenance and safety of the road. Consulting services for project design and construction supervision were also provided. The road runs through four of the country's six regions and serves about half of the population. It connects the two major urban centers of economic activity and population, which together account for over half of the country's gross domestic product (GDP) and 80% of industrial enterprises. Years of neglected maintenance resulted in serious deterioration of certain sections of the road that are periodically closed in winter months because of unsafe conditions. An all-weather road linking the two key centers of the country was deemed essential for the country's economic development and to improve transport safety. Policy and institutional reforms were added to enhance institutional capacity to address sector issues in a market economy.

ADB strategy at the time of project preparation, followed operational priorities that reflected greater emphasis on targeted investments addressing poverty reduction in parallel with efforts to stimulate broad-based economic growth that would enhance the role of the private sector. At the level of the country operational strategy and the country assistance plan, there was an acknowledged need to improve efforts to develop market mechanisms and foster growth while tackling the growing poverty effects of transition. The continued focus on growth efforts was deemed especially warranted given the dependence of the Kyrgyz economy on the former Soviet economy. As much as 30% of GDP was abruptly lost in 1991 as the Kyrgyz Republic declared its independence. Therefore, the Project with its focus on growth and its scope including two of the poorer areas in the country was relevant to ADB's country operational strategy. In addition, advisory TA attached to the Project provided much needed capacity building in urgent policy issues such as cost

recovery, road maintenance, and safety.

Based on evaluation carried out after its completion,⁶ the Project was highly relevant as it rehabilitated 135 km of the most important road in the Kyrgyz Republic. The Project was efficacious and met its objectives and will contribute even more to realizing the wider development goals after the two follow-on projects have been completed.⁷ The project funds for civil works were efficiently used. However, not enough road maintenance equipment was procured. The equipment should have included some efficient snow removal equipment instead of extra road construction equipment. The project outputs are fully sustainable, provided that road maintenance continues to be properly organized and financed and provided that the defects on some small sections of the road are repaired in a timely manner as agreed upon with the Government. Road maintenance issues are addressed in the follow-on projects. The Project has made a large institutional impact. Capacity building and policy support helped establish the Ministry of Transport and Communication during the reorganization of government. International competitive bidding and the practice of independent supervision of road works were introduced in the Kyrgyz Republic. The Project has greatly improved safety conditions compared with the situation before rehabilitation. This has been achieved through the use of concrete barriers, warning signs, and road markings. However, some hazardous situations remain on the project road, which are being addressed under the follow-on projects.

An economic reevaluation of the Project was carried out based on the methodology used at appraisal, comparing the with- and without-project cases. The primary differences between reevaluation and appraisal were (i) the revised economic costs were derived from actual financial costs, (ii) the construction period was 5 years compared with about 3.5 years anticipated at appraisal, and (iii) benefits were based on actual traffic data. The main sources of benefits were savings in vehicle operating costs and savings from diverted traffic. The revised economic internal rate of return was estimated at 9.7% versus 13.1% at appraisal. The de-

⁵ Loan 1444-KGZ(SF): *Road Rehabilitation Project*, for \$50 million, approved on 13 June 1996. This case study was prepared by N. Chakwin, Principal Evaluation Specialist, OED.

⁶ ADB. 2002. *Project Completion Report on the Road Rehabilitation Project in the Kyrgyz Republic*. Manila.

⁷ Loan 1630-KGZ(SF): *Second Road Rehabilitation Project*, for \$50 million, approved on 10 September 1998; and Loan 1853-KGZ(SF): *Third Road Rehabilitation Project*, for \$40 million, approved on 31 October 2001. The subsequent loans are part of the strategy to rehabilitate priority sections of the road in a sequential manner. This has proved to be a successful approach as there has been a great deal of learning by ADB and the Kyrgyz Republic during the Project, which can be applied to the design and implementation of the follow-on projects.

crease was attributed to higher economic costs, lower-than-expected traffic, and longer implementation period. The revised rate of return is below ADB's 12% threshold, but the uncertainty regarding future traffic levels due to implementation of the follow-on projects means that the rate of return could significantly increase in the future as the other sections of the road are rehabilitated.

The Project has had positive impacts that could not be quantified, including improvements in road safety, and development of local subcontractors and roadside businesses, such as small restaurants and vendors selling agricultural produce. A number of other positive developments in the project area may be partly attributable to the Project, including increased levels of employment and income in the project areas, and a noticeable reduction in prices for agricultural products in the two major cities connected by the road.

The Project was substantially implemented as planned. There were delays related to three factors: (i) financial—this was the first project in a new

member country and there were issues related to the contractor, which were eventually sorted out; (ii) technical—some of the most technically difficult sections of the road were included for rehabilitation under this first project and the work took longer than expected; (iii) planning—the works under the second project closed the main tunnel for almost 2 years for 18 hours every day during the construction season (April–November) and the road users avoided the tunnel due to its inconvenient opening hours (from midnight to 6–7 a.m.).

The selection and sequencing of road sections for rehabilitation could have been more forward looking to better maximize benefits and minimize disruptions to the traffic flow. In addition, some of the technical issues associated with temperature variation and altitude might have been better addressed at the design phase. Overall, the Project has been rated partly successful.

Appendix 7: Case Studies on The Pacific¹—Samoa and Vanuatu

Samoa

Financial Sector Program

The Program² supported financial sector reforms in Samoa. The attached technical assistance (TA)³ aimed at institutional strengthening of the central bank, the development bank, and the national provident fund, as well as corporatizing or privatizing eight state-owned enterprises.

One part of the Program was directed to monetary policy. In the Pacific small island states that use the currency of the United States, New Zealand, or Australia, macroeconomic policy is limited to tax and fiscal measures. However, the six biggest island states, including Samoa, issue their own currencies. This function calls for more sophisticated skills to manage monetary aggregates, interest rates, credit, inflation, and external accounts.

Also, in these very small markets, monetary policy can be overmanaged through direct interventions. Until 1996, the Government of Samoa fixed interest rates directly, set a ceiling on the amount of credit banks could provide, and required banks to hold 20–30% of their assets in liquid deposits, a quarter of which were noninterest-bearing deposits with the Central Bank. The result was serious distortions of Samoa's financial economy. High liquidity requirements, together with credit ceilings, eroded the incentives of banks to expand their deposit base and produced an "overhang" of uninvested funds. For considerable periods after inflation, interest rates on deposits were negative, and there were few alternative instruments for savers. Investors' decisions were distorted by interest rate rigidities and volatile inflation rates. Credit rationing resulted in the priorities of the Government and special interests sometimes dominating normal risk and rate-of-return considerations in the banks' allocation of capital. All these factors contributed to an excessive growth of unregulated nonbank lenders relative to the regulated banking sector. At the same time, the system did not allow easy adjustment of the Government's monetary policy. Excess bank liquidity made it difficult to ease policy, and the large unregulated sector of nonbank lenders made it difficult to tighten policy.

In January 1998, the Government began a financial liberalization program, removing interest

rate controls and credit ceilings, phasing out banks' liquid assets requirements, and starting weekly auctions of Central Bank securities as the main instrument of monetary policy. To facilitate this transition, the Asian Development Bank (ADB) provided funds under the Program, most of which were for general support of the national budget, but some, approximately \$1 million, was to cover the annual interest costs that the Central Bank incurred when it abandoned direct controls of interest rates and credit ceilings, and, instead, issued securities in competitive open-market operations. ADB's TA, along with TA from the International Monetary Fund, helped build the capacity of the Central Bank to manage the new system.

In the postliberalization period there have been some signs that the Program has been effective. For example, the private sector credit grew faster at an average rate of 13.6% in the 2 years after reform, compared with 10.6% in the 2 years before, which was a good sign given that inflation moderated at the same time.⁴ Average inflation was 6.2% per annum in 1996/97 and 1.5% in 1998/99. The commercial bank share of total lending, which was 14% below nonbank lending in 1997, is now about 15% higher. Interest rates have been noticeably more stable and positive, although a considerable spread between deposit and loan rates has remained, and loan rates are high relative to major markets. Lenders are now better able to factor credit risks into lending rates.

Over the 4 years of the Program, the Central Bank's interest rate on 91-day securities has varied between 5.25% per annum and 7.0% per annum, and has tended to remain around the middle of that range. The Central Bank has not yet aggressively

¹ These case studies were prepared independently by an international consultant, Mr. Kenneth Watson.

² Loan 1608-SAM(SF): *Financial Sector Program*, for \$7.5 million, approved on 19 February 1998.

³ TA 2989-SAM: *Institutional Strengthening of Government Financial Institutions*, for \$950,000, approved on 19 February 1998.

⁴ ADB. 2000. *Samoa 2000: Building on Recent Reforms*. Manila.

used interest rates to manage inflation targets, and, given the limited clientele for its securities (so far only the three commercial banks that operate in Samoa), the ability of the Central Bank to manage rates is still constrained.

Education Sector Project

The Project⁵ supported physical rehabilitation of 16 schools in Samoa, while the attached TA⁶ was for in-service teaching training in these schools.

In the past, other aid agencies such as the European Union Development Agency and Japan International Cooperation Agency had used a shared-cost model for microprojects in Samoa, whereby the village contributed about one quarter of the costs, in cash or kind, for small construction projects such as the installation of a water tank. Typically the village contributed labor in preparing and cleaning up the site and simple building materials. ADB decided to take a similar approach, although with the possibility of a full or part waiver of the local contribution if circumstances proved this necessary. Of the 14 resource agreements concluded with school committees, five received complete waivers, and nine partial waivers. The share of costs borne by the local community, where the waiver was partial, varied between 5% and 16%. There were no cash contributions; rather, all was in kind. However, the cash equivalents were substantial. The in-kind contributions tended to include land (typically owned communally), demolition and fill costs, clean up, fencing, walkways, and, in some instances, power and water supply to the site. The need to negotiate resource agreements between the local school committee and the Department of Education in each instance led to delays in project implementation, but probably was not the most important factor. As of September 2002, 3 of 16 subprojects were complete, one of which was designed before the loan was granted.

For several reasons, the shared-cost approach has proved of limited value in this case. First, the scale and sophistication of construction did not lend itself to a self-help approach. The construction costs were too large for villages to fund 25% of the cost. Many of the materials and types of labor needed were available only from commercial contractors. The rehabilitation involved extensive upgrading or complete reconstruction of school buildings to meet building code standards for the first time. In some cases, the Project involved the construction of special facilities such as libraries, teachers' rooms, and classrooms designed to accommodate agricultural studies or food and textiles studies under a new curriculum. School fees are a major source of school resources in Samoa, but they were typically already fully committed and could not be tapped for capital investment. Another factor that worked against the self-help approach was that ADB's contracting rules exclude the possibility of informal "mates rates" work on the project sites.

Second, the school committees were made up of people who represent the group that "owns" the school—chiefs and other people important in the local village, but not necessarily parents. In fact, parent and teacher associations are a recent innovation in Samoa. The composition of the school committee was particularly relevant in those cases where the school drew pupils from several villages. The committee might have been able to find volunteer inputs from the village that "owns" the school, but were less likely to be able to mobilize proportionate contributions from other villages. On the other hand, two-tier school fees for in-village and out-village pupils are not uncommon. All in all, the traditional concepts of village ownership of the local school, and ideas about who has "speaking rights" in regard to the school, have been important factors. ADB staff input is large for the amount of construction involved, but reflects the extensive discussions and the careful tailoring of the sub-project design to local "owners" that is necessary in the Samoan context.

These issues were particularly sensitive since Samoa is in the midst of implementing a school zoning system, which requires relocating large numbers of pupils from overcrowded but prestigious schools in the capital Apia to their home community schools. In fact, the first ADB subprojects to be funded and completed all relate to this pupil redistribution effort. The rural schools among the subprojects are yet to be reached.

Vanuatu

Urban Infrastructure Project

The Project⁷ covered a 5-year program of road and bridge rehabilitation, port rehabilitation, water supply, drainage and sanitation in Port Vila and Luganville, the two main towns in Vanuatu. The attached two TAs⁸ draft three key pieces of legislation⁹ and produce a sanitation master plan for Port Vila.

Although physical implementation took 3 years to get substantially under way, a good part of the works were begun in 2000 and finished before the December 2001 loan closing date. The scope of the

⁵ Loan 1752-SAM(SF): *Education Sector Project*, for \$7 million, approved on 5 September 2000.

⁶ TA 3498-SAM: *Education Support*, for \$820,000, approved on 5 September 2000.

⁷ Loan 1448-VAN(SF): *Urban Infrastructure Project*, for \$10 million, approved on 27 June 1996.

⁸ TA 2596-VAN: *Urban Growth Management Strategy for Port Vila*, for \$600,000; and TA 2597-VAN: *Sanitation Master Plan for Port Vila*, for \$360,000; both approved on 27 June 1996.

⁹ The Environmental and Resource Management Act, the Water Resources Management Act, and Building Regulations.

works was adjusted in two ways. First, the contractor engaged to resurface Luganville roads pointed out that the improvements would not be sustainable unless substantial improvements in drainage around the road were completed first. Second, in 2001 the scope of the whole Project was reduced when it became apparent that the funds available would be inadequate for full completion. Specifically, the sanitation component and the Port Vila traffic intersection improvements were put on hold, pending allocation of counterpart funds.

The Project had significant achievements. Most of the works, with a few significant exceptions, were completed and important work in regard to environmental and water resource regulation and building codes was undertaken. However, the late changes in scope highlighted weaknesses in estimating initial costs and in project monitoring. Reporting completion percentages is unhelpful if delays and potential overruns are accommodated by scope reductions. Similarly, the practice of calling an underrun “savings” is also unfortunate when the components that are completed have exceeded their estimated costs and the “savings” are only due to scope reductions.

The Government did not comply with several key loan covenants that were intended to ensure the long-term sustainability of the works, and included changes to the water tariff structure in Luganville, corporatization or privatization of the Luganville water supply authority, changes to road tax policy to generate funds for maintenance, and changes to port operations. Failure to comply with the covenants raises questions of priorities and process. If the covenants were essential, then there should probably have been a more detailed process of steps laid out to comply with them and disbursements linked to those steps. Among the steps there should have been opportunities built in for modifying a covenant if necessary. The failure to honor the covenants raises the question whether some of them were too specific, given that a clear evidence-based consensus had not yet emerged on the best way to proceed.¹⁰

Comprehensive Reform Program

The Program¹¹ and the attached TAs¹² were approved under crisis conditions. Over the previous decade the Government’s financial situation had deteriorated steadily, with large fiscal deficits that started with development fund overspending, and spread to recurrent expenditures. At the same time government revenues were declining, reflecting failures of tax policy and enforcement, and patronage appointments were eroding the quality of the public service.

The crisis came to a head in January 1998 when revelation of details of certain investments by the Vanuatu National Provident Fund led to serious riots in the capital. The Government stood by its guarantee of Fund deposits, but at the cost of a fiscal

deficit that reached 12.7% of GDP, with dramatic implications for inflation and the balance of payments. A run on the currency began in March 1998. At the end of that month a new government assumed office, and opened negotiations with ADB in regard to a loan. The loan involved disbursement of a first tranche of \$10 million to help restore liquidity to collapsing government finances. This and two further tranches of \$5 million were contingent on certain commitments by the Government for policy and institutional changes.

The Program covered a broad range of reforms, encompassing three key areas of the economy:

- (i) In the financial sector, the Government dissolved the Vanuatu Development Bank and recapitalized and restructured the National Bank and the Provident Fund. Nonperforming investments were segregated into an Asset Management Unit.
- (ii) The public sector fiscal regime was restructured with the introduction of a 12.5% value-added tax to replace a number of other indirect taxes.
- (iii) The public sector was reformed with the introduction of a merit-based professional cadre of department and agency heads, under life appointments (recently changed to 3-year performance contracts), with a changed relationship with the Minister. The Government also undertook to reduce the size of the public service by 10–15% and to withdraw from its excessive ownership of commercial enterprises.

This ambitious reform agenda was supported by grants from a number of sources who had a long-term interest in development in Vanuatu. However, each source came with administrative and political models that reflected its own background and historical experience. This proved problematic in a situation where fundamental changes in governance were being attempted under crisis conditions and where political and administrative friction had arisen during the incorporation of the English-French condominium into the new nation. What was needed exceeded the normal coordination of like-minded sources and stretched ADB’s governance expertise.

The conditions agreed to by the Government under the Program were extensive and controversial. One result was that program implementation

¹⁰ The requirement that Luganville water authority switch to a two-tier water tariff structure perhaps falls into this category.

¹¹ Loan 1624-VAN(SF): *Comprehensive Reform Program*, for \$20 million, approved on 16 July 1998.

¹² TA 2984-VAN: *Institutional Support to Central Agencies for the Comprehensive Reform Program*, for \$630,000, approved on 23 January 1998; and TA 3046-VAN: *Institutional Support to Central Agencies for the Comprehensive Reform Program (Phase II)*, for \$1.2 million, approved on 16 July 1998.

became a highly charged political matter. When the Government changed about 18 months after loan approval, the implementation agenda and timetable were set back. In retrospect, ADB may not have moved fast enough immediately after loan approval to disburse funds and to encourage the immediate performance of agreements.

Four years after loan approval, it seems that the Program has made a significant difference to the political economy of Vanuatu, although it is impossible to tell what reforms might have been made if the financial crisis had been allowed to run its course without external intervention. Key reforms that were achieved include introducing a value-added tax, downsizing the public service, strengthening the

merit principle within the senior public service, and some improvement in fiscal discipline. Nevertheless, fiscal deficits remain high, the Government has not withdrawn significantly from involvement in commercial enterprises, and the quality of social services and hopes of spurring development in agriculture and tourism have not borne fruit. Private investment remains low because of political uncertainty, lack of security of property, and structural problems in finance and regulation. On balance, the Program supported some important, but fragile, policy and institutional reforms, under extreme stress, but the work may have been more effective and more sustainable if there had been a narrower focus on the highest priorities.

Appendix 8: Environmental Activities

Environmental Mitigation Measures

The Asian Development Bank (ADB) has made good progress in integrating environmental considerations through improved project design and mitigation measures in all types of projects. The Operations Evaluation Department (OED) has examined issues related to power projects in two studies: one on environmental effects of hydropower projects,¹ and the other on environmental mitigation measures in thermal power projects.² Some of the projects included in the studies³ were started before a number of relevant policies and guidelines were adopted.⁴ In the hydropower projects, the most significant environmental impacts identified were associated with migratory fish species (see Box). In the thermal power projects, several shortcomings occurred, most of which could have been avoided or compensated with more diligence on the part of the project proponents, government agencies, and ADB. Several of the study projects experienced waste (ash) disposal problems due to reduced demand,

overestimation of demand for environmental improvements generated by the plant (i.e., district heating, wastewater, or sewage treatment), and inadequate space to install equipment required by new regulations (e.g., flue gas desulfurization). Identification and mitigation of project impacts improved with later study projects.

The environmental impact assessment process required and supported by ADB has often resulted in successful identification and mitigation of major environmental impacts. The study projects were generally in compliance with environmental protection regulations and guidelines of the respective developing member country, even though the mandate and capacity of environmental management agencies to regulate and monitor mitigation measures might have been low. Environmental personnel, management plans, and monitoring programs had variable success in sustaining environmental mitigation measures during the operational phase in the study projects. Mitigation measures requiring foreign exchange were usually financed by ADB, but related local expenditure for maintaining and monitoring mitigation measures were often delayed until the plant was well into the operational phase. Provincial environmental management agencies often had insufficient capacity, training, means, or the incentive to ensure compliance with regulations.

In agro-industry projects, positive impacts included the prevention of soil erosion, the introduction of new cultivation practices, and retention of

Mitigation Measures of Hydropower in the Lao People's Democratic Republic

The Nam Song Hydropower project had some negative environmental effects, such as reduced water flow to some villages and potential impacts on fisheries. The villages were supplied with wells, and a fish-stock program for the reservoir was successfully implemented. Adding roads and electrifying the villages have been an added bonus of the project. Environmental impacts of the Theun-Hinboun Hydropower project included loss of a fish passage for upstream migration, reducing fish populations. Irregular water flows and turbidity resulted in (i) migratory problems for particular species of fish, (ii) declining harvests in the lower areas near the Mekong, and (iii) increased access and mobility for fishing in some areas and difficulty in accessing other areas during the dry season. As the Government had insufficient funds, the power company provided support to mitigate some of these adverse impacts. A regulating pond was constructed during implementation to reduce the impact of the variable water flows on soil erosion. Similarly, the power company paid to relocate a village shrine. During implementation, the power company commissioned several studies on irrigated agriculture, rural development, and fisheries development to help the Government prepare a structured development plan for improving the incomes and lifestyles of affected people. Experience from these two projects and new policies resulted in successful mitigation works and provided compensation for alleviating and remedying negative social and environmental consequences in the Nam Leuk Hydropower project. Special actions included careful control of the contractor's and loggers' activities; designing and maintaining an attractive reservoir with undisturbed forest; good quality water; and relocated families were compensated for the loss of croplands, property, and assets in consultation with the people and to their satisfaction.

¹ ADB. 1999. *Special Evaluation Study on the Social and Environmental Impacts of Selected Hydropower Projects*. Manila.

² ADB. 1998. *Special Evaluation Study of the Environmental Mitigation Measures in Selected Bank-Financed Projects*. Manila. Two urban development projects were included in the sample along with four thermal power projects.

³ While the studies included projects in non-Asian Development Fund (ADF) recipient countries, lessons learned and recommendations from these studies provided feedback into subsequent lending to the power sector and are, therefore, relevant.

⁴ Specific policies and guidelines were approved in 1995–1998 for energy, involuntary resettlement, forestry, fisheries, and indigenous peoples.

soil microflora and moisture through preservation of cane trash. The effects of integrated rural development projects on the environment were more mixed. The positive impacts comprised (i) soil conservation and reforestation, (ii) reduction in flooding, (iii) mitigation of soil erosion, and (iv) controlled migration and settlement. These benefits were tempered by negative effects including (i) landslides along constructed roads, (ii) encroachment on forests due to expanded road infrastructure, (iii) degradation of watersheds due to forest encroachments and lack of proper watershed management, and (iv) river channelization caused by the installation of flood dikes and drainage systems along riverbeds.

A project in Pakistan⁵ is a good example of both positive and negative project impacts of such integrated rural development projects. The project contributed to improvement of the environment through its forestry subcomponent. An area of 29,367 hectares was afforested, equivalent to 3% of the total project area. However, the rural roads located in the mountainous terrain of one district required a substantial volume of soil cut and fill, which caused landslides along the roads. The environmental assessment for the roads was endorsed by the province's Environmental Protection Department, which overlooked this adverse effect. Further efforts were needed to identify mitigation measures to stabilize the cut and filled surfaces. Other activities under the project did not have any significant environmental effects.

Many of the irrigation projects or project components were environmentally neutral or positive in addressing concerns such as irrigation and drainage for agriculture. The problem of soil erosion is complex. Reconstruction and resectioning were generally successful in reducing erosion and in protecting agricultural land from intrusion of saline water. However, blocking of traditional water routes in some areas has obstructed navigation. One project in the water sector⁶ had positive environmental impacts and contributed to overall health improvement in the project area.

Road projects were more problematic for the environment. One major environmental contribution of road projects was the reduction in dust particles and improved air quality at roadside areas. The installation of drainage structures and raising of embankments accompanying road construction were seen as preventing soil erosion in some countries and contributing to reduced land fertility in others as a result of the interruption of normal flooding.⁷ Also in some projects, like the Champassak Road Improvement Project,⁸ the contractors responsible for cleaning up the borrow pits, removing spoils, replacing topsoil, and leaving the area in a safe and tidy condition were negligent. At some of the bridges where the construction required embankments that entered waterways, spoils and oil spillage covered the waterways. In addition, the

clearing of a section of forest attracted the attention of the World Conservation Union. A detailed environmental action plan was developed and the borrow pits were converted into fishponds as requested by surrounding villages. During construction, additional works were undertaken to minimize the effects of erosion on the areas immediately adjacent to the project works.

The role of public awareness and public participation differs by country, within sectors, and by projects. However, studies generally show that greater public participation improved the design, operation, and monitoring of mitigation measures. Increased transparency led to greater flexibility in adjusting measures to suit changing circumstances. Identification of major project impacts improved with later study projects as environmental impact assessment preparation and consultations with affected persons were introduced. Among the major reasons for these advances were the (i) strong emphasis given to social and environmental objectives in ADB's Medium-Term Strategic Framework 1995–1998, (ii) increased hiring of new ADB staff with skills in social and environmental fields, and (iii) preparation of policies that gave guidance for improving the social and environmental design of projects in general. ADB has made significant advances in expanding and clarifying its policies for environmental and social concerns.

Technical Assistance

There has been extensive technical assistance (TA) to support many facets of environmental activities. In 1995–2000, ADB provided 149 TA grants totaling \$122 million for environmental capacity building, with ADF countries receiving 61 TA grants for a total of \$79 million. Of these TA grants, 118 were country-specific and 31 were regional in scope. The grants covered six areas of activities: management, institutions, human resources, policy, planning, and legislation.

TA grants to improve natural resource and environmental management accounted for 70% of the total amount. They covered a wide range of natural resource and environmental management concerns that had been changing over the past 15 years. The number of grants focusing on environmental impact assessments significantly decreased in the last 8 years, while assistance for natural resource management support increased. The focus on environ-

⁵ Loan 1179-PAK(SF): *North-West Frontier Province Barani Area Development Project*, for \$32.8 million, approved on 24 September 1992.

⁶ Loan 1235-SRI(SF): *Second Water Supply and Sanitation Project*, for \$40 million, approved on 17 June 1993.

⁷ ADB. 2003. *Country Assistance Program Evaluation for Bangladesh*, Supplementary Appendix. Manila.

⁸ Loan 1369-LAO(SF): *Champassak Road Improvement Project*, for \$48 million, approved on 31 August 1995.

mental management paved the way for the transfer of environmentally sound technology and assisted countries in setting standards, introducing assessment and monitoring activities, and training a large number of government counterpart staff. The need to increase management and monitoring skills has been one of the crucial factors pointed out in OED's evaluations of activities in this area (footnote 2).

Institutional development and strengthening was the second largest category, receiving about 15% of TA grant funds. These were mostly directed toward strengthening environmental units or institutions. Although almost all of the TA projects involved training and skills development, about 7% of grants were directed specially to human resource development activities such as environmental monitoring and management; environmental planning; impact assessments; environmental law; implementation of the Kyoto Protocol and Clean Development Mechanism; transboundary atmospheric haze pollution; energy, soil, and water conservation; and wastewater treatment. Apart from government officials, people trained under ADB's TA grants included environmental journalists in the region, community volunteers, and staff of development banks.

About 4% of the TA was directed to develop or reform country policies that impinge on environmental and natural resource management. ADB's TA grants in this area sought to strengthen or develop land use and land tenure policies, promote cleaner production policies, and draft sector development policies that were environment-related and forestry policies.

Environmental planning was a neglected area in relative terms. Of the total TA funds, only 2% was directed toward planning. Planning has three dimensions—strategic, physical, and regional—and is critical to environmental capacity building. It is particularly the physical planning related to urban development, transport, and industrial zoning where TA support needs to be strengthened. TA support for environmental legislation also accounted for another 2% of the total. This was aimed primarily at strengthening environmental standards and enforcement policies, developing and implementing a pesticides regulatory framework, and formulating provincial legislation on environmental protection and natural resource conservation.

The environment-related TA activities have been, on the whole, generally successful. Recommendations and lessons learned from OED evaluations⁹ indicate that pursuing environmental capacity building in emerging sectors in developing countries is difficult. Extensive diagnostic assessments must be done before the TA can be really effective, and environmental issues need to be examined in the context of the root causes of environmental degradation such as poverty, population pressure, overconsumption, and illiteracy. Resources should be focused accordingly.

⁹ ADB. 1997. *Technical Assistance Performance Audit Report on Selected TAs in the Environment Sector to the People's Republic of China* (TAs 1436, 1690, and 0987). Manila; and ADB. 2001. *Technical Assistance Performance Audit Report on Selected Technical Assistance in the Environment Sector in Mongolia* (TAs 1647 and 2208). Manila.

Appendix 9: Case Studies on Human Development—Sri Lanka

Second Health and Population Project¹

This \$33 million project was launched in 1993 in response to a shift in government focus from local or primary to the neglected secondary hospitals. The authorities were concerned that the tertiary teaching and general hospitals at the district towns were overutilized and overburdened. The objective of the Project was to strengthen the midlevel units to increase patient confidence and increase both inpatient and outpatient use with a concomitant decrease in the patient loads at the larger tertiary facilities.

The project-aided hospitals were to receive a package of support including civil works (new facilities for outpatient care, administrative offices and staff quarters plus rehabilitation of existing structures) and emergency treatment packets to enable them to respond more effectively when life-threatening situations were presented (ambulances, telephone, and basic equipment). The Project invested an average of over \$280,000 in each secondary hospital. Originally 35 sites were to receive support, but in the end an additional nine units were assisted. To strengthen the capacity of the health providers, initially in the project-aided facilities and then nationwide, the National Institute of Health Sciences received substantial assistance consisting of almost \$1 million for civil works (classrooms, hostels, clinic) as well as technical assistance (TA) to develop a curriculum and upgrade trainer capacities.

The implementation of the Project was found to be generally favorable, but, in retrospect, its design was less favorably viewed. Using the five criteria of the Asian Development Bank's (ADB) evaluation methodology, the Project was found to be partly relevant considering patient behavior and the inability to modify behavior patterns. Although more facilities received assistance than originally programmed, there was no evidence that the referral system and utilization rates improved as a result of the project investment. Therefore, the Project was judged to be less efficacious. For the amount of resources invested in approximately 10% of the secondary hospitals in Sri Lanka without measurable results, the Project was not considered cost-effective and was classified as less efficient. Financial constraints and a lack of procedures to address maintenance problems raised concerns about the

sustainability of the project inputs and resulted in a less likely rating. Finally, there was little evidence of institutional development as a result of the Project, meaning that policies such as health care finance and in-service training were not modified, which made it difficult for project objectives to be achieved. Taking all five aspects together, the Project was rated partly successful.²

The lessons learned from the Project include the need to focus special effort on project preparation and design. It is also essential to ensure that an enabling environment and supporting government policies are in place so that project objectives can be achieved. Another lesson is the importance of identifying appropriate indicators during the project preparation phase and monitoring them during implementation. This keeps the effort on track and allows modification as required. Having a close relationship with previous health sector operations is also important. Although the formulation of the Project was guided by government policy changes in the early 1990s, the community-based efforts pursued in its predecessor may have had a greater long-term impact on the health status of the population.

The success of a project depends on the effectiveness of its preparation and design. For a social sector intervention such as the Project, in-depth analysis is crucial in the project design and formulation stage. For example, in the attempt to modify patient behavior toward health facility use, it is essential to ascertain what motivates the target population and determine what variables influence the choice. Intensive surveys, similar to methodologies used in marketing studies, can be used. Such studies will identify perceived needs and problems that will help determine how project resources can be programmed most cost-effectively.

Indicators of project outcomes and impact should be identified during the design phase, and

¹ Loan 1189-SRI(SF): *Second Health and Population Project*, for \$26.1 million, approved on 17 November 1992. This case study was prepared independently by an international consultant, Mr. David Pyle. The full report is available at the Operations Evaluation Department (OED) web site—http://www.adb.org/documents/studies/health_population_sri/health_population.pdf.

² ADB. 2000. *Project Completion Report on the Second Health and Population Project in Sri Lanka*. Manila.

strategies and methodologies to track performance developed. Advances made recently by ADB in this regard will greatly enhance the ability of project managers, both in the implementing agency as well as ADB, to determine in midcourse whether satisfactory progress is being made to achieve project objectives or if modifications are required to improve performance. It may be advisable to outsource the outcome/impact monitoring function to ensure that it is done properly and in a timely manner.

ADB assistance should be cumulative and should build on preceding projects. Thus, the lessons learned in one can be taken into account in the follow-on effort. In the case of Sri Lanka, difficulties in implementing the first project and a shift in national health policy resulted in a new focus on the strengthening of secondary hospitals. Nonetheless, the Government's continued interest in community-based health care and ADB's priority to community participation and reaching those most in need could well have supported an expansion of the health center network and would have achieved more in terms of impact at a lower cost. Integrating the preventive/promotive care with a modicum of curative care (e.g., integrated management of childhood illness) at the health centers at the grassroots level would have been a valuable contribution to the welfare of the most needy segment of the population and helped reduce the extremely high neonatal mortality rate.

ADB should identify what is required for the proposed project design to be effective and sustained, and then ensure full commitment of the executing agency and government to provide the necessary enabling environment. If the necessary policy changes are not forthcoming, ADB should either not proceed with the project or modify it to include a strategy that is not dependent on such changes.

Secondary Education Development Project³

This \$41 million project sought to improve access to quality secondary education in Sri Lanka and thus lead to greater employment opportunities for students in the rural districts of the country. The primary objectives were to improve the quality of Sri Lanka's secondary education for years 6–11 and provide more equitable access to it, particularly in rural areas. The Project was designed to assist the Government in four specific areas: (i) revisions to curriculum, (ii) improvements in teacher education and training, (iii) reforms in education and examination systems, and (iv) improvements in school administration and academic learning by providing physical infrastructure and equipment. In total, refurbishing and upgrading some 178 schools took place under the Project.

Revisions to curricula focused on changes to science, mathematics, computers, languages, and rural technology education programs. Improvements to teacher education and professional development

were designed so that curricular changes could be implemented more effectively in the classroom. Reforms to examination and testing included new structures and mechanisms to establish accreditation standards and new buildings, equipment and computers at the National Evaluation Testing Service (NETS). The development and upgrading of schools component addressed the strengthening of school management and upgrading of selected schools including the introduction of computer resource centers. For all four components, consulting services, fellowships, study visits, and benefit monitoring and evaluation of project activities were provided.

The implementation of the Project was exemplary. Both the Ministry of Education and Higher Education (MEHE) personnel and ADB project office personnel carried out their responsibilities and duties in a timely and competent fashion. The project design was both timely and effective in meeting the needs of the secondary education system. The quality of secondary education for grades 6–11 has improved and more equitable access to quality secondary education is now available, particularly in rural areas. Curriculum teaching and learning materials, teacher education and training, evaluation of the education system, and school improvements in physical infrastructure, equipment, and computers have all been strengthened. The NETS has a new building with a streamlined computer system to accommodate about 0.8 million candidates per year. As a result, the turnaround time between the taking of exams and results was reduced from 10 to 6 months during the course of the Project and more recent information reflects a decrease in this time to approximately 3 months. The 30 computer resource centers created under the Project are all now self-supporting and provide almost 100,000 students with computer education each year. The linkages with the follow-on project⁴ ensure that the initiatives started under this Project will be reinforced and expanded. Institutional development and capacity building under the Project have consequently been highly effective. According to the five criteria of ADB's evaluation methodology, the Project was found to be highly relevant, efficacious, highly efficient, likely to be sustainable, and having substantial institutional development impact. Overall, the Project was rated highly successful.⁵

³ Loan 1247-SRI(SF): *Secondary Education Development Project*, for \$31 million, approved on 24 August 1993. This case study was prepared independently by an international consultant, Mr. Bruce Mathews. The full report is available at the OED web site—http://www.adb.org/documents/studies/secondary_education_sri/secondary_education.pdf.

⁴ Loan 1756-SRI(SF): *Secondary Education Modernization Project*, for \$50 million, approved on 12 September 2000.

⁵ ADB. 2001. *Project Completion Report on the Secondary Education Development Project in Sri Lanka*. Manila.

Although the project design was well thought out, no baseline data was established at appraisal. Similarly, no logical framework was set at project preparation as it was not required in 1993. Indicators of project outcomes and impact should be identified during the design phase, and strategies and methodologies to track performance developed. Advances made recently by ADB in this regard will greatly enhance the ability of project managers, both in the implementing agency as well as ADB, to determine during project implementation whether satisfactory progress toward achieving project objectives is being made, or if modifications are required to improve performance.

One expected outcome of the Project was greater access to secondary education for needy students in the rural areas and a resulting increase in opportunities for employment. Impact of the Project on employment for students, however, has not been assessed or evaluated. It can be assumed that improvements to the curriculum in core subjects such as mathematics, science, computer science, and English will result in more employable students; however, this was not statistically verified. In education projects of this nature, follow-up tracer/evaluation studies, even on a limited basis will still provide an indication of project impact on student employability and program relevance.

The benefit monitoring and evaluation report for the Project addressed outputs from the four project components and provided a very positive assessment of achievements in line with stated goals and expected outcomes. At the same time, however, there was a wealth of information and statistics produced by MEHE, particularly the Department of Examinations of NETS, which was not analyzed or commented on. A thorough analysis of the statistics available for project districts could indicate the impact of the Project on student achievement. If the Project was primarily intended to improve academic achievement for poor students in the rural districts of the country, then the success of the design should be reflected in the improved performance.

In the future, ADB may be better served if it focuses its project design on a few inter-related objectives and institutions. As this was the first ADB-assisted Project in Sri Lanka's general education system and no other aid agencies were involved until that time, there was a tendency to overdesign the

Project, covering curriculum and materials, teacher training, and examination reforms as well as attempting to alter schools resource distribution. Consequently, investments were scattered too thinly over many institutions.

A strong and effective project implementation unit is essential to successful project outcomes. The Project was fortunate to have such a unit that coordinated the multiple aims and institutions (including aid agencies), and is responsible for the follow-on project. A strong unit is essential particularly when multiple agencies are involved in project activities.

Ensuring the sustainability of new institutions such as NETS requires a series of investment requirements over the medium term. Although major improvements were achieved at NETS under the Project, no institution can sustain efforts indefinitely without additional support: staff are always moving and new innovations in testing procedures need to be deployed, and follow-up training of teachers in school-based assessment is required. Consequently, follow-on projects are needed to deepen support. Additional support also acts as an incentive for executing agencies to perform well, knowing that further support is available.

Improving the overall quality of education is a complex process that requires a correct mix of investments in civil works, equipment, curriculum development, and learning materials combined with a strong component for capacity building. Capacity building allows various institutions such as NETS, MEHE, and schools to better organize and manage these learning inputs. The Project showed that providing guidebooks and training principals, teachers, and community leaders are a prerequisite to raising awareness and gaining local support for quality improvements both in the school and in the community. Physical inputs alone are not sufficient to improve education. MEHE, NETS, and the secondary schools need to build awareness through training to change the attitudes and thinking of students, teachers, and parents. Due to lack of time, the Project reduced its inputs to capacity building and thereby minimized awareness for change. The follow-on project will devote more resources to training administrators and community leaders to better understand and support quality improvements in schools.

Appendix 10: Case Studies on Poverty—Viet Nam

Irrigation and Flood Protection Rehabilitation Project, Red River Delta Water Resources Sector Project, and Rural Credit Project¹

These projects were prepared during the early phase of the Government's renovation (*doi moi*) reforms following the prolonged civil war and subsequent period of centralized planning and collectivized agriculture that had resulted in low incomes and widespread poverty. The Irrigation and Flood Protection Rehabilitation Project (IRP) was the Asian Development Bank's (ADB) first lending operation after Viet Nam's reunification. It was followed by the Red River Delta Water Resources Sector Project (RDP), and the Rural Credit Project (RCP). IRP and RDP supported the Government's water resources investment plan that emphasized rehabilitation of priority infrastructure, while RCP addressed acute supply constraints to meet the demand for credit unleashed by the reforms.

RCP was to help increase production and diversify agriculture to generate employment. IRP was to rehabilitate the Hanoi flood protection dike and priority structures in Song Chu and North Nghe An irrigation systems. RDP was to improve irrigation and drainage structures in the Red River Delta. RCP provided credit lines of \$32 million for medium-term subloans (1–5 years) especially for agroprocessing, and \$14.8 million for short-term subloans (less than 1 year) including \$2 million targeted for poverty subloans. While implementation was generally satisfactory, the design of all three projects was less than satisfactory. First, they did not directly address the growth with equity focus of the Government's socioeconomic development strategy and ADB's evolving poverty reduction agenda. Second, they were not part of an integrated strategy to improve irrigated agriculture and realize considerable production and poverty reduction benefits. Providing infrastructure was treated as sufficient to increase agricultural production. Technical assistance for implementation was not linked to irrigation system management or agricultural production targets, and agricultural support was not provided. Finally, target groups of beneficiaries (primary stake-

holders) were not involved in project formulation or implementation.

Project performance ratings in this case study reflect design limitations. All three projects were rated successful but the ratings mask internal variation. The Hanoi dike was an uncomplicated infrastructure component reflected in consistently high ratings. Agricultural interventions were more complicated and challenging with variable success. Irrigation and drainage interventions were less relevant as they suffered the above design limitations. The financial intermediation through RCP was relevant. RDP irrigation subprojects met agricultural production targets and were thus highly efficacious and also efficient. RCP was efficacious but less efficient, from the financial and process perspectives, because (i) its design misjudged credit demand; (ii) diversification, agroprocessing, and employment did not eventuate as anticipated; and (iii) credit demand remained unsatisfied. The IRP irrigation components and RDP drainage subprojects were both less efficacious because they did not meet irrigation improvement and agricultural production targets. They were also less efficient from both the economic and process perspectives. The Government has a good record of maintaining water resources infrastructure, and agricultural interventions are likely sustainable. Institutional development was generally moderate with considerable engineering achievements offset by ineffective improvement of irrigated agriculture. Overall, the Hanoi flood protection dike component of IRP was rated highly successful, RDP irrigation subprojects and RCP successful, and IRP irrigation components and RDP drainage subprojects less successful.

¹ Loan 1259-VIE(SF): *Irrigation and Flood Protection Rehabilitation Project*, for \$76.5 million, approved on 26 October 1993; Loan 1344-VIE(SF): *Red River Delta Water Resources Sector Project*, for \$60 million, approved on 13 December 1994; and Loan 1457-VIE(SF): *Rural Credit Project*, for \$50 million, approved on 12 September 1996. This case study was prepared independently by an international consultant, Mr. Colin Steley. The full report is available at the Operations Evaluation Department web site—http://www.adb.org/documents/studies/irrigation_water_credit_vie/irrigation_water_credit.pdf.

A recent review of bilateral cooperation came to similar conclusions with regard to poverty and agriculture.² It notes that Viet Nam remains a poor country and most of the population are rice farmers. Thus the strategic recommendations focus on effective ways of supporting systematic institutional change through a consciously pragmatic and long-term (20-year) approach, to reduce poverty through sustainable rural growth. The central recommendation, to invest more in participating in a learning process in Viet Nam's development, is based on the following characteristics of Vietnamese change processes.

Despite popular perceptions, Vietnamese decision making is not highly centralized, many officials are pragmatic, and the value of change is seen in practice, rather than in the abstract. Policies, which are often rather general, are evaluated through the results of practical trials and experiments and are usually only implementable if those upon whom they operate are in agreement. Change takes place from below with new methods, ways and results explored and assessed in reality. Thus, orthodox policy dialogue does not generate high returns, and nurturing bottom-up learning processes and building social capital are more likely to be effective. Proximity to, and close involvement in, heuristic change processes makes the difference in terms of effective development cooperation, avoids confrontation, and encourages interventions tailored to what is feasible at the time.

While the review found that what you do is not as important as how you do it, it also advocated rural development as a key activity area of poverty-focused development. Thus irrigated agriculture offers ADB an opportunity to simultaneously achieve dual objectives by pursuing pragmatic productivity gains and poverty reduction results while facilitating and documenting effective participatory learning and institutional change processes.

These are the main lessons of the evaluation of the three projects: (i) there is considerable potential to improve the performance of irrigated agriculture and reduce poverty; (ii) project design is critical to success; (iii) so too is effective technical assistance to support innovation in improving gov-

ernance, institutional change, and participation in project formulation and implementation; (iv) operating entities should be appointed as implementing agencies; (v) infrastructure and credit are necessary, but insufficient on their own; (vi) complementary irrigation management and agricultural interventions are also necessary; (vii) ADB missed an opportunity to promote a more holistic irrigation system improvement approach; and (viii) the recent reorganization of ADB and merger of the former Ministry of Water Resources with the present Ministry of Agriculture and Rural Development provide a better opportunity to pursue an integrated approach to improving the performance of the irrigated agriculture subsector.

The main recommendations are to (i) reorient the country strategy and policy dialogue to emphasize irrigated agriculture; (ii) progressively develop a subsector strategy; (iii) implement a pilot program to develop and document participatory processes for irrigation systems in social assessment, performance assessment and diagnosis, and integrated performance improvement interventions involving irrigation management, agriculture and credit, and phased improvement of priority infrastructure; and (iv) adopt a flexible phased design of future sector projects. The impending implementation of the follow-on project³ provides an ideal opportunity. This may begin with a protracted inception phase to review and reorient the design with all stakeholders and review agricultural potential and constraints, reasons for apparent poor performance of RDP drainage subprojects, and the Ministry of Agriculture and Rural Development's preferences regarding IRP irrigation management innovations, results of the Bac Hung Hai irrigation and drainage system diagnosis, and the holistic system approach to managing irrigated agriculture.

² Fford, A. 1999. *Vietnamese-Australian Cooperation—"From Unconscious to Conscious Pragmatism": Some Lessons from Experience and Recommendations for the Future Strategic Framework*. Sydney.

³ Loan 1855-VIE(SF): *Second Red River Basin Sector Project*, for \$70 million, approved on 13 November 2001.

Appendix 11: Integrating Policies

In the replenishment of Asian Development Fund (ADF) VII, contributors requested the Asian Development Bank (ADB) to continuously review and refine its policies in accordance with changing circumstances and emerging lessons from experience. In this spirit, ADB has taken initiatives and adopted a number of policies and practices during this period that have had a large impact on the development and delivery of strategic objectives in key areas. Safeguard policies, governance and anticorruption, participation of nongovernment organizations (NGOs), better knowledge management, and regional development and cooperation have all had a direct impact on the relevance, quality, and delivery of projects and programs.

Safeguard Policies

ADB policies and procedures on the environment, involuntary resettlement, and indigenous peoples have been grouped together to form a safeguard framework for ADB projects.¹ They have been put in place over the last decade to encourage sustainable development and focus attention on issues such as regional and transboundary environmental concerns, the displacement of people due to ADB-financed activities, and the equal participation of indigenous peoples in development. These policies have been instrumental in supporting the transformation of ADB from a project-based bank to a broader knowledge-based development institution. The safeguard compliance system checks at key milestone points that all public and private sector projects comply with ADB policies in these three areas prior to loan approval.

Environment

Protection of the environment in the region was adopted as one of ADB's five strategic development objectives in the first Medium-Term Strategic Framework,² and lending and technical assistance (TA) activities have been geared to meet this objective. The adoption of extensive guidelines and processes during the ADF VI–VII period reflects the growing importance of environmental issues in ADB.³ The 1995 reorganization of ADB further strengthened the position of environmental activities. In addition, ADB partnerships with the Global Environment

Fund and United Nations produced projects targeting climate change, biodiversity, and desertification issues in addition to transboundary activities in the greater Mekong subregion and Central Asia.

One of the major changes in the past few years has been ADB's ability to respond quickly to environmental emergencies in its developing member countries (DMCs). For example, emergency TA was provided to support mitigation measures when forest fires threatened Indonesia in 1998.⁴ In addition, TA was provided to Bangladesh and Tajikistan for water management⁵ and other pressing environmental concerns.⁶ ADB also responded to growing environmental concerns with regional TAs.⁷

The evolution of environmental policy and practice within ADB has led to increasing awareness

¹ ADB. 2001. *Reorganization of the Asian Development Bank*. Manila.

² ADB. 1992. *Medium-Term Strategic Framework (1992–1995)*. Manila.

³ ADB. 1992. *Environmental Loan Covenants: Helping Ensure the Environmental Soundness of Projects Supported by ADB*. Manila; ADB. 1993. *Environmental Loan Convents: Principles, Checklists, and Samples*. Manila; ADB. 1993. *Environmental Assessment Requirements Review Procedures of ADB*. Manila; ADB. 1994. *Environmental Assessment Requirements Handbook for Integrated Pest Management in Agriculture Projects*. Manila; ADB. 1996. *Workbook: Economic Evaluation of Environmental Impacts*. Manila; ADB. 1998. *Environmental Assessment Requirements of ADB*. Manila; and Lohani, B., et al. 1999. *Environment and Economics in Project Preparation*. ADB, Manila.

⁴ TA 2999-INO: *Planning for Fire Prevention and Drought Management*, for \$1 million, approved on 20 March 1998.

⁵ TA 3659-BAN: *Jamuna-Meghna River Erosion Mitigation*, for \$1 million, approved on 28 May 2001; TA 3319-TAJ: *Flood Disaster Management*, for \$205,000, approved on 2 December 1999; and TA 3495-TAJ: *Strategy for Improved Flood Management*, for \$550,000, approved on 5 September 2000.

⁶ TA 3269-BAN: *Bangladesh Environment Operational Strategy*, for \$99,000, approved on 30 September 1999; and TA 3357-BAN: *Oil Spill Impact and Response Management Program*, for \$1 million, approved on 22 December 1999.

⁷ TA 5822-REG: *Protection and Management of Critical Wetlands in the Lower Mekong Basin*, for \$1.7 million, approved on 22 December 1998; and TA 5712-REG: *Coastal and Marine Environmental Management in the South China Sea Phase II*, for \$2.7 million, approved on 13 December 1996.

among staff of the need to include good environmental practices in projects. These practices have expanded from the traditional infrastructure projects to specific loan covenants for environmental impact assessments and other screening procedures for subprojects to be financed by credit lines through financial institutions.

Involuntary Resettlement

An important advance in ADB has been the way resettlement issues are tackled in projects. The policy⁸ stipulates that projects should (i) avoid involuntary resettlement where feasible; and (ii) minimize resettlement where population displacement is unavoidable, and ensure, where effects are unavoidable, that displaced people receive assistance, preferably under the project, so that they would be at least as well-off as they would have been in the absence of the project. For any project that leads to loss of land, income, housing, facilities, and resources, resettlement is an integral part of the project design and must be dealt with from the earliest stages of the project cycle.

On average, close to 120,000 people are affected annually by ADB-funded projects. Of this number, about 40,000 require relocation and resettlement. Between 1994 and 2000, nearly 80 resettlement plans in 13 DMCs were prepared before project appraisal and approval. In terms of number of people relocated, the People's Republic of China (PRC) had the highest percentage (60%), followed by Viet Nam (14%), Bangladesh (12%), Indonesia (7%), Cambodia (2%), and Philippines and Sri Lanka (about 1% each). In terms of sectors, the transport project recorded the highest number of people relocated (78% of the total), followed by energy, and water supply and irrigation projects (9% each).

ADB formulated basic principles and approaches to address development-induced displacement of people.⁹ This policy ensures that people who may be adversely affected by an ADB-related development activity are consulted, compensated for their losses, and assisted in rebuilding their income sources, homes, and communities. Previously, resettlement programs tended to be limited to statutory monetary compensation for land, or occasionally, development of a resettlement site. Delays in project implementation, lower development impact to beneficiaries, and a growing awareness of the potential adverse economic, social, and environmental consequences of population displacement led to a new policy approach.

The three important elements in involuntary resettlement are (i) compensation for lost assets and loss of livelihood and income, (ii) assistance for relocation including provision of relocation sites with appropriate facilities and services, and (iii) assistance for rehabilitation to achieve at least the same level of well-being with the project as without it. The approval of ADB's poverty reduction strategy in 1999 has reinforced the importance of risk miti-

gation through comprehensive resettlement planning to reduce the risks of impoverishment through displacement.

The Operations Evaluation Department (OED) has assessed the relevance, adequacy, and effectiveness of the involuntary resettlement policy and the impact of its implementation.¹⁰ The policy framework was found to be comprehensive and relevant in providing fair treatment to people affected by a project. Projects approved during the early years of implementing the policy were not as detailed in reporting resettlement activities. Land acquisition and resettlement issues were dealt with more comprehensively during the preparation of projects approved between 1997 and 1999. As a result, resettlement plans were more detailed in terms of entitlements of displaced persons, specific time-bound resettlement actions, mitigating measures, and provisions for monitoring the status of resettled people.

Analysis of the field data on resettlement impacts indicated that progress was made in achieving the objectives of the involuntary resettlement policy, contributing in many instances to enhanced payments of compensation for lost assets, providing improved housing and infrastructure, and restoring livelihoods for many resettled families. Some affected households reported their status as poorer than before. In Indonesia and the Philippines, several implementation problems affected land acquisition and resettlement activities, ranging from unsatisfactory implementation to significant cases of noncompliance with involuntary resettlement plans.

There were, however, concerns about the practical aspects of implementing the involuntary resettlement policy framework, and the capacity of the DMC government or counterpart to implement and adhere to the policy guidelines. The policy demanded fundamental structural changes in national land acquisition laws and payments of compensation for development-induced displacement. This activity appeared to be almost entirely project-driven and compliance by DMCs was largely motivated by desire to gain loan approval. Improvements in compensation and other benefits were ad hoc and project-specific. The project case studies showed that a resettlement plan's effectiveness depended on local conditions and needs. The plan should be formulated with appropriate modifications to suit local conditions and needs.

Ineffective implementation and limited impact of the resettlement plan on the overall resettlement process of DMCs were a major concern. The evalu-

⁸ ADB. 1995. *Involuntary Resettlement*. Manila.

⁹ The formal policy was approved in November 1995.

¹⁰ ADB. 2000. *Special Evaluation Study on the Policy Impact of Involuntary Resettlement*. Manila. The study covered Bangladesh, PRC, Indonesia, and Philippines.

Box A11.1: Good Practice for Involuntary Resettlement

Six factors are crucial for an integrated approach to resettlement planning and implementation:

- (i) An appropriate policy and legal framework provides clear guidelines, specifies inclusive definitions of affected people, assures market or replacement value for all kinds of assets acquired, and establishes mechanisms for grievance resolution.
- (ii) Early attention is given to comprehensive planning to resolve land acquisition and resettlement issues; establish a database for development planning and a resettlement site with civic amenities, including options for resettlement; develop a gender-based income restoration plan, training for alternative income programs, and other programs as appropriate (e.g., for vulnerable groups); and provide for mitigating unanticipated project consequences.
- (iii) Disclosure and consultation with stakeholders include discussion and forming task-oriented special committees (comprising project staff, local government officials, experts, affected people, etc.) to collect specialized information, consult with local communities to assess the extent of impact, and determine compensation rates.
- (iv) A strong implementing agency is present in the field; local government officials, displaced people, the host community, nongovernment organizations, and community-based organizations are involved in resettlement policy implementation; and there is willingness to learn from experience, adapt, and improve implementation strategies.
- (v) Resettlement costs are properly budgeted and based on market or replacement value; funding is available on schedule and paid to displaced people prior to relocation.
- (vi) A system of supervision and internal monitoring is established, and monitoring data used as feedback to improve performance. Nongovernment organizations, community-based organizations, and affected people are involved in the monitoring process.

ation identified a number of issues: (i) lack of appropriate and compatible national resettlement policy in most DMCs; (ii) inadequate social investigations at the project preparatory level; (iii) improperly identified impoverishment risks, resulting in inadequate restoration of income and livelihood and serious implications for the sustainability of resettlement programs; (iv) weak executing agency's institutional capabilities and lack of or inadequate funding for resettlement activities; (v) weak supervision and monitoring of resettlement implementation; (vi) lack of consistency in capacity building and in the role of NGOs in project implementation and sustainability; and (vii) inadequate aid coordination among external agencies.

ADB is aware of the various policy and implementation issues that remain to be addressed. Several initiatives have been taken to resolve these issues, such as a review of national resettlement policies in some DMCs and a review of resettlement policy issues in view of ADB's new poverty reduction strategy and increased demands for public disclosure.

Overall, ADB's involuntary resettlement policy is adequate and relevant, but refinements should be made to clarify some specific policy elements (Box A11.1), and monitoring of resettlement implementation should be strengthened.

Indigenous Peoples

In 1998, ADB introduced the policy on indigenous peoples,¹¹ followed by the operational guidelines on indigenous peoples in 2000. Those are key policy instruments for ADB operations as they affect indigenous peoples and ethnic minorities. Given the tremendous diversity of culture, history, and current circumstances of indigenous peoples' communities, defining indigenous peoples can be a difficult task. As a starting point, indigenous peoples can be defined on the basis of characteristics they display, namely: (i) descent from population groups present in a given area before modern states or territories were created and before modern borders were defined; and (ii) maintenance of cultural and social identities, and social, economic, cultural, and political institutions separate from mainstream or dominant societies and cultures. The working definition of indigenous peoples used by ADB in its operations is the following: "Indigenous peoples should be regarded as those with a social or cultural identity distinct from the dominant or mainstream society, which makes them vulnerable to being disadvantaged in the process of development."

If the initial social assessment, required for all ADB-financed projects, identifies that indigenous peoples will be affected significantly or adversely by projects, an indigenous peoples development plan is prepared to address specific concerns. ADB has strengthened the process for early screening of projects affecting indigenous peoples. Thus far, 12 indigenous peoples development plans, more than 20 specific actions, and 8 indigenous peoples development frameworks covering 10 DMCs have been prepared. Staff are assisted in identifying and dealing with indigenous peoples issues by a handbook that contains checklists for the initial social assessments.¹² A report on indigenous peoples and ethnic minorities and poverty reduction in the Pacific region is being prepared for publication.

Participation of Nongovernment Organizations

Operational guidance on ADB cooperation with NGOs and other community-based organizations was set out in the 1998 NGO policy paper.¹³ In common with the assessments of other funding agencies (e.g., World Bank), the current policy emphasizes that NGO partnerships are not a panacea for improved project effectiveness. Potential strengths are engendering grassroots ownership and participa-

¹¹ ADB. 1998. *The Bank's Policy on Indigenous Peoples*. Manila.

¹² ADB. 2001. *Handbook on Poverty and Social Analysis: A Working Document*. Manila.

¹³ ADB. 1998. *Cooperation Between the Asian Development Bank and Nongovernment Organizations*. Manila.

tion, mobilizing communities, piloting innovations, and acting as intermediaries for DMC governments and funding agencies. Potential limitations are tensions with government agencies; questions of mandate, legitimacy, and accountability; perceptions of competitiveness with government; and variable managerial, financial, and technical capacities.

Over the past decade, ADB's involvement with NGOs and other grassroots organizations has increased significantly. OED examined the effectiveness of involving NGOs and other community-based organizations in lending and TA operations.¹⁴ In the 1990s, 150 projects had some form of NGO involvement. In 1998, 28 projects worth more than \$2 billion incorporated NGO activities. DMCs, where ADB developed NGO partnerships, increased from 4 in 1993 to 20 in 2001, covering virtually every sector. International NGO involvement was rather limited. There was a predominance of local grassroots organizations, with selective involvement of national NGOs. The most frequent NGO tasks were community mobilization and capacity building. Increased involvement of NGOs increased demands on capacity and expertise within DMC governments, the NGO community, and ADB.

The results of the evaluation indicated that in ensuring participatory project planning—an increasing trend in ADB operations since 1990—NGO involvement improved stakeholder consultation, a factor critical to project quality. No evidence was found based on project completion and disbursement indicators that NGO involvement accelerated project progress, although this did not mean that NGO involvement would not eventually lead to better development effectiveness.

Successful NGO involvement requires a conducive environment and effective working relations between partners (Box A11.2). The consultative process and NGO capacity assessment were weak in most of the cases OED examined. However, several projects demonstrated that, with the right commitment and expertise, capacity can be strengthened and NGOs can become effective partners.

There has been significant evidence of progress in ADB/NGO cooperation and of ADB's fulfillment of its commitment to involve NGOs as specified in the NGO policy and other operational strategy papers. However, evidence at the country and project levels is very mixed. NGO involvement varies significantly in its range, quality, and effectiveness. There are more effective NGOs in Southeast Asia than in the other regions of ADB operations. NGOs have been most active in the social sectors, rural development, and microcredit. In many projects, however, OED found significant gaps between intended provision, actual involvement, and achievement. At the project concept and design stages, ADB and government need to pay more attention to pivotal factors for successful NGO involvement, including nurturing a conducive environment, ensuring

Box A11.2: Success Factors for Nongovernment Organization (NGO) Involvement

Factors that increase the likelihood of more effective NGO involvement include the legal and regulatory environment for NGOs, the current state of government/NGO working relations, whether consultative mechanisms have been established, and prior NGO capacity assessment. When two or more of these factors are medium or weak, there is a strong likelihood that NGO involvement will be unsatisfactory.

executing agency and NGO capacity, and designing effective NGO selection and management and monitoring procedures. Field-based assessments reinforced the view that successful NGO involvement depends on project-specific judgments and careful design and appraisal by ADB and government planners.

Inspection

In December 1995, ADB established an inspection function¹⁵ to provide an independent forum to which interested parties could appeal in regard to ADB compliance with its operational policies and procedures. This paralleled other efforts within ADB to improve transparency and accountability, and complemented ADB's existing audit, supervision, and evaluation systems. The intent was to foster public participation and dialogue, and to enhance accountability and transparency.

Requests for inspection may be brought when (i) ADB has failed in the formulation, processing, and implementation of a proposed ongoing project, to follow its operational policies and procedures; (ii) this failure has had or is likely to have a direct and material adverse effect on applicant group's rights and interests; and (iii) this failure was brought to the attention of ADB management, which failed within a period of 45 days to demonstrate that ADB had followed, or was taking adequate steps to follow, its operational policies and procedures. A list of international experts has been compiled to constitute an inspection panel. ADB has drawn on these international experts to provide advice as needed.

A Board Inspection Committee, composed of four regional members (at least two borrowing DMCs) and two nonregional members, was set up to review requests for inspection and to recommend to the full Board of Directors whether an inspection is warranted. As of December 2002, there had been eight requests for inspection. The Board Inspection Committee recommended to proceed with two of

¹⁴ ADB. 1999. *Special Evaluation Study on of the Role of Nongovernment Organizations and Community-Based Organizations in ADB Projects*. Manila.

¹⁵ ADB. 1995. *Establishment of An Inspection Function*. Manila.

them—one in Sri Lanka¹⁶ and the other in Thailand.¹⁷

In 2002, a policy review was initiated to take into account implementation experience, particularly lessons learned from the inspection case in Thailand. Early findings indicate that more clarity is needed in regard to several aspects of the inspection function, and that ADB should be more explicit about the guiding principles of accountability. This is important for building consensus in the future. Some of the principles cover issues relating to independence, transparency, and fairness to all stakeholders. ADB's accountability mechanism is also under review. For the inspection function to work, it should be responsive to the concerns of local project-affected people, and be cost-effective and efficient. ADB is working toward developing a more constructive approach to the inspection function that would be less adversarial and legalistic. The outcome of the review will be an important input toward these goals.

Integrated Regional Development and Cooperation

ADB initiated a program for regional economic cooperation in 1992, which included the countries of the greater Mekong subregion—Cambodia, PRC, Lao People's Democratic Republic (Lao PDR), Myanmar, Thailand, and Viet Nam. Since that time, regional cooperation agreements have been established on new air routes, river navigation agreements, and border development. As of December 2002, ADB had provided \$772 million¹⁸ in financing for investment projects, mostly from ADF, plus TA grants amounting to \$46 million.

The initial emphasis was on developing linkages to increase trade and encourage investment among the DMCs. Priority was given to subregional projects in energy, transport, and telecommunications. ADF was used to support the first of these projects—Loans 1727-REG(SF) and 1728-REG(SF): *GMS: East-West Economic Corridor (Lao PDR and Viet Nam) Projects*¹⁹—a 1,500-kilometer road link from Mawlamyine on the Andaman Sea in Myanmar, traversing the Lao PDR and Thailand, and ending at Da Nang near the South China Sea in Viet Nam. Other projects include the Loans 1659-REG(SF) and 1660-REG(SF): *GMS: Phnom Penh to Ho Chi Minh City Highway Projects*²⁰ and Loan 1329-LAO(SF): *Theun-Hinboun Hydropower Project*.²¹

As the program evolved, increased attention has been given to human resource development, tourism, environment, and investment and trade. Initiatives in human resource development include addressing the needs of ethnic minorities in the border regions, searching for ways to mitigate the transborder spread of communicable diseases, and joint efforts to counter drug production and use. Initiatives in tourism included improving access, promotion, and development of projects in full part-

nership with the private sector. Synergy between economic activities and infrastructure development is being achieved by developing economic corridors.

The findings of an OED evaluation of the Greater Mekong Region program²² supported ADB's involvement in regional cooperation under a framework where it (i) contributed to regional peace and stability, prosperity, and sustainable resource management; and (ii) provided economies of scale, reduced transaction costs, speeded up development through improved sharing of knowledge, and increased opportunities, particularly those that partners on their own were not able to capture (such as improved resource mobilization, private sector development, and gains from trade). While supporting the Greater Mekong Subregion initiative, the evaluation found that the initiative had been constrained by limitations in ADB operations.

A more recent regional cooperation initiative for which background economic and sector work started in 1996 includes the DMCs of central Asia. These DMCs face the twin challenges of nation building and making the transition to a market economy. Given their landlocked and remote locations from major world markets, small domestic markets, and particular resource endowments, especially in energy and water, they face formidable challenges.

The Central Asian Regional Economic Cooperation program initiated in 1997 supports and encourages economic cooperation among Azerbaijan, PRC, Kazakhstan, Kyrgyz Republic, Mongolia, Tajikistan, and Uzbekistan. The overall objectives are to promote economic growth, raise the living standards of the population, promote market integration within and outside the region, develop financing options for infrastructure projects, and improve the policy environment for private sector development.

Partially supported by ADF, Loan 1775-GMS(SF): *Almaty-Bishkek Regional Road Rehabilitation (Kyrgyz Component) Project*²³ is under

¹⁶ Loan 1711: SRI(SF): *Southern Transport Development Project*, for \$90 million, approved on 25 November 1999.

¹⁷ Loan 1410-THA: *Samut Prakarn Wastewater Management Pollution Control*, for \$150 million, approved on 7 December 1995; and Loan 1646-THA: *Samut Prakarn Wastewater Management (Supplementary)*, for \$80 million, approved on 3 December 1998.

¹⁸ \$575 million for national projects with subregional dimensions and \$197 million for purely subregional projects.

¹⁹ For \$32 million and \$25 million, respectively; both approved on 20 December 1999.

²⁰ For \$40 million and \$100 million, respectively; both approved on 15 December 1998.

²¹ For \$60 million, approved on 8 November 1994.

²² ADB. 1999. *An Impact Evaluation Study of the Asian Development Bank's Program of Subregional Economic Cooperation in the Greater Mekong Region*. Manila.

²³ For \$5 million, approved on 31 October 2000 (\$65 million from ordinary capital resources).

implementation. This road will improve the link between Kazakhstan and the Kyrgyz Republic. Other projects supported by ADF include improving the nutrition of poor mothers and children by fortifying salt and flour with iodine, and the recently approved Regional Trade Facilitation and Customs Cooperation Program between the Kyrgyz Republic and Tajikistan,²⁴ and Regional Power Transmission Modernization Project.²⁵

ADB is also supporting subregional initiatives and programs in Southeast Asia, which include the Brunei Darussalam, Indonesia, Malaysia, and the Philippines-East ASEAN Growth Area (BIMP-EAGA) and the Indonesia, Malaysia, Thailand-Growth Triangle.

Though relatively recent, the recognition of the importance of regional cooperation has been growing.²⁶ Indeed, ADB is the only multilateral institution with a mandate to pursue regional cooperation in its Charter and a specific policy on regional cooperation.²⁷ However, there are institutional issues that may affect ADB's effectiveness in pursuing regional cooperation. OED's evaluation (footnote 22) pointed out that ADB's organizational structure, staff resources and incentives, and funding arrangements for TA and project design and development might not have been optimal for supporting such regional

initiatives and programs. The only funding arrangements for subregional initiatives were through department-based regional TA allocations for which there was no forward planning. Loans were financed from country allocations. While concerns about the budget remain valid, the creation of regional departments under the new organization has addressed concerns regarding coordination within ADB.

²⁴ Loan 1926-KGZ(SF): *Regional Trade Facilitation and Customs Cooperation Program*, for \$15 million; and Loan 1927-TAJ(SF): *Regional Trade Facilitation and Customs Cooperation Program*, for \$10 million; both approved on 29 October 2002.

²⁵ Loan 1976-REG: *Regional Power Transmission Modernization (Uzbek Component) Project*, for \$70 million; and Loan 1977-REG(SF): *Regional Power Transmission Modernization (Tajik Component) Project*, for \$20 million; both approved on 17 December 2002.

²⁶ A working paper—ADB. 2002. *Regional Cooperation In Asia: Long-Term Progress, Recent Retrogression, and the Way Forward*, ERD Working Paper 28. Manila—examines the growing trend toward greater regional cooperation throughout the world and the economic importance and benefits of cooperation.

²⁷ ADB. 1994. *Bank Support for Regional Cooperation*. Manila.

Appendix 12: Assessment of Country Operational Strategies

The Asian Development Bank (ADB) prepared six country operational strategies (COSs) in 1995. An evaluation¹ showed that four of them took into account ADB's previous COS in the country, but the analysis of actual performance was not thorough to provide adequate feedback into the COS under preparation. The analysis was generally limited to a listing of the objectives of the previous COS along with, in some cases, a summary of ADB's lending during the period the COS was in effect. Only in a few cases was an attempt made to assess the impact of the previous COS. Lessons learned from project implementation were based primarily on postevaluation reports, some of which were too outdated to be useful. Information gathered during portfolio reviews was not used to inform future COSs. No attempt was made to link the lessons learned to the development issues at hand. There was no evidence that lessons learned from technical assistance were incorporated into the COSs. Regional cooperation issues were not discussed.

For country assistance plans (CAPs), lessons learned from past experiences were incorporated in most cases. However, the treatment was broad and general, with simple references to postevaluation results. There was little discussion, if any, on how the lessons learned had influenced project selection, or how specific implementation issues would be addressed.² In addition, CAPs did not reflect COSs and some of the project concepts in the CAPs were not based on thorough sector analysis. At the project level, consideration of lessons learned and past experience

was left to a later stage in the project cycle, when its practical value was less.³

By 1997, the COSs and CAPs improved and were more uniform, but their quality still varied significantly.⁴ There was little emphasis on the environment and on women in development/gender and development (WID/GAD) (see Box). The low number of projects targeting these categories may have been due to difficulties or lack of familiarity in formulating and designing projects targeted at these areas compared with more traditional economic growth projects, or projects for health, education, and other social infrastructure. There was also the possibility that there was less understanding by governments as to the shift in ADB's focus on projects that supported WID/GAD, and poverty reduction. Staff constraints in projects departments resulted in limited input from sector specialists outside of thematic areas and affected the depth of sector analysis in many of the COSs. This limitation was somewhat ameliorated by the use of consultants, but such use constrained learning within ADB and was an issue throughout the preparation of the COSs. The result was that COSs often lacked in-depth sector analysis, relevant sector strategies, and performance indicators.

In 1998, the Operations Evaluation Department began to review country assistance programs.⁵ These evaluations assessed the rigor and relevance

Increasing the Focus on Targeting Poverty and Social Development Objectives

Within the social and environmental group of strategic objectives, the lending programs have not been equitably distributed. There has been little lending programmed for women—typically projects with the primary objective of women in development/gender and development attracted 1–2% of the annual lending program during 1992–2000. Although the overarching objective in many country operational strategies has been the reduction of poverty, not many poverty reduction projects were included in the country assistance programs to address this specific objective. Poverty lending was programmed in the range of 4–7% of resources available to the Asian Development Fund countries annually. This has been slowly changing as new projects have entered the pipeline. The 1999 country assistance programs did show an increase in lending for poverty to about 10% of total lending.

¹ ADB. 1996. *1996 Annual Performance Evaluation Program and Review of 1995 Activities*. Manila.

² There may have been several reasons for this: (i) guidelines for the revised CAPs were introduced late in the programming cycle, (ii) ADB experienced a significant staff turnover early in the year, (iii) the sample document provided as a guide for the preparation of the CAP paid insufficient attention to linkages with past experience.

³ This gap in analyses and critical review of important facts, as a basis for project identification and selection, continues to be a problem.

⁴ ADB. 1998. *1998 Annual Performance Evaluation Program and Review of 1997 Activities*. Manila.

⁵ Country assistance program evaluations have been completed for Bangladesh, People's Republic of China, Mongolia, Philippines, and Viet Nam.

of the COS and CAP in a given country. There was evidence that ADB had attempted to shift the emphasis in COSs to reflect its medium-term strategy. The evaluations, however, also indicated that there were often inadequate links between the COS and CAP. The COSs tended to be process driven rather than acting as instruments of change or reorientation of the CAPs. By the end of the ADF VII period, CAPs reflected the shift in COSs toward poverty reduction, especially among the larger, long-term borrowers.

One major breakthrough was the substantial improvement of aid coordination with multilateral and bilateral aid agencies in the COS and CAP pro-

cess. More consultation resulted in a better understanding of country project implementation capabilities based on experiences of other agencies, and was useful in identifying a distinctive role for ADB in the country. The consultation process became formalized and the results of the consultations were usually reported in a dedicated section in the COS. There is some evidence of consultations with nongovernment organizations in these documents, albeit to a limited extent. Some resident missions supported greater participation and assisted in the organization of general consultations with nongovernment organizations on a regular basis.

Appendix 13: Allocation of ADF Resources

Allocation of ADF Resources (by economy ^a and region, \$ million)						
Economy and Region	ADF VI		ADF VII		Total	
	Amount	%	Amount	%	Amount	%
A. Country						
1. Bangladesh	1,351.1	20.0	1,056.4	20.0	2,407.5	20.0
2. Pakistan	1,689.9	25.0	603.8	11.5	2,293.7	19.1
3. Viet Nam	937.5	13.9	1,012.1	19.2	1,949.6	16.2
4. Sri Lanka	517.6	7.7	689.1	13.1	1,206.7	10.0
5. Nepal	386.2	5.7	355.3	6.7	741.5	6.2
6. Lao PDR	384.9	5.7	241.1	4.6	626.0	5.2
7. Cambodia	246.0	3.6	237.6	4.5	483.6	4.0
8. Indonesia	284.7	4.2	195.0	3.7	479.7	4.0
9. Kyrgyz Republic	160.0	2.4	292.2	5.5	452.2	3.8
10. Mongolia	284.8	4.2	154.6	2.9	439.4	3.7
Subtotal	6,242.7	92.5	4,837.2	91.8	11,079.9	92.2
11. Philippines	292.6	4.3	23.8	0.5	316.4	2.6
12. Papua New Guinea	57.5	0.9	59.9	1.1	117.4	1.0
13. Tajikistan	0.0	0.0	99.0	1.9	99.0	0.8
14. Kazakhstan	40.0	0.6	20.0	0.4	60.0	0.5
15. Bhutan	12.7	0.2	43.3	0.8	56.0	0.5
16. Marshall Islands	24.1	0.4	28.1	0.5	52.2	0.4
17. FSM	17.1	0.3	26.0	0.5	43.1	0.4
18. Solomon Islands	0.5	0.0	36.0	0.7	36.5	0.3
19. Vanuatu	10.0	0.1	22.0	0.4	32.0	0.3
20. Maldives	8.8	0.1	21.3	0.4	30.1	0.3
21. Samoa	10.6	0.2	18.0	0.3	28.6	0.2
22. Uzbekistan	0.0	0.0	20.0	0.4	20.0	0.2
23. Tonga	18.5	0.3	0.0	0.0	18.5	0.2
24. Cook Islands	13.5	0.2	0.8	0.0	14.3	0.1
25. Kiribati	0.0	0.0	10.2	0.2	10.2	0.1
26. Tuvalu	0.0	0.0	4.0	0.1	4.0	0.0
Subtotal	505.9	7.5	432.4	8.2	938.3	7.8
Total	6,748.7	100.0	5,269.7	100.0	12,018.4	100.0
B. Region						
East and Central Asia	484.8	7.2	585.8	11.1	1,070.6	8.9
Mekong	1,568.4	23.2	1,490.8	28.3	3,059.2	25.5
Pacific	151.9	2.3	205.1	3.9	357.0	3.0
South Asia	3,966.3	58.8	2,769.2	52.5	6,735.5	56.0
Southeast Asia	577.4	8.6	218.8	4.2	796.2	6.6
Total	6,748.7	100.0	5,269.7	100.0	12,018.4	100.0

ADF = Asian Development Fund, Lao PDR = Lao People's Democratic Republic, FSM = Federated States of Micronesia.
Note: Figures may not add up to total because of rounding.

^a Ranked from the largest to the smallest borrower.

Source: Asian Development Bank's Loan Financial Information System.