

**MANAGEMENT RESPONSE TO THE
COUNTRY ASSISTANCE PROGRAM EVALUATION FOR
THE LAO PEOPLE'S DEMOCRATIC REPUBLIC**

On 12 May 2006, the Director General, Operations Evaluation Department, received the following response from the Managing Director General on behalf of Management:

A. Overall Assessment

1. Management appreciates the opportunity to review and comment on the Country Assistance Program Evaluation (CAPE) for Lao PDR prior to the Development Effectiveness Committee's (DEC) discussion on the CAPE. We note the cooperative efforts made by the Operations Evaluation Department (OED) for the CAPE preparation and the complicity involved in evaluating past performance in the developing member countries (DMCs) that have a limited information base. It is understood that the OED evaluation team endeavored to address this challenge by adopting a combination of quantitative and qualitative assessment techniques. It is regarded timely and appropriate that the CAPE assessed the performance of ADB's country operational strategies and assistance programs to Lao PDR for 1986–2004, and identified key lessons and recommendations for consideration of the Lao PDR Country Team during preparation of the forthcoming Country Strategy and Program (CSP) and its subsequent implementation. We note the overall 'successful' rating for the CSP performance at all levels combined.

B. Lessons Learned, Recommendations, and Conclusion

2. Management notes the importance of the lessons identified by OED. The following are Management's responses to the specific recommendations of the CAPE.

OED Recommendation 1: Need to Address the Problems of Limited Government Absorptive Capacity and Ownership/Commitment.

ADB should consider (i) determining the Lao PDR's cost-sharing ceiling based on the aggregate portfolio of the next CSP period during the preparation of the 2006 CSP; and (ii) discussing the issue of high aid intensity ratio with other development partners and pursuing collective policy dialogue with the Government. This objective would be to determine whether the total amount of development assistance should be reduced to be more in line with absorptive capacity and how to improve the Government's capacity in raising more domestic revenues so as to reduce the country's dependence on foreign assistance in the long run.
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Management Response:

a) Management agrees with the CAPE recommendation. ADB is sensitive to the importance of absorptive capacity and is currently working with the Government to address binding constraints to development effectiveness. This issue has been reflected in ADB's adjustments to current lending and non-lending operations for Lao PDR and in the proposed changes to strategic direction under the forthcoming CSP. More specifically, it is reflected in ADB's ongoing support to public expenditure management strengthening, and continued policy dialogue with the Government and development partners directed at improving financial management, revenue mobilization, and the fiscal situation.

b) On specific actions, we would like to note the following:

(i) ADB's Southeast Asia Department (SERD, then Mekong Department) delegated portfolio management to Lao PDR Resident Mission (LRM) that conducts annual and quarterly Portfolio Review Missions. The annual mission identifies the systemic issues adversely impacting on portfolio performance and prepares a mitigation action plan. Both the counterpart funding issue, and pace and extent of agreed reforms have been identified, and corrective actions are being discussed with the Government. ADB will continue to perform these assessments, and will apply the new cost-sharing framework during the implementation of the new CSP. In 2005, the Government, ADB, World Bank, and the Swedish International Development Agency jointly conducted the annual review, and prepared a joint Portfolio Effectiveness Review (JPER) which is currently being implemented. Joint assessments will continue and be broadened to include other development partners.

(ii) Both the Government and development partners identified the country's dependence on external assistance as an issue. The Government has set a target to exit least developed country status by 2020; however, in the short-run the dependency on external assistance will remain significant as identified in the draft 6th Five-Year Socio- Economic Development Plan (SEDP6).¹ The Government, ADB, and other development partners are conducting policy dialogue on the issue of aid dependency through various forums, including the round table process (RTP) for aid coordination. Considering the specific CAPE recommendation, ADB has requested the chairperson of the informal working group on macroeconomics and private sector development to table the issue of Official Development Assistance (ODA) dependence with the working group. Work commenced on implementation of the new cost sharing framework and will be finalized during CSP implementation when inputs from the ongoing public expenditure review, medium term expenditure framework, priority sector costing exercise, and harmonization action plan are available.

OED Recommendation 2: Need for Sector Selectivity.

Given the lower indicative planning figure of \$22.7 million for 2006 (\$30 million in 2005) compared with the average of \$55 million over the CAPE period for the Lao PDR, and concerns over the Government's limited absorptive capacity, the next CSP should focus on a smaller number of sectors.

Management Response:

a) Management agrees with the CAPE recommendation. ADB identified sector focus/selectivity as a pre-requisite for the new CSP.

¹ The National Growth and Poverty Eradication Strategy (NGPES) has been integrated into the Sixth 5-Year Socio-Economic Development Plan (SEDP6).

b) Specific Actions: In the Lao PDR CSP Initiating Meeting on 26 April 2006, the Lao PDR Country Team received Management's direction to reposition ADB assistance to sharpen focus and to maximize impact. This would include (i) repositioning ADB's public sector lending to concentrate on integrated support for government programs of policy and institutional reform, and strategic investments in the main sectors highlighted in SEDP6; (ii) using non-lending services to address strategic priorities, such as governance and support of the revenue management arrangements agreed under the Nam Theun 2 Hydropower Project through the joint Government/ADB/World Bank public expenditure management strengthening program (PEMSP); and (iii) forging positive synergies between the national and GMS program.

OED Recommendation 3: Need for Stronger Harmonization and Partnerships with Other Development Partners.

In line with the expectations stated in the Paris Declaration, ADB should develop more strategic partnerships with other development partners (e.g., joint preparation of CSP and sector strategies, cofinancing strategy, and program-based or sector-coordinated approaches) to provide a more coherent assistance program. This will help reduce the Government's transaction costs, enhance its role in leading the country's development agenda, and increase the possibility for other development partners to finance future recurrent costs after project implementation.

Management Response:

a) Management agrees with the CAPE recommendation: In the JPER Action Plan prepared in November 2005, it was agreed to assist the Government prepare a Harmonization Action Plan (HAP), in consideration of the Paris Declaration. The forthcoming CSP is premised on aligning and enhancing partnering principles, as well as responding to the Government's request to align with SEDP6, reduce transaction costs, move towards sector coordinated approaches, and address binding constraints to poverty reduction.

b) Specific Actions: ADB and the World Bank hosted joint harmonization/alignment workshops for the Government and development partners, and follow-up workshops with the key Government executing agencies. Work has commenced on the HAP and will include development of frameworks for capacity development for the priority sectors for consideration in the CSP. This will be valuable input into the government-owned initiatives for harmonization/alignment. ADB will continue to support the Government's harmonization and alignment initiatives including the Government's requests for option assessments of sector development approaches in the priority sectors, adoption of sector coordinated approaches, implementation of the JPER Action Plan, and continued participation in the RTP.

OED Recommendation 4: Need to Improve the Results Achieved by Program Lending.

Given the disappointing results of program lending, ways must be found to improve performance if use of this modality is to be continued.

Management Response:

a) Management agrees with the CAPE recommendations. In addition to the CAPE, we have identified similar issues under SERD's CSP Completion Report and pre-CSP analytics for selective sectors where program loans have been and/or are being implemented. In particular, these exercises identified the need to carefully assess client preparedness, as this is critical to identifying the appropriate lending modality and program design.

b) Specific Actions: ADB has commenced consultations with both the Government and development partners on programmatic approaches in various sectors. In its ongoing sector

work under the new CSP, ADB will coordinate closely with the Government and development partners to assess client preparedness for program lending and reflect this in the three year lending/non-lending program. In sectors identified for programmatic approaches, ADB will carefully assess the appropriate lending/non-lending instruments, align policy matrices to government priorities and degree of readiness, and develop appropriate results frameworks. In order to feed lessons learned into the strategy, program, and project designs, ADB will continue to carefully monitor and mitigate performance of program loans and/or programmatic approaches under the annual JPER and quarterly portfolio review exercise, as well as through regular review missions.

OED Recommendation 5: Need to Strengthen Sector Strategies with Focus on Governance, Anticorruption, and the Enabling Environment for the Private Sector Development.

The lack of good sector strategies resulted in diffused investments and failure to achieve sector outcomes. The role of ADTAs, and economic, thematic, and sector work should be strengthened to develop sector strategies to guide future ADB operations.

Management Response:

a) Management agrees with the CAPE recommendation. Both the CAPE and CSP Completion Report identified the need for strengthened sector strategies and greater integration of core thematic areas into our operations. ADB is committed to supporting the Government in strengthening their sector assessments and related policy frameworks, and to supporting the realization of priorities of the SEDP6.

b) Specific Actions: In response to both the CAPE and the Sector Assistance Program (SAPE) for the Agriculture and Natural Resources Sector in Lao PDR (Dec 2005), as well as in consideration of reduced Asian Development Fund (ADF) allocations to Lao PDR, ADB has reprioritized its 2006 TA resources in order to advance its sector work in the agriculture, natural resources and environment sector through an ADTA on Institutional and Policy Analysis of Agriculture and Natural Resources Sector in Lao PDR. The Government has recently formed a sector working group to strengthen sector focus/selectivity, efficiency and effectiveness in the sector. This working group will oversee the implementation of the ADTA. The proposed ADTA will also assist the Government develop its roadmap for operationalizing the SEDP6 for the agriculture, natural resources and environment sector. In the education sector, ADB is currently assisting the Government, in close coordination with other development partners, to develop a common policy framework for the education sector under the PPTA for a Basic Education Development loan. In addition, an ADTA is under preparation for the Government and development partners to work together towards a sector or programmatic approach to education sector development. In the health sector, ADB will continue to remain focused on primary health care through the national program. The Government has prepared a strategy for the sector which ADB and other development partners are assisting the Government to operationalize through three core working groups. For the transportation sector, a GMS Transport Sector Strategy has been prepared for consideration of member countries. It is aligned with national strategies and priorities, and proposed to be largely operationalized in Lao PDR during the forthcoming CSP period. Similarly, a GMS strategy for the energy sector is under preparation and will guide future operations in the sector. Prioritization and costing exercises for the SEDP6 priority sectors are being undertaken by the Government with support from various development partners. As part of CSP preparations, the Lao PDR Country Team has prepared draft sector assessments and roadmaps as well as thematic assessments for proposed ADB assistance 2007–2011.

OED Recommendation 6: Need to Improve the Management of the TA Program.

Many ADTAs did not perform well due to limited government commitment. This was particularly true for TAs that were not attached to any project. ADB should improve the management of TAs by (i) improving the link between lending and nonlending programs; (ii) programming TAs strategically; (iii) focusing on achievement of TA outcomes, rather than outputs; and (iv) increasing government participation in TA design and implementation to increase client ownership.

Management Response:

a) Management agrees with the CAPE recommendation. SERD's self assessment under the CSP Completion Report and pre-CSP sector/thematic diagnostics and portfolio review also identified the need to more closely align the TA program with the strategic focus of the CSP. This will be done during formulation of the forthcoming CSP.

b) Specific Actions: SERD has recently conducted a TA rationalization exercise, which reduced the department-wide number of TAs by 40–50% while aligning TA support to the CSPs. Under the forthcoming Laos CSP, TAs will be aligned with the results framework to be developed and carefully monitored during CSP implementation to enhance performance and development effectiveness of the TA program. As the CSP will be closely aligned to the SEDP6, the TA program will be linked to Government priorities, thus instilling greater government ownership and participation. Finally, as the CSP is being developed in a consultative manner, the TA program will also complement and/or supplement interventions of other development partners in key sectors with ADB participation.

OED Recommendation 7: Need to Balance the Coverage of the next CSP with Available ADB Resources.

Given the need to strengthen aid coordination, policy dialogue, and project implementation at the field level, LRM's role should be strengthened with increased delegation of authority and redeployment of staff. This should be considered in relation to the regional role of the Thailand Resident Mission.

Management Response:

a) Management agrees with the CAPE recommendation. In the past 2–3 years, SERD has been decentralizing its responsibilities, including rationalizing the respective roles of sector divisions and resident missions, and matching the country's needs and staff's skill mix both in the sector divisions and resident missions.

b) Specific Actions: Under the recent ADB organizational realignment, SERD has deployed one additional professional staff position to LRM, and during CSP preparation, will conduct a further assessment of needs and required skill mix. Other positions have been redeployed to other resident missions in the region from which LRM can draw resources and enhance client and partner responsiveness. LRM has also commenced to strengthen its cadre of national officers to take increased responsibilities for portfolio management, project administration, and other selective operations functions. Staff members appointed as LRM focal points will continue to support non-operational matters, including knowledge products and services, policy issues, and cross-cutting areas.