

EXECUTIVE SUMMARY

The Asian Development Fund (ADF) is a central instrument of the international community for reducing poverty in the Asia and Pacific region. ADF represents an effective partnership between the international community, the Asian Development Bank and ADF client countries. Established in 1973, ADF is the only multilateral development bank concessional fund dedicated exclusively to the economic and social development of the region. Resources of the Fund come mainly from contributions of donor members (Donors) of the Asian Development Bank. ADF has been replenished seven times. Over the eight-month period October 2003 – May 2004 Donors met on four occasions to plan a further replenishment of the Fund (i.e. ADF IX). The ADF IX replenishment will cover the period 1 January 2005 – 31 December 2008.

A. Reducing Poverty in Asia and the Pacific – Achieving the Millennium Development Goals

Reducing poverty remains the overarching goal of ADF. Despite progress in reducing poverty in Asia and Pacific over the last decade, almost two-thirds of the world's poor live in the region. The mixed record on non-income poverty is reflected in the millions of children who continue to live in hunger, slow progress in reducing maternal and child mortality, and deteriorating education systems in many countries. Even though the Asia and Pacific Region is on track to meet the Millennium Development Goal (MDG) target of reducing by half the proportion of people living on less than a dollar a day it is unlikely to meet the goals for reducing non-income poverty. Asian Development Fund (ADF) IX operations and assistance to reduce poverty in the region will require among other things a continued and sharpened focus on sustainable economic growth, inclusive social development, and good governance, supported by an emphasis on the cross-cutting issues and thematic priorities of private sector development, regional cooperation, and the mainstreaming of environment and gender. Effective implementation in ADF IX will require a consistent focus on results and development effectiveness. In this context, the strategic emphasis by ADB will shift to improve implementation of operations.

Addressing the global development agenda in ADF IX. Donors agreed that the goals, strategies, and policies of ADF IX should support the priorities of the global development agenda applied to the needs and conditions of the region. This agenda incorporates agreements that have emerged in multilateral dialogues, including the Millennium Summit and Declaration and the Monterrey Consensus, highlighting the need for sound development policy and financing; the Johannesburg Summit focusing attention on sustainable development; the Rome Declaration reflecting the international financial institutions' commitment to harmonize operations; and the Doha Trade round giving priority to improving trade rules that benefit all countries and contribute to poverty reduction globally.

Enhancing ADB's Poverty Reduction Strategy. Donors assessed ADB's progress in reducing poverty under the framework of the ADB wide Poverty Reduction Strategy. Donors reaffirmed that the three pillars of the Strategy—support for sustainable economic growth (including trade and private sector development), inclusive social development, and good governance—continue to provide a sound framework to guide ADF IX-assisted programs and projects. Implementation of the Strategy's thematic and cross-cutting concerns must be strengthened including a new focus on capacity

building. Donors endorsed the key recommendations of the Strategy. ADB will strengthen overall Strategy implementation; improve methods for measuring poverty impacts; introduce more flexible project and program modalities; emphasize results in all ADB operations; strengthen alignment with national poverty reduction strategies, and collaborate more effectively with its development partners.

B. Using Development Results to Improve Development Effectiveness and Impact

From results to development effectiveness. Donors stressed the importance of improving the development effectiveness and impact of ADF IX operations through careful attention to results at project, sector, country, and regional levels. ADB's newly established Results Management Unit (RMU) has a primary responsibility for the design and monitoring of the results system in ADB. Donors recommended that ADB nurture a strong "results culture" across the organization involving staff at all levels under the leadership of senior Management, including the ADB President, and with the full support of all stakeholders. The RMU will also develop and implement indicators that define progress on strategic outcomes. Monitoring at three broad levels is important: at country, institutional, and program and project levels. Benefits of managing for development results will include, among others, stronger project quality at entry, better prioritization based on results, greater accountability, more effective resource use, and enhanced credibility for ADB in the donor community and in ADF client countries.

Managing for development results. ADB will develop results-based country strategies that are aligned with nationally owned poverty reduction strategies. ADB will use indicators developed in cooperation by other multilateral development banks and development partners in-country. Country strategies will identify clear objectives, describe a credible plan for achieving those objectives, and specify time-bound indicators. ADB will continue to establish a more results-oriented monitoring and evaluation system grounded in the principle of country ownership that will support more effective management of the ADB's Poverty Reduction Strategy. In partnership with ADF clients, country strategy indicators will focus on a subset of results reflecting the national poverty reduction strategies. ADB's results framework will: (i) measure impact and provide indicators for private sector development and private sector operations, gender, good governance, and environmental stewardship; (ii) examine aggregate achievement of Country Strategy objectives; (iii) monitor alignment between ADB operations and its Strategy at the project, sector, and country levels; and (iv) support stronger institutional capacity to implement the Strategy. ADB will reorient staff incentives to reward achievement of measurable development outcomes rather than lending targets.

Harmonization to achieve development effectiveness. Donors agreed that harmonization and improved division of labor across institutions reduces transaction costs for client countries and increases development effectiveness. Donors recommended that ADB deepen its collaboration with the Bretton Woods Institutions, specialized agencies of the United Nations, and bilateral development agencies. Such collaboration should span country level planning, implementation, analytical work, co-financing, sector wide approaches (SWAPs), policies –including those on performance based allocation- and measuring and monitoring accomplishments in relation to the MDGs and other poverty-related indicators. Donors recognized that ADB has taken the lead in donor coordination in some developing member countries (DMCs) where it has

strengths and where DMC Governments have requested such involvement. ADB will intensify further cooperative agreements with its development partners. At a country level, and working through better resourced Resident Missions with appropriate delegation of authority, it will strengthen donor cooperation within the framework of national poverty reduction strategies.

C. Recognizing and Rewarding Performance – Using Resources Effectively

Strengthening the Performance-Based Allocation Policy. By rewarding strong performance, ADB's policy on Performance-Based Allocation (PBA) aims to put ADF resources to where they will be most effectively used. Donors agreed that the PBA system would also be used to allocate grants, other than technical assistance grants, in ADF IX. To serve greater transparency, ADB will bring disclosure on country performance ratings into alignment as early as possible with the International Development Association (IDA) and prepare a roadmap for full disclosure. Donors underlined the importance of clear institutional accountabilities for ADF resource allocation and agreed to Management's proposal to situate the PBA exercise in an organizational focal point outside of operations departments. Given that triggers have proven costly to implement they will be discontinued. Consistent with the ADF IX emphasis on development effectiveness, an increased formula weight will be given to performance. Donors supported Management's proposal to give governance a central role in the allocation system by increasing its effective weight in country performance scores to over 50 percent. Donors requested ADB to actively participate in an interagency review of performance-based allocation systems.

D. Weakly-Performing Countries – Staying Engaged

Weakly-performing countries are a development priority. Donors noted that weakly performing countries are usually less able to respond to significant development and poverty reduction challenges. Such situations can deteriorate rapidly, with political, economic, social, and security consequences for both the country concerned and neighboring countries. Typically, the key conditions under which aid conditionality can be effective are likely to be missing. Consistent with the PBA and the low income countries under stress (LICUS) approach of the World Bank, Donors recommended that ADB quickly operationalize a special approach for weakly performing countries. Principles underlining the approach stress the need for continuing engagement; an emphasis on quality rather than quantity of assistance; the need for innovative and highly focused approaches to dialogue, strategies and operations; leveraging demand for positive change and a reliance on deep partnerships with donors, other development agencies and civil society. Engagement will involve a judicious mix of loans, grants and technical assistance resources and will be determined on a case-by-case basis within the framework of country strategies. The nature and success of that engagement would also depend upon the underlying commitment to reform by the country concerned and its willingness to cooperate with the international community. ADB will provide necessary incentives to staff to ensure a strong institutional focus on weakly performing countries.

E. Development Effectiveness through Grants

Grants in ADF IX. Donors agreed to establish a grants program in ADF IX that will: (i) take into account the debt burden of development finance in the poorest countries; (ii) assist poor countries in transition from post-conflict situations to peace and

stability; (iii) combat HIV/AIDS and other infectious diseases; and (iv) support priority technical assistance. In that regard, Donors endorsed an ADF IX grant allocation framework as set out in the main report. Donors acknowledged that grants could represent up to 21% of total ADF IX operations, including an allocation of 3% to ADB's to finance priority technical assistance. The ADF IX grant allocation framework applies to ADF IX only and does not commit future replenishments. In recognition of the importance of greater and improved coherence and harmonization on debt sustainability analysis and its use across the multilateral system, ADB will continue close and systematic cooperation with the World Bank and the IMF on the evolving debt sustainability framework. ADB will follow closely the developments that take place in ongoing negotiations on the IDA14 and African Development Fund (AfDF) 10 replenishments and will assess their relevance to ADF accordingly. To this end, donors will examine the grant allocation framework and its application towards the end of the second year of ADF IX, and will consider proposals for adjustment. ADF IX grant financing, other than for technical assistance, will be determined under the PBA framework. Grant funded operations will be in line with national poverty reduction strategies. The framework in the main report identifies indicative country allocations that should not be considered entitlements. Donors noted the importance of retaining some flexibility within the ADF IX framework on the application of grants in ADF IX through the work of the ADB's Board of Directors. Donors agreed to a compensation framework for the foregone interest of resources used for grants, on the basis of the "Belgium Option". Donors also committed to maintain the financial strength of ADF.

F. ADB's Commitment to Reform – A Stronger Development Partner

Implementing ADB's reform agenda. Donors discussed various aspects of ADB operations and the management of ADF resources. Donors noted the exceptional commitments on reforms made by the President and the steps taken by the Management team to lead and accelerate implementation.

Deliverables Completed

- A new accountability mechanism came into effect in December 2003, providing a strengthened framework for investigating possible violations of ADB's operational policies and procedures.
- An independent Operations Evaluation Department was established on 1 January 2004 and is now fully operational.
- A Results Management Unit (RMU) was created in February 2004.

Deliverables in Process

- Corporate governance will be strengthened through the articulation of a transparent and integrated Management accountability framework that will clearly define the scope of Vice Presidents' responsibilities.
- The review of the Poverty Reduction Strategy is nearing completion and will soon be considered by ADB's Board of Directors.
- The review of the Performance Based Allocation policy is advanced and will be completed in time to determine allocations at the start of ADF IX. This will result in a strengthened performance-allocation link, a central role for governance and increased transparency and disclosure.

- RMU is now developing the processes and procedures for delivering on the corporate-wide results agenda.
- The formulation of the Human Resources Strategy is moving forward and extensive consultations with staff have now been undertaken. This strategy commits to reforming staff incentives to encourage attainment of development outcomes, improving alignment between staff training programs and operations, focusing on performance management and accountability, supporting managing for development results across the organization, and encourage an appropriate gender balance.
- Pilot, results-based Country Strategy and Programs are in process and will be completed by 2004. ADB is making tangible progress towards integrating the MDGs, as well as goals for governance and private sector development in operations. There should be early involvement by the Board of Directors in this process.
- Concerted steps for early implementation are being formulated to reduce the burden posed by year-end bunching of project approvals.
- Management has initiated a systematic process for reviewing efficient and effective resource use within the ADF loan portfolio, including the potential for reprogramming undisbursed loan commitments.
- Results Management Unit is working closely with other international financial institutions on harmonization of results indicators.

Deliverables Planned

- An independent review of the reorganization will commence shortly and is targeted for completion in 2004.
- A unified public communications policy will be submitted to the Board in 2004.
- A review of governance and anticorruption policies will be submitted to the Board in 2004
- A review of the private sector development strategy will be submitted to the Board of Directors in 2004.

Donors agreed that this reform agenda consolidates important issues and provides a sound and timely basis for real progress towards greater organizational effectiveness and achieving development impact in the region.

G. From Commitment to Advocacy and Action – Deepening Accountability

Communicating and advocating ADF IX priorities. In order to translate this ambitious ADF IX agenda into reality, ADB must communicate the associated goals and responsibilities throughout the organization, including Resident Missions. To this end, ADB will implement a strategic communications and advocacy plan. ADB staff will need to be fully informed on Management's commitments to the comprehensive reform agenda, and other understandings and recommendations of ADF Donors. A comprehensive set of workshops and seminars will be held to explain and promote ADF IX priorities, and define unit responsibilities and accountability under the Framework. The communications and advocacy plan will specify the activities required to disseminate fully the reform agenda to all ADB stakeholders, including in developing member countries.

ADF IX Midterm Review. The Midterm Review (MTR), provisionally scheduled for the fourth quarter of 2006, represents a central mechanism for consolidating ADB's accountability to Donors in ADF IX. In order to monitor progress and keep Donors fully informed on a timely basis on all aspects of ADF IX operations, the MTR will draw upon and complement the work of the Operations Evaluation Department and the results-based tools developed by the Results Management Unit. While the precise content of the MTR will be finalized depending upon emerging operational issues and Donor priorities, Donors have requested discussion papers to be prepared for the MTR: (i) report on the financial position of ADF, and the mobilization and use of ADF IX resources, including efforts made to increase mobilization of undisbursed loan commitments; (ii) an assessment of grants in ADF IX, including the grants framework; (iii) report on review of Performance-Based Allocation; (iv) report on Managing for Development Results including harmonization; (v) ADB's experience with weakly-performing developing member countries; (vi) a report on the implementation of the new human resource strategy; and (vii) a report on planning for ADF X. Information papers will be prepared covering: (a) further review of PRS implementation in ADF borrowing countries; (b) selected evaluations of ADF operations; and (c) ADB cooperation with development partners in ADF IX.

H. A Partnership for Financing ADF IX

ADF IX program and financing framework. Donors endorsed an ADF IX program of \$7.0 billion, plus additional amounts for financing foregone interest of grants. The ADF IX program is derived from ADB's strategic operational planning process. The ADF IX program took into account the increased need for concessional assistance in the region for: (i) accelerating progress towards the MDGs in the poorest countries, (ii) meeting the special needs and circumstances of smaller, less developed countries; (iii) assisting countries in their transition from conflict; (iv) assisting countries with significant debt challenges; (v) strengthening regional cooperation and (vi) supporting priority technical assistance across the region. Donors recommended continuation of eligibility as applied to ADF VIII for allocating resources in the planned ADF IX period (2005-2008). This ADF IX program should enable robust implementation of ADB's strengthened Poverty Reduction Strategy. ADB committed to maximize the mobilization of internal resources, while maintaining its financial integrity. Of the total of \$7 billion, at least \$3.7 billion will be provided from internal resources, with the remainder provided by new contributions pledged by donors on a burdenshared basis of \$3.2 billion, plus some additional, voluntary contributions. New contributions pledged by Donors were made mainly on accepted burden sharing principles. Donors agreed to work towards achieving a 50/50 share of regional and non-regional contributions. Contributions to ADF IX included a first-time contribution from the People's Republic of China and renewed support to ADF from Malaysia. Donors' contributions represent a significant effort to assist accelerated poverty reduction in the Asia-Pacific region.