Chair’s Summary

1. Asian Development Fund (ADF) deputies, representatives from ADF developing member countries (DMCs), Asian Development Bank (ADB) Management and staff, and observers from ADB’s Board of Directors and other international organizations met in Manila, the Philippines on 28–30 October 2015 for the first ADF 12 replenishment meeting.

2. ADB President Takehiko Nakao opened the meeting. He expressed his condolences to the people of Afghanistan and Pakistan affected by the recent earthquake. He highlighted the unique nature of the ADF 12 replenishment, the first replenishment following the combination of ADF lending operations with the ordinary capital resources (OCR) balance sheet. While the combination allows ADB to substantially increase its concessional assistance (CA), he stressed the continued need for donor contributions to support grant operations in CA countries. He highlighted ADB’s commitment to ensure the best use of its expanded resources.

3. Donors recognized ADB’s contribution to development in the region, while recognizing that CA countries continue to face both conventional, and new and emerging challenges. They called on ADB to continue addressing global and regional development challenges in CA countries. Donors appreciated ADB’s commitment to upscaling resources to the poorest and most fragile countries resulting from the ADF–OCR combination.

4. ADF recipient countries thanked ADB for its continued support, and for scaling up this assistance through the ADF–OCR combination. They welcomed the focus on disaster mitigation and climate change. They highlighted the importance of strengthening absorptive capacity. They called on ADB to continue providing CA to bridge the financing gap as countries make efforts to strengthen mobilization of domestic resources. They highlighted ADB’s strategic advantage in financing large-scale infrastructure projects, developing capacity, and strengthening regional cooperation.

5. Donors expressed broad support for the strategic and operational priorities proposed by ADB for the ADF 12 period. Some donors asked for further clarity on priority vii (supporting regional public goods), in particular ADB’s support to specific regional institutions. ADB will use its CA to support inclusive growth and sustainable development in CA countries. This support will focus on seven key priorities: (i) mainstreaming gender in operations, (ii) addressing fragile and conflict-affected situations, (iii) promoting food security, (iv) strengthening private sector development, (v) improving governance and capacities, (vi) strengthening preparedness and response to climate change and natural disasters, and (vii) supporting regional public goods.

6. It was pointed out that the strategic priorities for inclusive growth and sustainable development are guided by the midterm review of the Strategy 2020, which applies to both OCR and ADF operations. Donors welcomed ADB’s commitment to consult with all stakeholders, including the ADF contributors, in the process of drafting its new long-term strategy. Some donors expressed the view that no parallel discussions on ADB’s priorities and strategic orientation should take place in the ADF 12 replenishment negotiations and that the ADF 12 replenishment negotiations should explicitly focus on the grant-receiving countries.
7. To implement these priorities, sustainable infrastructure development will continue to be a mainstay of ADB’s operations, encompassing investments in clean energy, sustainable transport, water, and urban development. ADB will expand its social sector development interventions to complement its support for infrastructure and to deepen the inclusiveness of its overall assistance under ADF 12. Such support will be manifested in operations in the education and health sectors as well as for social protection.

8. Donors stressed the importance of aligning ADB’s support with the international development agenda, defined by the Sustainable Development Goals, the Addis Ababa Financing for Development Conference, and the United Nations Framework Convention on Climate Change 21st Conference of Parties (COP21). They commended ADB for its pragmatic approach to provide support for the broad international development agenda within the context of its own strategic framework and comparative advantage. Donors urged ADB to continue working together with other development partners in responding to country needs. They also stressed the need for coherence between ADF replenishment discussions and ADB’s upcoming new corporate strategy leading to 2030, which should include consultations on the future role of the ADF, bearing in mind the changing realities for the poorest countries and the expected graduation of ADB DMCs from access to grants only to blend to OCR-only.

9. With respect to inclusive growth, donors called for an approach that is focused on outcomes and is better informed by diagnostics and analysis. Donors and ADB agreed on the need for a focus on results and outcomes, rather than inputs and a clear articulation on how ADB’s interventions will support inclusive growth, especially for poor, vulnerable and marginalized groups. Donors welcomed ADB’s commitment to double financing for climate change mitigation and adaptation, and some called for greater efforts and more ambitious targets for renewable energy and asked for information on how the climate commitments would be implemented.

10. ADB was encouraged to further deepen gender mainstreaming, including improved measurement of gender disaggregated data, and to expand investment in gender targeted projects. ADB was also asked to further improve the gender balance at all levels of the organization.

11. The unique challenges of fragile and conflict affected situations (FCAS) were recognized. ADB’s increasing presence in Pacific countries, many of which are identified as FCAS, was welcomed. Donors called on ADB to continue expanding staff capacity and resources for project management in FCAS that require systematic conflict/fragility analysis and better preparation and supervision. Donors in particular called on ADB to strengthen its expertise, staff, and internal incentives for conflict sensitive project management in FCAS. The need for streamlining internal processes—including those related to procurement—for operations in FCAS, as well as to pay greater attention to project design and conflict sensitivity was recognized.

12. Donors commended ADB for its good performance in private sector development and operations in CA countries, and encouraged ADB to focus on expanding public-private partnerships and job creation.

13. In the area of governance and capacity development, the need to increase efforts to build further capacity, including supporting private sector development was recognized. Donors also stressed that the low level of domestic resource mobilization in most recipient countries is an impediment to development that needs to be tackled with highest priority, in line with the
Addis Ababa Action Plan. Some suggested that an analysis of the existing problems and the countries’ potential to increase domestic resource mobilization should be an integral part of all country partnership strategies.

14. The importance of infrastructure development for inclusive and sustainable development was highlighted. Donors emphasized the need for a stronger focus on sustainability in infrastructure, local ownership and long-term maintenance and for strengthening linkages with climate change and inclusive growth.

15. A number of donors also called on ADB to expand support for the financial sector.

16. Donors noted that ADB has made good progress on internal reforms since the ADF XI midterm review, but that staff capacity should be further strengthened and business processes more streamlined to improve efficiency and effectiveness, including in simplifying procurement processes. Donors also called for a stronger focus on project readiness, completion rate and quality and speed of implementation to improve project performance.

17. A number of donors requested further clarification on the specific challenges faced by grant-eligible countries, and ADB’s approach in these countries, including an analysis of the economic, fiscal/debt and social situation of these countries, of which most are fragile states. They also requested a more specific and integrated discussion of the role and expected results and outcomes the various components financed by grant resources would play, as grants are the subject of the financial replenishment.

18. Donors welcomed the timely study and supported the recommendations made by the Independent Evaluation Department on the ADF X and XI operations. They also welcomed ADB’s management response and concurrence with the recommendations. Donors reiterated the need to better operationalize ADB’s approach to inclusive growth, towards a more outcome-oriented approach, and the importance of building the inclusive development agenda around core areas of operations, especially infrastructure. Management agreed with the independent evaluation on a portfolio approach towards inclusive growth. ADB has developed guidelines for stronger analysis in country partnerships strategies to deliver a better understanding of the development context. The discussion also focused on the potential tradeoff between ensuring contributions to inclusive growth and increasing complexity of project design and implementation.

19. Donors welcomed the improving success rates of ADB’s operations and called on ADB to solidify the improving trend from the earlier low success levels. Discussions centered on the wide variation of success rates across sectors and criteria and clarification was sought on its causes. It was recognized that the country development context needs to be taken into account (through stronger analytical work, including at the project design stage), especially for FCAS. Donors also noted that ADB should continue focusing its support in areas of comparative advantage. At the same time, but at limited scale, ADB may consider enhancing its investments in sectors where results have been strong (such as health). ADB must remain responsive to the needs of its DMCs, while continuing to focus on niche areas for the Bank.

20. In order to better deliver its assistance to CA countries, ADB proposed a number of revisions to the performance-based allocation system. These include:
   (i) introducing a base allocation of $6 million per year to CA countries,
   (ii) discontinuing the 4.5% set-aside for the Pacific DMCs,
   (iii) providing exceptional support to Afghanistan at about the level of ADF XI,
21. Donors expressed broad support for the proposals. Recipient countries welcomed the proposals for increased support. With respect to proposal (ii), ADB and donors agreed that a transition arrangement would be developed for Papua New Guinea as its CA allocations would be negatively affected by the removal of the 4.5% Pacific set-aside. With respect to proposals (i)–(iv) donors also stressed that increasing allocations should go hand in hand with developing absorptive capacity (through increased technical assistance and ADB staff on the ground) and one donor sought further analysis of an increase to the base allocation beyond $6 million. To ensure that allocations would be used most efficiently, ADB committed to review the special allocations to Afghanistan and Myanmar at the ADF 12 midterm review and adjust them if required. With respect to proposal (v), ADB and donors agreed to separate the 10% set-aside for grant DRF (estimated at $218 million) from the contingency fund. A number of donors also requested that the Independent Evaluation Department evaluate the DRF at the ADF 12 midterm review. In relation to proposal (vi), consideration should also be given to a transition arrangement for Bhutan and Lao People’s Democratic Republic. ADB also clarified that Nauru would not be affected by the gap country proposal. With respect to proposal (vii), it was agreed that while country performance assessments would, in principle, be conducted every two years, increasing the frequency could be flexibly considered if the situation warranted it. With respect to proposal (viii), some donors felt that the grant contingency may not be sufficient to absorb potential fluctuations in grant demand, while several others noted that retaining this high amount of grants contingency funds may not optimize the use of resources. ADB clarified that reducing the grants contingency to a lower level entails the risk of underfunding. There was broad agreement to retain the contingency (now renamed reserve for changes in debt distress) at the proposed level (i.e. $436 million, or 20% of ADF grant financing in the base case scenario), with the condition that the use of unutilized resources would be reviewed during the ADF 12 midterm review.

22. ADB presented its case to establish the Supplementary ADF Window (SAW) to address new challenges by accommodating the willingness of some donors to provide additional contributions. The emerging challenges that the SAW was proposed to address include disaster risk reduction (DRR) and supporting the provision of regional public goods. ADB took feedback from donors into consideration and presented new options for governance and financing arrangements to meet these challenges. In terms of proposed objectives, there was broad support among donors for DRR and to further mainstream this into ADB core operations. A number of donors requested ADB to further develop the case for supporting regional public goods. While recognizing the importance of strengthening regional health care systems, some raised the question if ADB should focus on this area as health is currently not one of ADB’s priority areas. It was agreed that the ADF 12 midterm review would provide a good opportunity to review ADB’s progress in addressing these emerging challenges.

23. Some donors also expressed the view that ADB should make a stronger case for its proposal to provide grants to all CA countries. It was argued that an extension of the eligibility
for grants was a departure from the current practice of providing grants to heavily indebted countries.

24. Discussions further focused on the governance and financing arrangements to enable ADB to address these challenges. With respect to governance arrangements, donors expressed preference not to fragment the governance structure, while some also noted that flexibility may need to be considered in view of the changing nature of the ADF. Several donors expressed reservations about establishing a new set-aside for DRR or regional public goods within the ADF. Most donors stressed that the objectives of DRR should instead be mainstreamed, possibly through the existing DRF set-aside. Fewer donors also suggested that regional public goods get mainstreamed through the existing regional set-aside. In terms of financing options, it was recognized that providing flexibility in donor contributions through the use of additional contributions (both above-the-line and below-the-line budget provisions) was the most practical approach.

25. ADB proposed its operational program in CA countries for the ADF 12 period. Donors welcomed ADB’s commitment to substantially increase its support to CA countries, especially FCAS, resulting from the ADF–OCR combination. Some donors noted that project pipeline data showed a decrease in certain thematic priorities. ADB committed to ensure that strong focus to the agreed priorities would be given in further developing the pipelines.

26. Donors supported the proposed replenishment of the Technical Assistance Special Fund. They recognized the need to scale up technical assistance (TA) in line with the increase in project operations, with a specific focus on FCAS. Donors also highlighted the importance of the ongoing TA reforms, including at the Country Partnership Strategy level, to improve the effectiveness and efficiency of the TA program. ADB clarified that the proposed TASF replenishment of $461 million alone is not sufficient to meet TA demand, but that it provides a solid basis for generating additional grant-funded TA to meet the demand.

27. ADB sought donors’ guidance and endorsement on the following financial issues relating to the financing framework: (i) proposed financing scenario, (ii) proposed contribution framework, (iii) use 2-month average daily exchange rates from 1 Nov–31 Dec 2015, (iv) use 10% average inflation rate to determine eligibility of unit of obligation, (v) set aside $155 million liquidity, (vi) proposed standard encashment schedule, and (vii) discount rate of 1.8% for the accelerated note encashment program.

28. There was strong support for the financing scenario that allows for additional contributions to support DRR. A number of donors also expressed support for the financing scenario incorporating support for regional public goods. ADB committed to further build the case for supporting regional public goods. A number of donors highlighted the importance of ADB’s commitment to substantially reduce donor contributions as a result of the ADF–OCR combination, while at the same time allowing for flexibility in contributions to address the emerging regional challenges and maximizing support for the poorest countries.

29. Donors further expressed broad support for proposal (ii). Some donors clarified that their support for their proposed contribution framework was to be understood as a broad principle as the indicative framework is to be used as a reference point. Donors also endorsed proposals (iii)–(vii). One donor pointed out that the internal financial planning for the ADF contribution was based on the previous standard encashment schedule; in case a deviation would not be approved the donor would have to adhere to the previous encashment schedule. Some donors inquired if there would be scope to increase the OCR net income transfer. ADB clarified that
under the current-less favorable-financial conditions, ADB had maximized the transfer. Some donors also inquired about the implications of the financing gap. ADB clarified the nature of the financing gap, that this was a technical gap, and that it was a feature of multilateral replenishments, following which there was broad consensus among donors.

30. Donors also endorsed the proposals related to the review of financial policies of ADF grant operations. These include (i) shifting calculation of commitment authority to US dollars, (ii) converting ADF liquidity to US dollars, (iii) establishing a foreign exchange buffer of 25% of the projected encashment, (iv) holding a prudential minimum liquidity of at least 50% of the 3-year projected cash outflows, and (v) setting aside liquidity based on target maximum commitments in the first half of a year and projected annual investment income.

31. It was agreed that the second and concluding pledging meeting for ADF 12 will take place in Kathmandu, Nepal on 24–26 February 2016. Topics to be discussed at the second meeting include:
   (i) Development context of ADF grant countries including economic outlook and the case for the ADF 12 grant replenishment,
   (ii) Supporting DRR,
   (iii) Supporting regional public goods,
   (iv) Updated Concessional Assistance Policy,
   (v) Review of country classifications under ADF 12,
   (vi) Enhancing relevance of policy based lending,
   (vii) ADF 12 Donors’ Report, including expected results and outcomes; and
   (viii) Draft Resolution of the Board of Governors.

32. Donors expressed their desire for management to make future papers more concise to reduce repetition across papers and enhance clarity.

33. In addition, ADB would conduct an initial consultation on its new long-term strategy and results framework. ADB and donors also agreed to continue the constructive dialogue between the replenishment meetings.