

**ANNUAL REPORT OF THE DEVELOPMENT EFFECTIVENESS COMMITTEE
TO THE BOARD OF DIRECTORS
AUGUST 2003**

INTRODUCTION

1. The Development Effectiveness Committee (DEC) of the Board of Directors was established to assist the Board in carrying out its responsibility for ensuring that the programs and operations of the Asian Development Bank (ADB) achieve development effectiveness. For purposes of the Committee's work, "development effectiveness" is considered to be achieved if (i) ADB's programs and operations result in the desired outcomes through implementing ADB's policy and strategy framework, and (ii) if these programs and operations make efficient use of ADB's available resources. Such development effectiveness is continuously assessed through ADB's operations evaluation program.

2. Accordingly, the DEC is expected to review the annual work program of the Operations Evaluation Department (OED) and selected outputs of that work program in order to satisfy itself that ADB's operations evaluation activities are adequate and efficient, and to report its conclusions and recommendations to the Board. To ensure that post-evaluation lessons learned regarding development effectiveness have an impact on current operations, the DEC is also responsible for reviewing the annual performance of loan and technical assistance under implementation.

Composition of the DEC

3. During the period covered by this annual report, August 2002 to July 2003, the DEC was composed of the following members:

Zhao Xiaoyu, Chairman in August-September 2002
Jusuf Anwar, Chairman starting October 2002
Frank Black, in August 2002 to June 2003
Lori Forman, starting October 2002
P. G. Mankad
Osamu Tsukahara
Chantalle Wong, in August-September 2002
Yang Shaolin, starting October 2002.

Agenda of DEC Meetings, August 2002 to July 2003

4. The DEC meetings held in the period covered by this annual report included a selection of studies that the Committee considered to be of high priority in ADB's medium term agenda, of high relevance to ADB's medium term work program, and representative of the wide range of issues and challenges faced by ADB at the project, country, sector, and institutional levels. A complete listing is given in the **Attachment**.

Components of the DEC's Annual Report

5. The DEC has chosen to fulfill its responsibilities to the Board, as stated in paragraph 2, by reporting to the Board on the observations, conclusions, and recommendations from the Committee's detailed reviews of three annual summary reports prepared by OED:

- I. *Status of Implementation of Key DEC Recommendations in 2002*
- II. *Annual Report on Loan and Technical Assistance Portfolio Performance for the Period Ending 31 December 2002*
- III. *Annual Review of Evaluation Activities in 2002*

The Committee's own reports on these three staff reports - in combination and as presented in succession below - form the substance of the Committee's annual report to the Board for the Board's consideration.

Overview

6. The Committee's detailed reports on each of the three annual report components follow this introductory perspective and overview.

(i) Status of Implementation of Key DEC Recommendations in 2002

This was the first status report commissioned by the Committee since its inception and the Committee has asked that it be prepared annually hereon. Its purpose is to monitor actions implemented by Management and staff on the Committee's previous recommendations. This is important because, unless the DEC's recommendations are acted upon in a timely and effective manner, their value will diminish. Also, since the Committee's membership can change every two years, this provides a mechanism for continuous monitoring of and accountability for actions being taken by ADB on DEC recommendations.

The Committee has determined that of seven recommendations for action it made in its annual report last year (2002), the status of implementation of two remain unsatisfactory. Completed actions on these recommendations remain outstanding and will continue to be monitored by the Committee:

- *introduction of a "project readiness filter" as a project management tool to reduce persistent delays in loan effectiveness after loan approval; and*
- *attention by ADB Management to the continued annual shortfalls in accomplishment of the required project completion reports (PCRs) and TA completion reports (TCRs).*

(ii) Annual Report on Loan and Technical Assistance Portfolio Performance for the Period Ending 31 December 2002

On behalf of the Board, the Committee reviews the annual report on the current performance of loans and TA under implementation, including achievement of loan project and TA completion reports. While prepared by OED, the report relies on the statistical information regularly gathered and assembled by the Central Operations Services Office (COSO) and is the culmination of quarterly updates provided to the Committee during the performance year.

Having reviewed the annual report, the Committee broadly endorses its findings and conclusions. At the same time, the Committee remains concerned about certain issues identified in the report, and will continue to monitor ADB's actions on these. In particular,

issues of TA management and effectiveness as discussed in the report will be closely monitored. A key recommendation by the Committee is that, in the future, the annual report by OED should not shy from being more evaluative by delving beyond the statistics and analyzing, more definitively, the reasons behind annual trends in portfolio performance indicators.

(iii) Annual Review of Evaluation Activities (AREA) in 2002

The AREA is OED's annual report on ADB's evaluation results. It consolidates the information based on which the Committee can assess the adequacy and efficiency of ADB's evaluation program. The AREA is of primary significance as a background reference for the Board because it not only presents thematic evaluation issues cutting across countries and sectors, but also provides a comprehensive summary of the DEC's reviews of individual evaluation studies in its meetings throughout the year, all put together in one framework.

Having considered the AREA, the Committee generally endorses its conclusions. At the same time, the Committee recommends that, in the future, the AREA should be more evaluative in nature, again, proceeding beyond statistical reporting of results and defining, in clear and operational terms, how lessons learned from evaluation should be implemented in future operations in order to increase ADB's development effectiveness. As an example prominent in the Committee's mind, a clearer institutional understanding and policy on the relationship of infrastructure development to poverty reduction in ADB projects is needed. The Committee also recommends that ADB's evaluation activities be planned along a more systematic and themes-based direction in the future in order to have a deeper and institutionalized impact on ADB's operations.

Overall Conclusion

7. The Committee is satisfied that ADB's operations evaluation activities in 2002 were adequate and efficient, and so reports to the Board. Areas for improvement in ADB's development effectiveness are noted by the Committee in this annual report.

8. The members of the Committee who have prepared this annual report, and whose terms of appointment ended on 15 August 2003, take this opportunity to thank the Chairman of the Board for the trust he has placed on them to carry out this important responsibility on behalf of the Board.

**I. STATUS OF IMPLEMENTATION OF KEY DEVELOPMENT EFFECTIVENESS
COMMITTEE RECOMMENDATIONS IN 2002**

STATUS OF IMPLEMENTATION OF KEY DEVELOPMENT EFFECTIVENESS COMMITTEE RECOMMENDATIONS IN 2002

	DEC Recommendations	Action(s) Taken/Proposed	Department/ Office Responsible	DEC Assessment of Implementation as of 2003
A. Annual Report on Loan and Technical Assistance Portfolio Performance for the Period Ending 31 December 2001 (Discussed by the DEC on 30 May 2002)				
1.	The Committee was concerned about the time taken for loans to be effective as long delays result in an inefficient use of resources. The Committee believed that it was time to introduce a "project readiness filter" as a management tool to ensure that conditions set originally for Board consideration are not deferred to loan effectiveness, possibly delaying the latter.	COSO revised PAI 1.01: Initial Project Administration Activities in June 2002 to incorporate and recommend a number of good practices relating to project readiness (see Section C: Actions During Loan Processing, paragraph 8 of PAI 1.01).	COSO; SPD	Unsatisfactory
2.	As the shortfall in contract awards under project loans would affect future disbursements and might impede project implementation, the Committee recommended that the reasons for the decline of contract awards be investigated by the project administration units (PAUs) in headquarters and resident missions (RMs), and corrective actions be taken.	Major efforts have been made to identify the reasons for the decline of contract awards. Some of the reasons identified for the decreasing trend include lengthy procurement process and issues on right of way, land acquisition and resettlement. Sometimes, underachievement of projections is beyond the control of ADB staff and the executing agency (EA), e.g. delays in approval of higher government authorities, the need for re-bidding, pending issues, etc. In some cases, projections of EAs have to be accepted to exert pressure on them to achieve their own projections. To improve project monitoring, contract awards and disbursements projections are discussed regularly at regional department's (RD) quarterly project administration meetings to ensure that they are both realistic and consistent with ADB-wide ratios. The following actions are being taken by sector divisions of RDs to improve contract awards: <ul style="list-style-type: none"> a) contract awards and disbursements are discussed with EAs during review missions; b) contracts with large amounts are closely monitored and follow-ups are done with EAs if projections are not achieved; c) PAU missions have conducted frequent briefing sessions together with COSO to build capacity and expedite contract awards. d) RMs were requested to discuss low achievements during Country Portfolio Review Missions; and 	RDs	Satisfactory

	DEC Recommendations	Action(s) Taken/Proposed	Department/ Office Responsible	DEC Assessment of Implementation as of 2003
		e) Consistent reviews of projections are undertaken, with remedial actions taken in cases of underachievement.		
3.	As timely submission of audited project accounts is essential for accountability and indicative of good governance, the Committee recommended that the underlying causes for the deterioration in the submission of audited project accounts in 2001 be investigated by the PAUs in headquarters and RMs, and remedial actions be taken.	<p>Actions taken by RD's sector divisions to ensure timely submission of audited accounts are:</p> <ul style="list-style-type: none"> a) Fax reminders sent to EAs before audited project accounts (APAs)/audited financial statements (AFSs) become due. b) RMs requested to follow up submission of APAs/AFSs. c) Consistent reminders undertaken to ensure timely submission of APAs/AFSs and specific follow-up and support for projects that encounter recurrent difficulties in submitting on schedule d) Extensive discussions with EAs are done during inception and review missions to ensure that ADB's requirements on APAs are understood and strictly followed. Timely submission is also dealt with in the Project Administration Memorandum e) In the case of DMCs where government auditing practices vary and do not meet international standards, loans regularly include provisions for (i) the EAs to contract an accounting firm to prepare the APA/AFS; and (ii) computerized accounting systems that comply with accounting standards to facilitate project financial management f) PAU and concerned ADB staff are in regular dialogue with the Auditor Generals of DMCs g) Implementation of a detailed tracking and monitoring system h) Enforcement of suspension of loan disbursements is to be taken as a last recourse 	RDs	Satisfactory
4.	The Committee noted a pattern of some departments having persistently met their targets in the past five years while others showed frequent shortfalls. The Committee recommended that Management look into the issue of continued shortfalls in accomplishment of PCRs and TCRs, which appeared to be a matter of inadequate management at the department level.	<p>COSO (i) highlighted to Management the 2002 PCR and TCR performance of the four organizational groupings and individual departments and offices; and (ii) recommended increased oversight for those departments and offices with recurring shortfalls.</p> <p>RDs closely monitor the achievement of PCR and TCR targets at quarterly project administration meetings and are closely monitored by sector divisions and PAUs throughout the year. MKRD and SARD have confirmed</p>	COSO; RDs	Unsatisfactory

	DEC Recommendations	Action(s) Taken/Proposed	Department/ Office Responsible	DEC Assessment of Implementation as of 2003
		that their 2003 PCR and TCR programs will be completed as scheduled.		
5.	The Committee recommended that in line with the resident mission (RM) policy, further delegation of project administration to the RMs be pursued.	<p>The regional departments are actively pursuing further delegation of project administration to resident missions taking into account each RMs capacity and resources. Actions taken and plans for further delegation by each RD are:</p> <p>MKRD: In 2002, six projects were delegated to Cambodia Resident Mission. In addition, four projects have been delegated early January 2003 to Viet Nam Resident Mission and one project to Lao Resident Mission. Over the three years period 2002-2004, subject to staff availability and further training of national staff (proposal submitted to BPHR on 5 May), the number of projects delegated to RMs could be increased from 4 projects at the end of 2001 to 27 projects at the end of 2004, representing 31% of the actual portfolio</p> <p>SARD: SARD has delegated a total of 20 loans and 9 TAs from the period 1 January 2002 to 30 May 2003. Twelve (12) additional loans and their related TAs have been identified and are scheduled for delegation during the second half of the year.</p> <p>ECRD: Plans for further delegation of projects to selected RMs (PRCM and URM) based on assessment of each RM's capacity and resources have been developed and are being implemented.</p> <p>PARD: PARD is in the process of establishing more field offices and will be delegating project administration to them when they are ready. Additional projects were delegated to SPRM in 2003.</p>	SPD; RDs	Satisfactory
B. Annual Review of Evaluation Activities in 2001 (Discussed by the DEC on 7 August 2002)				
1.	The Committee was concerned about the doubtful sustainability of more than half of the evaluated projects. As all projects were considered sustainable when presented to the Board, the assessment of related risks, including their minimization and mitigation, should be provided in the report and recommendation of the President. Consequently, they should be discussed, and measures for their mitigation proposed, in the country strategies and programs (CSPs). To enhance sustainability, it is essential that the follow-up actions recommended in	<p>RDs have incorporated key lessons learned in the processing of proposed projects. In some cases, follow-up actions recommended in the evaluation reports are taken up during policy dialogues and in the processing of subsequent related technical assistance projects. Specific actions/measures taken by each RD to improve project sustainability are:</p> <p>MKRD: CSP (2002-2004) and CSPU (2003-2005) for Viet Nam report updates on portfolio performance and measures taken to mitigate potential project-related risks, including: (i) joint portfolio reviews and</p>	RDs: OED	Satisfactory

	DEC Recommendations	Action(s) Taken/Proposed	Department/ Office Responsible	DEC Assessment of Implementation as of 2003
	evaluation reports be implemented for completed projects, and the lessons learned incorporated in future projects.	<p>harmonization initiatives with the Japan Bank for International Cooperation (JBIC) and the World Bank; (ii) provision of TAs to address resettlement, procurement and financial management; and (iii) Government's new decree on management and utilization of official development assistance (ODA) resources. Key lessons learned from post-evaluation findings will be discussed in CSPU (2003-2005) for Lao PDR in order to ensure that these findings will be appropriately reflected in future project formulation. As part of the process of preparing a full CSP for Cambodia, a Country Assistance Program Evaluation is being done, the conclusions and recommendations of which will feed into the new CSP; risks and their mitigation are part of that.</p> <p>SARD: Recently prepared CSPs (India, Pakistan, and Maldives) and those under preparation (Sri Lanka, Nepal, and Bangladesh) include a chapter on risk assessment, mitigation factors, and monitoring and evaluation to help ensure project sustainability.</p> <p>ECRD: CSPs are more firmly grounded in the country's own development strategies and based on the Poverty Reduction Strategies and Programs (PRSPs) and public expenditure reviews that are being undertaken. In the ADF borrowers in the Central Asian Republics, such as Tajikistan and Kyrgyz Republic, all ADB projects are subject to a rigorous prioritization exercise and included in the public investment programs that are guided by IMF conditionalities.</p> <p>PARD: PARD is currently reviewing the CSPs and CSPUs and will address the lessons learned from past projects to mitigate the risks and issues identified.</p> <p>SERD: The current CSP for Indonesia attempts greater selectivity on both sector and geographical basis. This will force more continuity in interventions; more focused attention to sectoral issues and provide opportunities for following up unfinished agendas in previous interventions leading to greater overall sustainability of the program. A new CSP for the Philippines is now under preparation, and it will address this vigorously.</p>		
2.	The Committee believed that the issue of the persistent divergence between project cost estimates and actual costs warranted a thorough examination and recommended that a special evaluation study	The Special Evaluation Study of Project Cost Estimate is being done in 2003.	OED	Satisfactory

	DEC Recommendations	Action(s) Taken/Proposed	Department/ Office Responsible	DEC Assessment of Implementation as of 2003
	(SES) be included in OED's 2003 work program. The SES should thoroughly investigate the reasons why actual costs differ from appraisal estimates, with a view to making project cost estimates more realistic.			

**II. ANNUAL REPORT ON LOAN AND TECHNICAL ASSISTANCE
PORTFOLIO PERFORMANCE FOR THE PERIOD ENDING 31 DECEMBER 2002**

II. ANNUAL REPORT ON LOAN AND TECHNICAL ASSISTANCE PORTFOLIO PERFORMANCE FOR THE PERIOD ENDING 31 DECEMBER 2002

A. Introduction

1. The Development Effectiveness Committee (the Committee) of the Board of Directors of the Asian Development Bank (ADB) met with staff on 7 May 2003 to discuss the *Annual Report on Loan and Technical Assistance Portfolio Performance for the Period Ending 31 December 2002* (the AR), which was circulated to the Board on 23 April 2003 (IN.80-03). This is the second year the Operations Evaluation Department (OED) has prepared the AR. Under the ADB reorganization of 2002, the responsibility for AR preparation was transferred from the Central Operations Services Office (COSO) to OED. COSO continues to be responsible for the production of statistics on portfolio performance and preparation of quarterly portfolio updates. Accordingly, the AR relies on the data in *Quarterly Portfolio Update as of 31 December 2002* supplemented by other information sourced from regional departments (RDs).

2. The purpose in shifting the responsibility for AR preparation to OED was to provide more evaluative contents to the report. This will help deliver on the Medium-Term Strategy requirement that OED undertake regular portfolio evaluation reviews by 2005 to support the assessment of development impact and country performance. Nevertheless, the present form and substance of the AR needs to develop to become a full evaluation of portfolio performance as it is still heavily drawing on data principally supplied by RDs and collated by COSO. After two years of preparing the AR, OED is planning to enhance the robustness of its evaluation of portfolio performance. This may well involve complementing the desk study with a number of country or thematic studies on significant areas raised by the previous report to produce independent information. This would make portfolio evaluation an ongoing activity throughout the year rather than an annual event as at present. OED is working through these issues as it moves to recruit a replacement Portfolio Evaluation Specialist.

3. The Committee commends OED for preparing a comprehensive and informative AR. However, the Committee notes that the AR is more focused on quantitative presentation but lacking on qualitative assessments. While it appreciates the cautions annotated in the AR on interpreting statistical data, the Committee believes that the AR needs to be more analytical and the reasons and conditions that account for the numbers be further explored. The Committee has noted that OED is taking steps to make the AR more evaluative in the future.

4. The purpose of the Committee's report is to present to the Board a summary of OED's principal findings as well as the Committee's major observations, conclusions, and recommendations. This report is organized along 10 themes that were the focus of discussions during the 7 May meeting: (i) size and composition of loan portfolio; (ii) technical assistance portfolio; (iii) project/program ratings; (iv) start-up indicators; (v) contract awards and disbursements; (vi) loan cancellation; (vii) submission of audited accounts; (viii) country portfolio performance; (ix) PCR/TCR programs; and (x) implementation of resident mission policy.

B. Size and Composition of Loan Portfolio

5. The public sector loan portfolio declined in amount by 5%, from \$34.1 billion in 2001 to \$32.3 billion in 2002, while the number of loans increased slightly from the previous year. As of 31 December 2002, the portfolio consisted of 505 loans (up from 501 loans in 2001) for 443

projects (the same as in 2001) in 32 developing member countries (DMCs). Eighty-five public sector loans were approved in 2002, 18% more than in 2001. Forty-two percent of 2002 loan approvals by amount were classified under poverty intervention, exceeding the target of 40%. By sector, almost half of the amount of new public sector approvals went to energy, industry, and transportation and communications, while agriculture and natural resources and social infrastructure accounted for 20%. The Committee is concerned about the increasing gap between these two sector groups and inquired whether this trend is in accord with the millennium development goals.

6. As of 31 December 2002, the private sector portfolio consisted of 91 projects (down from 99 in 2001) for \$681 million (insignificant change from 2001). Four new private sector loans were approved in 2002 for a total of \$145 million, compared to \$38 million in 2001. Four new equity investments were also approved in 2002 for a total of \$36 million, compared to \$30 million in 2001. In addition, political risk guarantee was provided for two projects for a total of \$60 million.

7. Of the 69 public sector loans closed in 2002, 83% required extensions to the closing date with the average extension being 28 months. This result indicates that expected implementation schedules are too optimistic and that implementation problems are not being resolved in a timely fashion. The Committee observes that this issue was discussed by the DEC last year and that no improvements have been achieved so far.

8. The aggregate net resource transfer (the difference between disbursements and loan service payments) turned negative in 2002 with a net \$1.3 billion being transferred to ADB from DMCs. By country, more than half of the borrowing DMCs had a negative net resource transfer in 2002. The Committee is concerned by this outcome and suggests that the reason behind this phenomenon be examined thoroughly.

C. Technical Assistance Portfolio

9. The number of technical assistance (TA) grants approved in 2002 rose by almost a third. Regional TAs had the highest increase in number (51%), followed by project preparatory TAs (38%) and advisory TAs (13%). The amount of TA approvals rose by 23%. Over half the amount of new TA approvals was for advisory TAs with the balance approximately evenly divided between regional and project preparatory TAs. One hundred and seventy TAs were closed in 2002, the lowest level in the last 5 years. This, coupled with the increased number of TAs approved in 2002, caused the large increase in the number of ongoing TAs.

10. The Committee suggests that the increase in TA approvals should be considered in relation to quality of TA management, efficiency, and effectiveness. The Committee is disappointed that a high number of TAs (394) was reported as completed but not yet closed. The Committee believes that this aspect of TA management needs to be improved, particularly in light of rapidly shrinking resource base for TA operations. The Committee recommends that some mechanisms be devised so that TA accounts are closed as soon as they are completed.

11. The Committee notes the high success rates of completed TAs and wonders whether our internal assessments are realistic.

D. Project/Program Ratings

12. The Project Performance Report (PPR) is the tool used for assessing the performance of active projects and, through aggregation of the individual ratings, the performance of the portfolio as a whole. PPRs are updated on a quarterly basis. Projects are rated on a four-category scale¹ for (i) implementation progress, and (ii) the likelihood of achieving their development objectives, using targets and indicators specified in the project framework during project preparation. Problem projects are those with a partly satisfactory or unsatisfactory rating for either of the two areas. Potential problem projects are those having satisfactory or highly satisfactory ratings, but showing signs of emerging problems through a system of early warning “flags” (e.g., shortage of counterpart funds or noncompliance with covenants). Problem and potential problem projects are collectively classified as “at risk” projects that require remedial action.

13. The performance of the public sector portfolio showed a marked improvement in 2002 as measured by the percentage of problem projects and “at risk” projects. In 2002, 86% of public sector projects was rated as satisfactory or better, while 14% was classified as problem projects. Of the projects rated satisfactory or better, 2% was classified as potential problem projects to give a total of 16% of projects “at risk”. For 2001, the comparable figures were 79% of projects satisfactory or better, 20% problem projects, 6% potential problem projects, and thus 26% “at risk”. By loan amount the trend towards improved portfolio performance is even more notable—15% problem projects in 2002 compared to 25% in 2001 and 17% “at risk” compared to 30% in 2001. Part of the improvement in portfolio performance has come from the fact that more projects have returned to the satisfactory or highly satisfactory categories along with the closure of a number of problem projects. The proactivity index (defined as the percentage of problem projects 12 months earlier that are no longer problem projects, or have been closed) rose from 39% in 2000, to 59% in 2001, to 67% in 2002. In the case of private sector portfolio, there was little change in performance in 2002.

14. The Committee finds the improvements in portfolio performance in 2002 encouraging and commends ADB for this. However, the Committee believes that there is a need to further improve the systems upon which these results are based to ensure the robustness of performance measurement. The Committee supports OED in its efforts to improve results indicators.

E. Start-Up Indicators

15. The number of loans signed but awaiting effectiveness dropped from 22 in 2001 to 14 in 2002. However, the Committee notes that the average time taken for loans to become effective after signing increased sharply from 108 days in 2001 to 149 days in 2002, well beyond the standard 90 days normally stipulated in loan agreements. The Committee also notes that it is even more problematic in the case of ADF loans where they took on average of 179 days to become effective. While it acknowledges that the long delays may be due to capacity constraints, some Committee members are concerned that the delays might be a likely consequence of rushing loans to the Board for approval.

¹ Highly satisfactory, satisfactory, partly satisfactory, and unsatisfactory.

F. Contract Awards and Disbursements

16. The actual achievement of contract awards compared to projections for project loans improved substantially in 2002, rising from 69% to 85%, although still short of the 100% achievement in 1999 and 2000. The contract award ratio also improved in 2002 reversing a 3-year downward trend. Actual disbursement in 2002 was 103% of that projected at the start of the year, up from 91% for the previous 2 years. The amount disbursed was \$4.1 billion, up 8% from the previous year.

17. Despite such year to year improvements in contract awards and disbursements, the Committee believes that benchmark rates or internal parameters to which the annual figures can be compared need to be established.

G. Loan Cancellation

18. Cancellation of surplus loan proceeds was up 20% in 2002. Five DMCs accounted for 83% of the cancelled amount—India (28%), PRC (16%), Thailand (15%), Philippines (12%), and Indonesia (12%). The Committee is concerned about the increasing rate of loan cancellation and recommends that OED further investigate this matter.

H. Submission of Audited Accounts

19. The deterioration in full and timely submission of audited project accounts that occurred in 2001 was reversed in 2002. There was an 83% rate of full compliance (either on time or late) while the rate of noncompliance dropped from 22% to 12%, with the balance partly complying.

20. The Committee is pleased to note that compliance rates for submission have increased. The Committee observes that Indonesia has improved dramatically, from 28% in 2001 to 74% in 2002. The Committee wonders how the Indonesia performed so well and suggests exploring if there are lessons learned from the positive Indonesian experience that can be shared with the three countries that performed worse last year (India, Philippines, and Tajikistan).

I. Country Portfolio Performance

21. As in 2001, an aggregate rating system using four positive indicators—the proportion of projects not “at risk”, degree of full compliance with the submission of audited project accounts, achievement against projected contract awards for project loans, and achievement against projected disbursements—was used to assess country-specific trends. DMCs with at least five active loans and a portfolio of more than \$100 million were rated. Based on this aggregate rating, all but five DMCs improved their performance in 2002. Those that did not (Cambodia, Mongolia, Nepal, Papua New Guinea, and Uzbekistan) showed only a minor deterioration in performance.

22. The Committee finds the country sections of the report (Appendix 3) useful and recommends that these sections be referred to as inputs into all country strategies and programs and country strategy and program updates. The Committee appreciates the table on summary portfolio performance by country and suggests including a column on “at risk by loan amount”.

J. PCR/TCR Programs

23. The preparation of project and TA completion reports is an important part of ADB's project performance management process. The Committee observes that there is noticeable improvement in the submission of project completion reports (PCRs)—from achievement rate of just over 70% in 2000 and 2001 to 84% in 2002. However, the Committee considers this rate still low and requests that regional departments provide explanations for the delays. The Committee is disturbed that the gap between planned and actual circulation of technical assistance completion reports (TCRs) is increasing. The achievement rate in 2002 is 68%, the lowest for the last 5 years. The Committee notes that the worst performers are some of the knowledge departments such as the Economic Research Department and the Regional and Sustainable Development Department. The Committee requests that the Heads of these departments provide explanations for their low achievement rates. The Committee also noted the clarification provided by staff that while the completion rate of PCRs/TCRs needs to improve, significant improvements have been made in the quality of self-evaluation as a result of revisions to the Project Administration Instructions and OED's in-depth review process for around 50% of PCRs.

Implementation of Resident Mission Policy

24. ADB's resident mission (RM) policy states that, as far as practicable, projects will be delegated to RMs as both qualitative and quantitative evidence indicates that RM proximity improves project performance. As of 31 December 2002, 87 loans (17% of the total number of active loans) were being administered by RMs, one less than in the previous year. During the year, 20 loans were delegated to RMs, 11 fewer than in the previous year. Over the last 5 years, there was a slow upward trend in the number of RM administered loans.

25. The Committee is disappointed with the slow pace of delegation of loan administration to RMs. The Committee requests Management to share with the Board the results of the ongoing review of the RM Policy.

Other Areas of Concern

26. Other areas of concern that were discussed during the meeting include the (i) loan classification system and poverty partnership agreements, and (ii) status of implementation of the Committee's recommendations on the 2001 annual portfolio performance review discussed in May last year. The Committee is pleased to note that these issues are currently being addressed. A brief status report on item (ii) will be part of the Committee's report.

Conclusion

27. In the context of the above observations and concerns, the Committee broadly endorses the AR. Overall, 2002 was a good year in terms of portfolio performance based on indicators such as performance ratings, percentage of problem and "at risk" projects, contract awards, disbursements, and submission of audited accounts. All but 5 of the 18 DMCs with at least five active loans and a portfolio of more than \$100 million improved their performance over the 2001 levels. Areas requiring attention and remedial action include the longer time taken for loan effectiveness, the need for extensions to loan closing dates, the increasing proportion of loan cancellations, management of the TA portfolio, strategic alignment of resource allocation and the loan and TA classification systems, and the lower proportion of the TA and project completion report program actually carried out. Given the importance of follow-up actions on

these areas, the Committee will monitor the actions taken or proposed to be taken by the Management to further improve portfolio performance.

III. ANNUAL REVIEW OF EVALUATION ACTIVITIES IN 2002

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A. Introduction

1. The Development Effectiveness Committee (the Committee) of the Board of the Asian Development Bank (ADB) met on 18 June 2003 to discuss the *Annual Review of Evaluation Activities in 2002* (AREA)² prepared by the Operations Evaluation Department (OED). The AREA, the twenty-fifth in the series, reports on the findings and recommendations of 48 evaluation reports and other evaluation activities in 2002, as well as provides a long term trend of evaluation results. In 2002, there were 31 project/program performance audit reports (PPARs), 6 technical assistance performance audit reports, 3 country assistance program evaluations, 6 impact and special evaluation studies, and 2 annual reports.

2. The Committee broadly endorses the AREA and finds it well prepared and written. The Committee notes the substantial increase in evaluation activities in 2002 (an increase of almost 50% in the number of evaluation reports over 2001) and commends staff for this. The Committee appreciates the new chapter on long term trend of evaluation results. However, the Committee is of the view that future AREAs should be more analytical and less statistical. While noting the comments, OED staff clarified that the AREA, which reports the evaluation activities on an annual basis, provides an opportunity to present some statistics for basic informational purposes.

3. The purpose of this report is to present to the Board a summary of OED's major findings and recommendations as well as the Committee's major observations, conclusions, and recommendations. This report is organized along the six major themes that were the focus of discussion during the meeting: (i) projects/programs, (ii) trends in evaluation results, (iii) thematic evaluation studies, (iv) follow-up actions, (v) evaluation harmonization, and (vi) infrastructure development and poverty reduction.

B. Projects/Programs

4. In 2002, 27 public sector projects and 6 programs, and 1 private sector operation were evaluated in 31 reports. Based on five evaluation criteria—relevance, efficacy, efficiency, sustainability, and institutional development and other impacts—4 (12%) of the public sector projects/programs were rated highly successful, 23 (70%) successful, and 6 (18%) partly successful. None was rated unsuccessful. Projects and programs rated successful or highly successful accounted for 93% of the total actual project and program cost of \$5.0 billion, and 89% of associated ADB loan disbursements of \$2.3 billion. The only private sector operation evaluated was rated successful.

5. Of the 27 public sector projects, 4 were rated highly successful, 19 successful, and 4 partly successful. Project design influences project success. Projects that had minimal or moderate design issues were rated either highly successful or successful while projects with key deficiencies in design were rated partly successful. However, some projects with design flaws at approval became successful at completion due to appropriate changes made in their initial design during implementation. The Committee queried what constitutes a good project design, and if there is an accountability mechanism in case of a poorly designed project.

² Circulated to the Board of Directors on 20 May 2003 (IN.98-03).

6. There were significant differences in success rates across sectors. All 14 economic infrastructure projects (6 in energy and 8 in transport and communications) were rated either highly successful or successful. On the other hand, of 12 evaluated agriculture and social projects (7 for agriculture and 5 for social sector), 8 (67%) were rated successful and 4 (33%) partly successful. The only project in the industry sector was rated highly successful. There was also considerable divergence in the rating values across sectors with respect to efficacy, efficiency, and sustainability: 93% of economic infrastructure projects was rated efficacious as compared to 67% for agriculture and social sector projects; 100% of the former was efficient or better as compared to 58% of the latter; 93% of the former is likely to sustain benefits over their full life as compared to 75% for the latter. Overall, the results highlight the difficulties of multifaceted design and implementation of agriculture and social sector projects to fully achieve their objectives. The Committee noted these significant differences between ratings for economic infrastructure against agriculture and social sector projects and inquired whether the divergence was mainly due to evaluation methodology used. OED staff clarified that the same methodology was used for all evaluated projects. The difference in results can be due to the fact that agriculture projects are oriented towards producing traded goods in a highly distorted world market, while infrastructure projects are supplying domestic demand. In addition, implementation was more complicated in agriculture and social sector projects, requiring (i) direct measures to address social concerns; and (ii) increased coordination among a larger group of stakeholders and agencies. The likelihood of sustainability is higher in economic infrastructure than agriculture and social sector projects.

7. The overall average delay in the 27 public sector projects was 2.5 years. Only 2 projects were completed within schedule. Four had minor delays of less than 1 year, 11 experienced delays of 1-3 years, while 10 suffered delays of more than 3 years. Nineteen projects (70%) were implemented with moderate to substantial cost underruns averaging 18%. Eight (30%) projects experienced an average cost overrun of 23%. There is little difference in success rates in relation to project delays and cost variations. The four partly successful projects experienced a below average delay and two of them had cost underruns. On the other hand, 10 successful projects experienced average delays of more than 3 years. Both highly successful and partly successful projects have resulted in moderate to substantial cost underruns or overruns.

8. The Committee notes that implementation delays and significant cost variations are recurring issues and ADB should be able to come up with some concrete results and improvements in these areas in the future. The Committee suggests that a mechanism be set up to improve cost estimates. OED staff reported that a special evaluation study (SES) on project cost estimates is being carried out in 2003 and will examine thoroughly the issues on project cost estimates with a view to make recommendations on required changes in guidelines, systems, and procedures to improve their reliability.

9. ADB is making progress in implementing programs. Four (67%) of the six programs evaluated in 2002 were rated successful, and two partly successful. All four successful programs achieved their program purpose with impacts likely to be sustained. The six programs were designed with two-tranche loans, and had an average of 53 program conditions, including 8 for second tranche release. Across all six programs, only 17 conditions were not met by program completion and only 2 conditions for second tranche release were waived.

10. The Committee notes that too many conditions were attached to programs. Staff reported that the *SES on Program Lending*, which was circulated to the Board of Directors in November 2001, reinforces this view, and has been noted by the operations departments.

C. Trends in Evaluation Results

11. OED has estimated trends in evaluations using ratings at program/project completion and at evaluation in 2002 for the first time. The proportion of projects and programs rated successful was calculated by year of completion for all evaluated projects and programs since 1974. The results show that a downward trend in the proportion of projects/programs rated successful was halted and reversed in 1989. A slow improvement in the social and agriculture sectors was reinforced by higher success rates in economic infrastructure projects and in new borrowers. The upward trend may be explained by changes in operations in the 1980s and by a number of institutional factors designed to improve project performance factors overtime: (i) the adoption of country strategies from mid-1980s onwards; (ii) the new emphasis on policy reform in program lending from 1987 onwards; (iii) the greater emphasis on institutional development and capacity building from the early 1990s onwards; (iv) the work of the Task Force on Improving Project Quality in January 1994; and (v) the establishment of additional resident missions with focus on project administration. The Committee notes the upward trend in success rates, and the preliminary analysis of improvements in processes from the 1980s onwards.

D. Thematic Evaluation Studies

12. Nine thematic evaluation studies were undertaken in 2002, of which three were country assistance program evaluations (CAPEs) and six impact and special evaluation studies (SEs). The Committee notes the importance of these studies as they provide major useful lessons. Of the nine thematic evaluation studies, four (CAPEs for Mongolia, Philippines, and Bangladesh, and SES on ADF VI and VII) were discussed by the Committee in detail in its previous meetings. The highlights of these earlier discussions are given below.

13. The CAPE for Mongolia³ covered the years 1991 to 2001, the entire period of cooperation between Mongolia and ADB during which ADB was the second largest donor after Japan. It sought to assess program priorities and implementation, and ADB's contribution to the transition process. Capacity building mostly focused on inputs such as training and consulting services; the fragmented approach did not promote overall public sector resource management. There was a high proportion of program lending, and a high degree of consistency across reforms in different sectors. However, policy matrixes were overloaded, and policy-based lending to agriculture and industry was only partly successful. Economic reorientation and diversification was an explicit but not very well articulated goal. Projects for rehabilitation and diversification of infrastructure were successful in improving technical performance, and commercializing and corporatizing infrastructure services. Financial sector transformation had a large agenda. Improvements induced by a first program were set back by the Asian and Russian financial crises, but subsequent operations are now bearing fruit. Overall, ADB's country assistance program made significant contributions to the transition process. The Government had strong ownership of individual projects and reform initiatives; and ADB's responsiveness, timeliness, and budget support were appreciated. There was substantial cooperation and coordination with other funding agencies. The CAPE underscored the importance of (i) providing strategic guidance to operations; (ii) undertaking necessary background work to, and using a logical framework approach in, formulating country strategies and programs (CSPs); and (iii) setting specific monitorable targets for the goals.

³ Discussed by the Committee on 27 November 2002.

14. The Committee notes the key ingredients of the successful outcome of transforming Mongolia's economy from a command to a market-based system, namely the important role played by the private sector that achieved a share of about 75% to gross domestic product, the strong ownership of the reform process by the Government, and the responsiveness and relevance of ADB's assistance. The Committee endorses the four recommendations for the CSP process. Since the lessons learned were valuable also for other transition economies such as Tajikistan, the Committee suggests that the lessons be brought to the attention of all regional departments.

15. The CAPE for the Philippines⁴ focused on the period since 1986, which was a watershed in the country's history. The economy performed poorly during this period, well below the performance of the ASEAN neighbors, although the Philippines was less severely hit by the Asian financial crisis. Since 1986, ADB lending totaled \$5.9 billion for 86 projects and programs; 210 TA operations were implemented. Despite some progress in social indicators, high poverty incidence prevails. Project performance was disappointing; of 36 projects completed and postevaluated in 1986-2001, roughly one third each was rated generally successful, partly successful, and unsuccessful. Ten of the unsuccessful projects were completed in the 1980s; there was some improvement in ratings in the 1990s. Issues of sustainability arose in all lending and nonlending interventions stemming from lack of institutional capacity, inadequate budget allocations, and lack of political will. Overall, ADB's assistance program was assessed as relevant, less efficacious, moderate in its institutional development and other impacts, and with question marks on the sustainability of its benefits. The CAPE recommended that selectivity in operations be combined with maintaining a critical mass for ADB to remain relevant; project preparation and close monitoring, and stakeholder involvement be strengthened to improve project performance; emphasis be given to social and regional development, particularly in the southern Philippines; private sector participation be supported, particularly in small and medium enterprises, and infrastructure development; and policy-based lending be flexible, to allow for competing interests.

16. The Committee commended the well-written, frank and comprehensive CAPE, and suggested that a seminar be considered to provide feedback on its findings to the Government and private sector.⁵ The Committee emphasizes the need for better design based on strong analytical work, more realistic assessment of institutional capacity, adequate benchmarks and monitoring indicators, strong stakeholder participation including NGOs, and selectivity.

17. The CAPE for Bangladesh⁶ focused on the period since 1986 when the first country operational strategy (COS) was formulated. The CAPE highlighted the various challenges faced by Bangladesh such as being one of the poorest countries in the world, having a very high population density, depending heavily on official development assistance, and suffering from poor resource management, numerous natural disasters, endemic governance problems and frequent political turmoil. Despite these drawbacks, there were significant positive achievements in the past 2 decades, namely accelerated economic growth (particularly since 1996), self-sufficiency in foodgrains, decelerated population growth and steady, though decelerating, reduction in poverty incidence. On the negative side, income distribution became more skewed in the 1990s. From 1989 to 2001, ADB lending was increasingly linked to institutional and policy

⁴ Discussed by the Committee on 19 February 2003.

⁵ On 10 March 2003, the Director General, OED and the Country Director, ADB Philippines Country Office held a press briefing on the findings of the CAPE for the Philippines with a focus on lessons learned and how these will be incorporated in the new CSP and in project design. Prior to this press briefing, the findings were disseminated to staff of National Economic and Development Authority.

⁶ Discussed by the Committee on 31 March 2003.

reform, and first interventions in health, education, and urban and rural infrastructure placed a greater emphasis on human development and poverty reduction, together with expanded operations in urban and rural infrastructure, and education. The basic thrust of ADB's assistance program was relevant. Earlier slow progress in public sector reform was compensated by promotion of private sector participation, working with nongovernment organizations, and a greater appreciation of governance issues. There was a high proportion of projects rated partly successful, particularly in the agriculture and social sectors. However, project performance improved somewhat since 1986. The CAPE made a number of recommendations for future CSPs, such as a more proactive approach to governance issues, increased support for small and medium enterprises and the recurrent budget in health and education, concerted action to address arsenic contamination of groundwater, support for local champions, particularly in private organizations, and focus on fewer sectors.

18. The Committee notes the positive achievements of Bangladesh despite its various drawbacks. The challenge now is to reduce implementation delays and improve project performance. Although some statements in the CAPE were too general, appropriate issues were identified. The Committee generally endorses the CAPE, including its analysis of the strengths and weaknesses of ADB's past assistance and its recommendations for ADB's future operations.

19. *The Special Evaluation Study of the Asian Development Fund (ADF) VI-VII Operations*⁷ assessed ADB's projects, policies, and processes approved and implemented from 1992-2000 and whether they met ADF objectives. There were 318 projects approved under ADF VI-VII for a total loan amount of \$12 billion, about 24% of ADB's total lending, and about 4% of the total net resource flow to ADF borrowing countries. ADF VI coincided with the introduction of the five strategic development objectives for project classification. A large number of new policies were successively introduced, such as for governance, resettlement, inspection, indigenous peoples, nongovernment organizations, and gender. While almost 60% of projects are still under implementation, there is evidence of uneven but satisfactory progress in meeting the ADF VI-VII objectives and commitments in a way that has affected all ADB operations. Changes in strategic planning and country-programming processes have been found highly satisfactory. ADF project quality and performance have improved and are considered satisfactory. Economic growth projects show solid returns; poverty reduction investments have been improving with experience; practices on project-related issues that affect the poor, such as resettlement and environmental damage mitigation, have improved. While ADB's family planning activities have not been sustained, investments in human development have expanded. Improvements in environmental management have proceeded unevenly and are considered partly satisfactory. A substantial effect on environmental capacity building and mainstreaming had been combined with a less than expected number of projects. ADB's program lending has sometimes been overambitious and governments have lacked the capacity to implement difficult reforms. Finally, incorporating gender concerns remains a difficult area for ADB and is considered unsatisfactory. Project selection and design have not effectively supported this objective, and the impact of mainstreaming gender concerns has been limited.

20. The Committee notes that OED did a credible job in this comprehensive evaluation, and is pleased with the generally satisfactory performance of ADB during the ADF VI-VII period. The Committee also notes that the various recommendations made during its previous discussion of the ADF I-V report were followed in the SES. The Committee requested the ADB

⁷ Discussed by the Committee on 31 March 2003.

delegation to the ADF VIII midterm review meeting to take into account its views such as the concern about the exclusion of the PRC and India from access to ADF resources.

E. Follow-up Actions

21. OED assessed the actions taken in relation to follow-up actions recommended in 28 reports completed in 2001. In total, there were 145 follow-up actions comprising 106 in evaluations of individual operations and 39 in SESs. Seventy-six (52%) actions were addressed to DMCs, and 69 (48%), including nearly all those from the SESs, were related to ADB's processes, guidelines, or strategies. The actions were specific with respect to who was to do what, but less specific on by when. As to the follow-up actions in performance audit reports, 73% were fully or partly implemented and 7% will be addressed in future operations. In 2% of the cases, no response was received and in 18%, no action was taken because concerned DMCs or ADB departments disagreed, or because substantial budgetary resource commitments, major legislation change, or institutional changes over multiple government agencies would have been required. As to the follow-up actions recommended in SESs, 77% were fully or partly taken and 23% will be addressed in future operations. Overall, follow-up actions were relevant to operations and reasonably well addressed. However, the Committee recommends that the time specificity of follow-up actions should be further improved. To enhance applicability to operational needs, follow-up actions should be assessed for their practicality, with deeper involvement of executing agencies, DMC governments, and operational departments. Follow-up actions involving major resource commitments or policy changes should be separated, and facilitated in future operations.

F. Evaluation Harmonization

22. The Evaluation Cooperation Group (ECG) of the multilateral development banks sought to share lessons from evaluations, reduce the costs to DMCs of the evaluation procedures and criteria of different institutions, and enhance the comparability of results. It had completed the good practice standards for individual public and private sector operations and now focuses on higher-level evaluations, including country assistance programs and policy-based lending. The study of Good Practices for the Evaluation of Policy-Based Lending, which ADB is managing on behalf of ECG, has already commenced its Phase I that includes (i) stocktaking of current practices and issues relating to the evaluation of policy-based lending, (ii) collecting materials on good practices, and (iii) proposing an outline of a good practices paper. The ECG is also cooperating with the community of practice dealing with results-based management, to specify an appropriate relationship between independent evaluation and management. The Committee notes the shift in focus of ECG from individual operation to higher-level evaluations.

G. Infrastructure Development and Poverty Reduction

23. Although beyond the scope of the AREA, Committee discussion evolved on the importance of infrastructure projects for poverty reduction. One Committee member mentioned that the World Bank has changed its infrastructure policy in recognition of the fact that development of infrastructure projects is one of the most effective ways of alleviating poverty, and was interested to know whether ADB is thinking along this line. The Committee is of the view that ADB needs to present a clearer policy on the relationship of infrastructure development to poverty reduction in its operations. Some Committee members suggest that OED reviews the relative efficiency of recent infrastructure projects, which have poverty or pro-poor components. OED staff noted the Committee's view and clarified that the general relation between infrastructure and poverty reduction is being addressed in the ongoing management

review of ADB's Poverty Reduction Strategy. OED could consider a study on infrastructure project design in its future work program.

H. Other Areas of Concern

24. Other areas of concern that were discussed during the meeting include (i) the ban classification system and poverty partnership agreements (with OED clarifying that they also are being reviewed by the Task Force for Review of the Poverty Reduction Strategy); and (ii) possibility of establishing an explicit mechanism for accountability of staff involved in loan processing.

**DEVELOPMENT EFFECTIVENESS COMMITTEE
MEETINGS HELD FROM 28 AUGUST 2002
TO 18 JUNE 2003**

Date	Agenda	Type of Study ^a
28 August	Investment Fund Operations Social Action Program (Sector) Project (PAK) Agriculture Sector Program (KAZ)	IES PPAR PPAR
9 October	Integrated Irrigation Sector Project (INO) Fourth and Fifth Road Improvement Projects (LAO) Second Ports Project (IND)	PPAR PPAR PPAR
27 November	Country Assistance Program Evaluation (MON) OED's Work Program for 2003	CAPE
19 February	Country Assistance Program Evaluation (PHI) The Committee's Work Program for 2003	CAPE
31 March	ADF VI-VII Operations Country Assistance Program Evaluation (BAN)	SES CAPE
7 May	Annual Report on Loan and Technical Assistance Portfolio Performance in 2002 PCR/TCR Programs for 2003/2004	AR
18 June	Annual Review of Evaluation Activities in 2002	AR

^a AR = Annual Report; CAPE – Country Assistant Program Evaluation; IES = Impact Evaluation Study; PPAR = Project/Program Performance Audit Report; SES = Special Evaluation Study; TPAR = Technical Assistance Performance Audit Report; WGR – Working Group Report