ADB

Validation Report

Reference Number: PVR-404
Project Number: 43321
Loan Numbers: 2659 and 2950
July 2015

Marshall Islands: Public Sector Program—Subprograms 1 and 2

Independent Evaluation Department

Asian Development Bank

ABBREVIATIONS

ADB	–	Asian Development Bank
CAP	–	comprehensive adjustment program
CTF	–	compact trust fund
DMF	–	design and monitoring framework
GDP	–	gross domestic product
IMF	–	International Monetary Fund
MEC	–	Marshalls Energy Company
MOF	–	Ministry of Finance
PCR	–	program completion report
SOE	–	state-owned enterprise
TA	–	technical assistance
US	–	United States

NOTES

(i) The fiscal year (FY) of the Government of the Marshall Islands ends on 30 September. "FY" before a calendar year denotes the year in which the fiscal year ends, e.g., FY2014 ends on 30 September 2014.

(ii) In this report, "$" refers to US dollars.

Key Words

asian development bank, compact trust fund, completion report, country performance assessment, governance, marshall islands, public sector management, tax, revenue, state-owned enterprise, validation

PROGRAM BASIC DATA

Project Number:	43321	**PCR Circulation Date:**	1 Oct 2014	
Loan Numbers:	2659 and 2950	**PCR Validation Date:**	Jul 2015	
Project Name:	**Public Sector Program—Subprograms 1 and 2**			
Country:	Marshall Islands		**Approved** ($ million)	**Actual** ($ million)
Sector:	Public Sector Management	**Total Project Costs:**	14.50	14.87
ADB Financing: ($ million)	**ADF:** 2659 (9.50)	**Loan:** 2659 / 2950	9.50 / 5.00	9.98 / 4.89
		Borrower:	0.00	0.00
	OCR: 2950 (5.00)	**Beneficiaries:**	0.00	0.00
		Others:	0.00	0.00
Cofinancier:		**Total Cofinancing:**	0.00	0.00
Approval Date:	17 Aug 2010	**Effectiveness Date:**	28 Sep 2010	28 Sep 2010
Signing Date:	8 Sep 2010	**Closing Date:**	28 Feb 2011	28 Feb 2011
Project Officer:	K. Nakamitsu, C. Sugden, H. Everett	**Location:** ADB headquarters	**From** Aug 2010	**To** Feb 2011
Initial Reviewers:	C. Dingcong, Consultant; L. C. Ocenar, Evaluation Officer, IED1	**Peer Reviewer:**	A. Perdana, Evaluation Specialist, IED1	
Quality Reviewer:	E. Gozali, Principal Evaluation Specialist, IED1	**Director:**	W. Kolkma, IED1	

ADB = Asian Development Bank; ADF = Asian Development Fund; IED1 = Independent Evaluation Department, Division 1; OCR = ordinary capital resources; PCR = program completion report.

I. PROGRAM DESCRIPTION

A. Rationale

1. During program preparation, the Marshall Islands had a fragile public sector that was constrained by weak public sector institutions, limited budgetary resources, and underdeveloped governance systems. The economy relied heavily on government expenditure, and on foreign funds, which funded more than two-thirds of government expenditure. The United States (US) provided nearly all of the external grants mainly under the amended Compact of Free Association.[1] These compact grants were to be reduced annually until FY2023. To generate an income stream that would gradually replace these grants, the governments of the Marshall Islands and the US invested in a compact trust fund (CTF). However, the contributions of the Government of the Marshall Islands fell short because recurrent expenditure was excessive and revenue performance was poor. The value of the CTF dwindled below target, and the

[1] The Compact of Free Association defined the relationship between the US and the Marshall Islands, as a former US trust territory, in which US assistance, including grants, was provided. In 1986, the first compact was signed and, in 2013, it was amended to cover the period up to 2023.

International Monetary Fund (IMF) recommended that fiscal adjustment begin immediately to close the looming revenue gap and achieve fiscal surplus.

2. In 2009, the government initiated a comprehensive adjustment program (CAP) to advance public sector reform as well as promote macroeconomic stability and sustainable growth. Under the CAP, a comprehensive recovery plan for the state-owned Marshalls Energy Company (MEC) was prepared and the Tax and Revenue Reform and Modernization Commission formed to prepare the plans for fiscal reform. These initiatives formed the basis of the government's strategy to address impediments to greater private sector participation and reduce the role of the large and inefficient public sector in the production of goods and services. The public sector program of the Asian Development Bank (ADB) was designed to support the critical areas of reform in the CAP.[2]

B. Expected Impact

3. The expected impact of the program was for the public sector to provide people with more efficient and effective services. In subprogram 1, the design and monitoring framework (DMF) specified two impact indicators: (i) a one-step grade increase in the country performance assessment rating for criterion 15 (quality of public administration), assessed as 2.0 in 2009; and (ii) a one-step grade increase in the country performance assessment rating for criterion 6 (business regulatory environment), assessed as 2.5 in 2009.

4. In subprogram 2,[3] the DMF impact indicators were revised. The program completion report (PCR)[4] based the assessment on the achievement of the revised indicators under subprogram 2. Three impact indicators were identified: (i) a positive score for government effectiveness on the Worldwide Governance Indicators by 2015 from a baseline of –1.28 in 2010; (ii) a one-step grade increase in the country performance assessment rating for criterion 13 (quality of budgetary and financial management) by 2015, from a baseline of 3.0 in 2012; and (iii) a one-step increase in the country performance assessment rating for criterion 15 (quality of public administration) by 2015, from a baseline of 2.0 in 2012.

C. Objectives or Expected Outcome

5. The expected outcome was fiscal sustainability of the government. Under subprogram 1, the outcome indicators were as follows: (i) annual contribution from the general fund to the CTF of at least 3% of gross domestic product (GDP) by the end of FY2012, and (ii) the CTF assessed by the IMF is on track to achieve FY2023 targets under baseline scenario. Under subprogram 2, indicator (i) was updated as having an annual contribution from the general fund to the CTF of at least 3.0% of GDP by the end of FY2013, from a baseline of 0.6% of GDP in FY2011. Indicator (ii) remained the same as in subprogram 1.

D. Outputs

6. To achieve the outcome of fiscal sustainability, the program aimed to deliver five outputs: (i) the government's fiscal discipline improves over the medium term; (ii) the Cabinet enforces restraint on recurrent expenditures; (iii) the Ministry of Finance (MOF) increases tax

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[2] ADB. 2010. *Report and Recommendation of the President to the Board of Directors: Proposed Program Cluster, Loan for Subprogram 1, and Technical Assistance Grant to the Republic of the Marshall Islands: Public Sector Program.* Manila.

[3] ADB. 2012. *Report and Recommendation of the President to the Board of Directors: Proposed Policy-Based Loan for Subprogram 2 to the Republic of the Marshall Islands for the Public Sector Program.* Manila.

[4] ADB. 2014. *Completion Report: Public Sector Program – Subprograms 1 and 2 in the Marshall Islands.* Manila.

revenues; (iv) selected state-owned enterprises (SOEs) improve their performance; and (v) the Cabinet ensures effective stakeholder participation in public sector reform initiatives.

7. The five outputs were further broken down into 15 policy actions under two subprograms (Table 1).

Table 1: Key Actions of the Public Sector Program, by Output

Medium-Term Direction	Policy Actions under Subprogram 1 Single Tranche Release	Policy Actions under Subprogram 2 Single Tranche Release
Output 1: The government's fiscal discipline improves over the medium-term.		
Achievement of fiscal discipline	1.1. Cabinet endorsement of budget targets for FY2011 and FY2012 1.2. Cabinet endorsement of public sector debt management guidelines for FY2011 and FY2012	1.1. Achievement of budget targets for FY2011 and FY2012. 1.2. Budget Coordinating Committee direction to line ministries that preparation of FY2013 budget enforces fiscal restraint. 1.3. Adherence to the public sector debt management guidelines for FY2011 and FY2012. 1.4. Cabinet endorsement of a public sector debt management strategy to become effective in FY2013. 1.5. Parliament introduction of fiscal responsibility legislation.
Output 2: The Cabinet enforces restraint on recurrent expenditure.		
Government expenditure at sustainable levels	2.1 Conduct of an independent review of public expenditure by the CAP Advisory Group and Cabinet endorsement of the Group's report. 2.2 Cabinet endorsement of key CAP recommendations for implementation in the FY2011 and FY2012 budgets. 2.3 Cabinet endorsement of key recommendations from work force audits.	2.1 Implementation through the FY2011 and FY2012 budgets of actions to control recurrent expenditure in the general fund. 2.2. FY2013 budget demonstrates no reversal of fiscal restraint. 2.3. Public sector work force audits completed for 6 other ministries (finance, foreign affairs, internal affairs, justice, parliament, resources and development) 2.4. Action commenced in at least 3 ministries (finance, foreign affairs, and public works) to improve productivity, drawing on the findings of the work force audits.
Output 3: The Ministry of Finance increases tax revenue.		
Tax revenue raised to 20% of GDP and collected in a more efficient and equitable manner.	3.1. Completion of an independent assessment of the tax system by the TRAM Commission and Cabinet endorsement of the Commission's report. 3.2. Cabinet endorsement of time-bound actions (to be performed by 2015) to improve the efficiency and equity of the tax system, with implementation to commence in FY2011.	3.1. Implementation of time-bound actions on track, as evidenced by introduction of tax legislation in Parliament.

Output 4: Selected state-owned enterprises improve their performance.		
Financial performance and corporate governance standards match regional benchmarks	3.1. Endorsement by Cabinet of recommendations for improving SOE performance. 3.2. Cabinet endorsement of good practice principles for 11 SOEs. 3.3. MEC comprehensive recovery plan prepared and endorsed by the MEC Board. 3.4. Implementation of MEC comprehensive recovery plan commenced. 3.5. Cabinet and MEC Board endorsement of actions restructure MED debt. 3.6. MEC Board endorsement of a maintenance and repair account to hold sufficient funds set aside to meet all MEC maintenance and repair needs.	4.1. Continued annual public reporting on SOE performance and progress of the program. 4.2. Adoption of an SOE policy by Cabinet and introduction into Parliament of an SOE Act to give effect to the good practice principles for SOEs. 4.3. Implementation initiated of the time-bound recovery plans for at least 3 SOEs that apply the good practice principles. 4.4. MEC comprehensive recovery plan on track to achieve: (i) full Board independence; (ii) creation of a statement of plan the sets out MEC's strategic direction and performance targets; and (iii) full cost recovery of operating costs and interest costs on the electricity business. 4.5. Actions to restructure MEC debt are implemented, with no reversal: (i) establishment of a financing agreement between the MOF and MEC that will be used to reform and stabilize the MEC; (ii) deferral of principal repayments for 2 years of the existing loan with the Rural Utility Services of the US Department of Agriculture; and (iii) establishment by the MOF and MEC of a debt servicing sinking fund for the financing agreement between the MOF and MEC.
Output 5: Cabinet ensures effective stakeholder participation in public sector reform initiatives.		
Enhanced bottom-up planning and community participation	5.1. Implementation of a public consultation program through stakeholder forum. 5.2. SOE, TRAM Commission, and CAP Advisory Group reports public available.	5.1. Continued implementation of a public consultation program.

ADB = Asian Development Bank, CAP = comprehensive adjustment program, GDP = gross domestic product, MEC = Marshalls Energy Company, MOF = Ministry of Finance, SOE = state-owned enterprise, TRAM = tax and revenue reform and modernization, US = United States.

Source: ADB. 2014. *Completion Report: Public Sector Program – Subprograms 1 and 2 in the Marshall Islands.* Manila.

E. Provision of Inputs

8. ADB provided $14.5 million in the form of program cluster loans, comprising $9.5 million for subprogram 1 and $5.0 million for subprogram 2. The loan size considered the (i) MEC's adjustment costs in refurbishing its major assets and achieving sound financial position, (ii) significance of the policy actions, and (iii) the program's alignment with ADB's Country Operations Business Plan, 2010–2012.[5] Under subprogram 1, the bulk was used for restructuring MEC's sovereign-guaranteed loan with the Bank of Guam.[6] The program also helped partly offset the cost of the fiscal budget's overall financing requirement (equivalent to 0.76% of GDP in FY2012 and 0.75% in FY2013). The loans for subprogram 1 and 2 were fully disbursed on time.

9. ADB provided technical assistance (TA)[7] amounting to $900,000.[8] The TA project envisaged the same impact, outcome, and outputs as the program (paras. 5–10). The TA project prepared a public sector debt management strategy and fiscal responsibility and debt management legislation, standard operating procedures to improve MOF processes, an SOE policy, and implemented MEC's comprehensive recovery plan. Despite successful completion of these activities, the TA outputs were not fully achieved (paras. 22–29). The TA projects helped improve the government's fiscal discipline and the operations of MEC, and facilitated stakeholder participation and consultation. Tax revenue increased but the approval of tax legislations remained pending in Parliament. Hence, the reforms could not be fully implemented. Similarly, debt management and implementation of SOE reforms were also delayed pending approval of the SOE and fiscal responsibility legislations. The envisaged TA outcome to achieve fiscal sustainability was not achieved because of continuing fiscal deficits (paras. 22–23).

10. The TA project was complemented by other ADB TA projects. In 2010, ADB approved a grant[9] to support MEC's reforms, improve MEC's efficiency, and contribute to MEC's recovery plan. In the same year, ADB approved a TA project to help develop the fiscal management model adopted and used during the FY2013 budget process.[10] ADB's regional TA for private sector development in the Pacific[11] also provided support to complete the draft new SOE legislation.

F. Implementation Arrangements

11. The MOF was the executing agency responsible for implementing the program cluster, including program administration, disbursements, and maintenance of program records. The envisaged program steering committee was not established. Instead, the government's budget committee provided a program component oversight to monitor fiscal targets and other public finance reforms, the MEC Board for the MEC comprehensive recovery plan, and a work force

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[5] ADB. 2010. *Country Operations Business Plan: Marshall Islands, 2010–2012. Manila.*

[6] $8,542,445 (89.9%) was initially onlent to MEC, which was followed by an additional $1 million. The total amount is slightly greater than $9.5 million because of changes in exchange rate.

[7] ADB. 2010. *Technical Assistance to the Republic of the Marshall Islands for Supporting the Public Sector Program.* Manila.

[8] The initial amount approved was $600,000, which was followed by an additional amount of $300,000.

[9] ADB. 2010. *Proposed Grant Assistance to the Marshall Islands for Improved Energy Supply for Poor Households.* Manila.

[10] ADB. 2010. *Pacific Economic Management-Enhanced Economic Management (Subproject 2).* Manila.

[11] ADB. 2009. *Pacific Private Sector Development Initiative Phase II.* Manila.

committee facilitated by the Public Service Commission for the human resources component. The PCR indicated that the implementation arrangements were adequate to deliver the program outputs. This validation notes that the program could have benefited more from a centralized oversight body as envisaged in the design.

12. All covenants under the loan agreements were complied with. No covenants were modified or waived during the program period.

II. EVALUATION OF PERFORMANCE AND RATINGS

A. Relevance of Design and Formulation

13. The PCR assessed the program *relevant*. The program was based on the government's reform agenda and was in line with the Marshall Island's national development plan.[12] It was also aligned with the Marshall Islands' country operations business plan for 2012–2014[13] and ADB's Pacific Approach for 2010–2014.[14] The program design reflected lessons from the earlier ADB policy program in the Marshall Islands and the Pacific, as well as ADB's approach to engaging with weakly performing countries, by adopting a country-led set of policy actions, and initiating long-term policy dialogue and providing targeted technical assistance.

14. Adjustments were made in the triggers, particularly for the proposed bills under the program. In view of the time involved in the approval process of envisaged legislations, the policy actions for the fiscal responsibility amendment bill and the SOE bill were changed from a requirement of endorsements by Parliament to only introduction of these bills in Parliament. These changes indicate that the lengthy process of legislation in the context of the Marshall Islands was not realistically taken into account during program preparation.

15. Given the fragile fiscal condition that the Marshall Islands faced, the use of a cluster program modality was considered appropriate in that it allowed for ongoing policy dialogue with government and for initial actions from subprogram 1 to be built into subprogram 2. The associated TA appropriately complemented the other ADB TA projects for the sector (para. 10).

16. The PCR assessed the program design and DMF as over ambitious in scope and time frame, and allowed for achieving challenging targets, such as the parliamentary approval of key legislations to fully implement the reforms. The PCR stated that the outcome of the government to achieve fiscal sustainability would have required more time than the period covered by the two subprograms, and would depend highly on factors beyond the control of the program. The PCR indicated that the output, "government's fiscal discipline improves over the medium term," would appropriately have been the program's intended outcome since achieving it was partly dependent on completing the policy actions. This validation shares the PCR's view that the program goals could have been refined further to reflect more appropriately the intended outcome arising from the policy actions and time available. The issue of time involved in the approval of new legislation was addressed by adjusting the triggers but these should have been anticipated at design preparation.

[12] Government of the Republic of the Marshall Islands. 2001. *The Strategic Development Plan Framework, 2003–2018.* Majuro.
[13] ADB. 2009. *Country Operations Business Plan: Marshall Islands, 2010–2012*. Manila.
[14] ADB. 2009. *ADB's Pacific Approach 2010–2014*. Manila.

17. Notwithstanding these design issues, this validation assesses the program *relevant*. The policy actions taken were appropriate in addressing the fragile fiscal situation and constraints to achieving fiscal sustainability. The policy measures initiated provided the needed momentum for the reforms to be implemented, although not fully because of pending legislations in Parliament. However, this validation is of the view that the program design could have been made simpler, clearer, and less ambitious in scope and in the timeline for achieving the targets.

B. Effectiveness in Achieving Program Outcome and Outputs

18. The PCR assessed the program *less than effective* in achieving the intended outcome of fiscal sustainability. The two outcome indicators specified in the DMF were not achieved. First, the performance target for the CTF as assessed by the International Monetary Fund (IMF)—to be on track to achieve FY2023 targets—was not met. Based on the 2013 Article IV staff report of the IMF, the Marshall Islands needed to reach a budget surplus target of 5% GDP by FY2016 to ensure that the CTF is on track to replace the compact grants in FY2024. Unless further fiscal improvements are achieved, projections suggest that this target would not be met.

19. The second outcome indicator was for the annual contribution from the general fund to the CTF to reach at least 3.0% of GDP by the end of FY2013, from a baseline estimated at 0.6% of GDP in FY2011. This was not achieved. The related output targets for FY2011 and FY2012 budgets were actually met with fiscal surplus above 3% of GDP. However, a fiscal deficit equivalent to 0.8% of GDP was registered in FY2012 and FY2013. As a result, no transfers were made into the CTF during this period because of the deficits. The PCR reported that this situation is not likely to improve with annual budget deficits beyond FY2015, expecting the situation to widen to about 2% of GDP.

20. As regards the expected outputs, the targets for output 1 (government's fiscal discipline improved over the medium term) were achieved. The ratio of current expenditure to GDP of 48.0% was successfully lowered compared with the baseline of 51.6% in FY2011. The ratio of government debt-to-GDP in FY2013 was 51.8%, less than the baseline of 60.3% of GDP in FY2011. The policy action on the amendment to the Financial Management Act 1990 to enhance fiscal responsibility and debt management was introduced in Parliament. However, pending Parliament approval, the required fiscal and debt management strategies could not be made fully effective, which are essential for effective expenditure control.

21. For output 2 (restraint on recurrent expenditure) the target to reduce government expenditure (as a percentage of GDP) below the baseline level was not achieved. Government wages and salaries for FY2013 were 20.8% of GDP, slightly more than the baseline of 20.1% in FY2011. All policy actions relating to output 2 were carried out, including an independent review of public expenditure by the CAP advisory group and its preparation of specific actions to restrain recurrent expenditure in the budgets of FY2011 and FY2012.

22. Output 3 (MOF tax revenue increased) target was achieved with the ratio of tax revenue-to-GDP of 16.5% in FY2013, more than the 14.3% FY2011 baseline and target ratio of 16.2% by 2015. The tax reform was introduced in Parliament but remained pending for action.

23. For output 4 (performance of selected SOEs improved), the targets were not achieved. The ratio of subsidies to SOEs to GDP for FY2013 was 5.3%, which was higher than the

FY2011 baseline of 3.0%. The consolidated rate of return on equity of SOEs in FY2012 remained negative at –11.3. Nonetheless, a key achievement in output 4 was the successful implementation of the comprehensive recovery plan for MEC, which helped MEC set strategic direction and performance targets, and keep it on track toward achieving full cost recovery. The cash flow savings from restructuring were used to strengthen the financial position of MEC and finance priorities under the comprehensive recovery plan. In FY2013, MEC produced a profit for the first time in 10 years of $2.1 million. The SOE legislation was introduced in Parliament, which when passed, will improve governance and performance of SOEs.

24. Lastly, output 5 (effective stakeholder participation in public sector reform initiatives by the Cabinet) was achieved. MOF carried out public program consultations on reform initiatives, engaging all key stakeholders. The second development partners' meeting was conducted as planned, which gave the government opportunity to present its public sector program and discuss reform and development priorities.

25. This validation assesses the program *less than effective*. Of the five outputs specified in the DMF, two were not achieved even though the associated policy actions were largely met with some adjustments in the triggers. The envisaged outcome of financial sustainability was not realized.

C. Efficiency of Resource Use in Achieving Outcome and Outputs

26. The PCR assessed the program *less than efficient*. The government complied with the preconditions for the timely release of funds and disbursements were not delayed. However, there were delays in the approval by Parliament of the amendment to the Financial Management Act, tax reform, and SOE legislations constrained the full implementation of the reforms, resulting in intended outputs not fully achieved. The design did not adequately take into account the lengthy process involved in passing new legislation. The program implementation period was not sufficient to substantially achieve the outcome of fiscal sustainability. This validation assesses the program *less than efficient*.

D. Preliminary Assessment of Sustainability

27. The PCR rated the program *less than likely sustainable*. The legislation introduced in Parliament needs to be passed for key envisaged reforms to be fully implemented. If passed, further assistance from development partners will likely be needed to implement the reforms. The fiscal deficits recorded during the program period indicated that fiscal sustainability has not yet been achieved. Consequently, no transfers were made to the CTF. Nonetheless, reform momentum was gained through the program, which can be pushed further with the approval of new legislation. This validation assesses the program *less than likely sustainable*.

E. Institutional Development

28. The program did not achieve fiscal sustainability, but there were significant developments in institutional capacity. The fiscal reforms initiated, such as the enforcement of fiscal restraint, helped strengthen budget processes. Public sector debt management was improved with the adoption of debt management guidelines and debt management strategy. Tax administration was improved. However, tax reforms were not fully implemented because the enabling legislation was not passed during the program period. Work audits were conducted to improve productivity in public service. The recovery plan for MEC was

implemented, which helped restructure its Board, adopt new financial management policies, and set out strategic direction toward full cost recovery. The new legislation relating to tax reforms, financial management, and SOEs introduced in Parliament, once passed, is expected to further build the public sector's capacity in fiscal management and administration. This validation assesses the institutional development of the program *significant*.

F. Impact

29. The targets for the impact indicators specified in the DMF were not met. Based on the Worldwide Governance Indicators, the government effectiveness score for the Marshall Islands deteriorated to –1.65 in 2012, significantly lower than the positive score targeted in the DMF. The one-step grade increase targeted in the country performance rating for quality of budgetary and financial management was not achieved. In 2013, the country performance rating was 3.0, which was the same as the 2012 baseline. For the criterion on quality of public administration, the program targeted a one-step grade increase in country performance. In 2013, assessment rating was 2.5, which was only a half-step increase from the 2012 baseline of 2.0. With these metrics, the envisaged impact of the public sector providing people with more efficient and effective services was not fully realized. This validation assesses the impact of the program *moderate*.

III. OTHER PERFORMANCE ASSESSMENTS

A. Performance of the Borrower and Executing Agency

30. The PCR rated the performance of the borrower and executing agency *less than satisfactory*. The PCR indicated that the government's CAP was ambitious and challenging to implement, and had inconsistencies that were carried through to the public sector program. This validation notes that the PCR did not further elaborate what the inconsistencies are in the CAP. The PCR assessed the MOF's performance satisfactory in developing the reforms, drafting the needed legislation, and initially engaging stakeholders. However, these were not sustained to achieve broad political buy-in. As a result, the much needed legislation remained pending in Parliament. While the political process is beyond the control of the executing agency, the PCR is of the view that sustained multi-partisan consultation should have been undertaken on the need to pass the new legislation. This validation shares the PCR's view and considers the borrower and executing agency's performance *less than satisfactory*.

B. Performance of the Asian Development Bank

31. The PCR assessed ADB performance *less than satisfactory*. ADB fielded one fact-finding mission for subprogram 1 and also one for subprogram 2. One review mission for subprogram 1 was carried out and none for subprogram 2. No program completion review mission was fielded for the two subprograms; only a desk review was carried out. The PCR indicated that the program design was overly ambitious in the Marshall Islands' context of limited government capacity and pace of reforms. The activities completed under the associated TA project complemented the reform program. However, the strategies formulated could not be fully implemented because the enabling laws remained pending in Parliament. The program period was unrealistic given the extent of reforms needed to achieve fiscal sustainability. The process involved in legislation and possible political resistance to reforms should have been adequately anticipated at appraisal. The outcome and impact statements in the DMF should have also been aligned with the policy actions of the program. This validation considers the performance of ADB *less than satisfactory*.

IV. OVERALL ASSESSMENT, LESSONS, AND RECOMMENDATIONS

A. Overall Assessment and Ratings

32. The PCR rated the program *less than successful*. This validation also considers the program *less than successful* (Table 2). The envisaged outcome of fiscal sustainability was not realized. The fiscal position continued to register deficits, and the CTF was not on track to replace the compact grants. The program was *relevant* to the Marshall Islands' fragile fiscal situation and addressed the constraints to achieving financial sustainability. It was *less than effective* in that the expected outputs were not fully achieved and expected outcome was not realized. It was *less than efficient* because of delays in the approval of the needed reforms, the process of which was not adequately taken into account in the program design. It was *less than likely sustainable* in that fiscal deficits are expected to continue and, as legislation remains pending for approval, the reforms cannot be fully implemented.

Table 2: Overall Ratings

Criteria	PCR	IED Review	Reason for Disagreement and/or Comments
Relevance:	Relevant	Relevant	
Effectiveness in achieving outcome and outputs:	Less than effective	Less than effective	
Efficiency in achieving outcome and outputs:	Less than efficient	Less than efficient	
Preliminary assessment of sustainability:	Less than likely	Less than likely	
Overall Assessment:	**Less than successful**	**Less than successful**	
Institutional development:	Not rated	Significant	Refer to para. 28.
Impact:	Not rated	Moderate	The targets for impact were not met (para. 29).
Borrower and executing agency:	Less than satisfactory	Less than satisfactory	
Performance of ADB:	Less than satisfactory	Less than satisfactory	
Quality of PCR:		Satisfactory	Refer to para. 36.

ADB = Asian Development Bank, IED = Independent Evaluation Department, PCR = program completion report.
Source: ADB Independent Evaluation Department.

B. Lessons

33. The PCR presented valuable lessons. This validation particularly notes the observation that the program design was overambitious and should have taken into account the historically slow pace of reforms in the Marshall Islands and political sensitivity to the reforms. The outcome and impact statements and targets in the DMF could have been more realistic in view of the country's context. Setting conditions relating to budget processes and/or controls and lower targets may have been more appropriate for the program. ADB support in policy dialogue is important for public sector reform in the Marshall Islands. Sector reforms should proceed at the same pace as the government's capacity to implement the reforms. The lessons identified are appropriate, and this validation has no further lesson to add.

C. Recommendations for Follow-Up

34. The PCR gave suitable program-related recommendations. The MOF should continue efforts to have the pending legislations approved by Parliament, and implement the needed reforms once they have been passed. To achieve fiscal stability and sustainability, additional TA support is needed to continue the initiatives and support the action plans. The general recommendations are appropriate. Reforms should be prioritized and arranged in sequence. Pooling resources and sharing experiences in the Pacific region will be useful to institutionalize best practices and leverage shared resources.

V. OTHER CONSIDERATIONS AND FOLLOW-UP

A. Monitoring and Evaluation Design, Implementation, and Utilization

35. The MOF complied with the covenant to establish a program performance monitoring system. While the extent of the system's use was not discussed in the PCR, it was apparent that the monitoring and evaluation of the program was based on the DMF and policy matrix. The DMF could have more appropriately reflected the intended impact and outcome arising from the policy actions.

B. Comments on Program Completion Report Quality

36. This validation rates the PCR quality *satisfactory.* The PCR provided evidence to substantiate the ratings. The PCR's discussion of the program outputs and related issues was detailed and informative. The lessons drawn from the findings and the recommendations were sound. Appendix 1 clearly summarized the program achievements based on the DMF. The status of actions on the policy matrix presented in Appendix 2 was informative.

C. Data Sources for Validation

37. Sources used for this validation were the PCR, the report and recommendation of the President for subprogram 1 and subprogram 2, loan review mission reports, and the TA completion report.

D. Recommendation for Independent Evaluation Department Follow-Up

38. The Independent Evaluation Department may conduct a program performance evaluation to sharpen the understanding of issues and lessons learned, to thus benefit future program design.