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ABBREVIATIONS

ADB	–	Asian Development Bank
ADF	–	Asian Development Fund
AusAID	–	Australian Aid Agency
CAPE	–	country assistance program evaluation
CGA	–	country governance assessment
CPIA	–	country policy and institutional assessment
CPA	–	country performance assessment
CPS	–	country partnership strategy
CSP	–	country strategy and program
CSPU	–	country strategy and program update
DFID	–	Department for International Development (UK)
DMC	–	developing member country
FSI	–	Failed State Index
GACAP II	–	Second Governance and Anticorruption Action Plan
HLF-2	–	Second High-Level Forum on Aid Effectiveness
IEI	–	Innovation and Efficiency Initiative
Lao PDR	–	Lao People’s Democratic Republic
LICUS	–	low income countries under stress
MDBs	–	multilateral development banks
MDGs	–	Millennium Development Goals
MfDR	–	managing for development results
MOU	–	memorandum of understanding
NGOs	–	non-governmental organizations
OECD-DAC	–	Organisation for Economic Co-operation and Development—Development Assistance Committee
PBA	–	performance-based allocation
PNG	–	Papua New Guinea
RM	–	Resident Mission
UN	–	United Nations
UNDP	–	United Nations Development Programme
USAID	–	United States Agency for International Development
WPC	–	weakly performing country

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EXECUTIVE SUMMARY

This paper examines the Asian Development Bank's (ADB's) experience working in weakly performing countries (WPCs) and presents an approach to engaging them in development that strengthens the effectiveness of existing and future operations. There are major variations among ADB's developing member countries (DMCs) that can be classified as weakly performing. Thus, the approach provides a framework for guiding operational planning and implementation that includes a methodology for classifying WPCs and alternative interventions that may be modified based on country context.

ADB has considerable experience with countries with small, isolated, and vulnerable economies and with much larger countries that are making the transition from centrally-planned to market economies or that are emerging from conflict.¹ That experience and the Organisation for Economic Co-operation and Development's Development Assistance Committee's (OECD-DAC's) Twelve Principles for Good Engagement with Fragile States have provided useful guidance for formulating the approach. ADB's approach also draws on the work of OECD-DAC and the World Bank in classifying countries into four models for engagement: (i) countries in prolonged political crisis; (ii) countries in post-conflict or political transition; (iii) countries facing deteriorating governance or rising conflict risk; and (iv) countries going through a gradual reform process. The appropriate responses for each model vary in terms of programming issues, emphasis of program, capacity and accountability, and other aspects of engagement.

ADB links Asian Development Fund financial assistance to performance of eligible DMCs through the Performance-Based Allocation (PBA) Policy. Country performance assessments (CPAs) undertaken under the policy provide useful data for country programming, policy dialogue, and the design of program lending, as well as tracking annual trends and facilitating early identification of deteriorating performance. CPAs and consideration of conflict and post-conflict vulnerability provide the starting point for assessing performance. Specifically, it is proposed that "weak performers" are DMCs that are either (a) ranked in the fourth and fifth quintiles on CPA assessments for 2 of the most recent 3 years or (b) are considered to be in conflict or post-conflict. This classification would be done on a rolling basis and would not be publicly disclosed. The intention is not to impair in any way a country's position as a member of ADB; rather, it is intended to draw attention to the challenges the country faces and to improve the effectiveness of ADB assistance. The approach recognizes that weak performance does not disappear when a country shows a small improvement in performance scores that might move it above a cut-off point. Regional departments operating in countries that might not be classified as WPCs but that exhibit evidence of weak performance are encouraged to adapt elements of the approach in their operations.

Effective assistance programs in WPCs must have country ownership; capacity development will be required to strengthen ownership and the ability to absorb and manage assistance. ADB will respond to this need by scaling up technical assistance and other grant financing from partners. ADB operations in WPCs will involve partnerships at all stages, including pursuing cofinancing opportunities. ADB will continue to (i) refine its approach to identifying and defining weak performance, (ii) re-think its operational planning, and (iii) adapt its business processes and instruments to ensure that its engagement is suitable and effective for individual WPCs and is consistent with the Paris Declaration.

¹ Examples include, but are not limited to, Afghanistan, Cambodia, Nepal, Solomon Islands, Tajikistan, and Timor-Leste.

I. INTRODUCTION

1. This paper examines the Asian Development Bank's (ADB's) experience working in weakly performing countries (WPCs) and presents an approach for engaging them in development programs that seeks to strengthen the effectiveness of existing and future operations. While the Asian Development Fund (ADF) IX Donors' Report calls for a, "...specific and strategic approach," there are major variations among ADB's developing member countries (DMCs) that can be classified as weakly performing; no single or standardized approach applies uniformly across WPCs in Asia and the Pacific. The approach provides a framework for guiding planning and implementation including a methodology for classifying WPCs and interventions that may be modified based on the country's situation. Applying the approach will depend on country-specific circumstances and the decisions of experienced ADB staff and partners working in WPCs.

2. *Context:* Many of the region's poor people live in DMCs that have weak governance, ineffective public administration and rule of law, and civil unrest. These countries have been referred to variously as WPCs, fragile states, low-income countries under stress (LICUS), and difficult partnership countries.² Service delivery systems in such countries seldom function well, and the government's ability to guarantee the basic security of its people is often limited. WPCs are more likely to experience large-scale and violent civil conflict than other low-income countries.³ The costs of weak performance include its impact on citizens, costs to neighboring countries, and global costs. One study estimated those costs at United States dollars (\$)100 billion which is about twice the annual total of development assistance worldwide.⁴ In such settings, achieving the Millennium Development Goals (MDGs) represents a major challenge.

3. *Need to engage with WPCs:* WPCs deserve attention because normal operations may no longer be effective when country performance deteriorates; ADB may need to re-examine local conditions to find ways to work effectively. Given the complexity of the operating environment in most WPCs, priority must be given to partnerships and to developing joint approaches and solutions. In extreme cases, ADB may suspend operations while continuing to monitor the situation and to identify entry points for re-engagement. Failure to engage is likely to entail major human, social, economic, and security costs.

4. *Structure of the paper:* Chapter II discusses various definitions of weak performance including the relationship between weak performance and fragility, ways to differentiate WPCs, and the factors underlying weak performance. Chapter III discusses aspects of ADB's institutional frameworks, policies and experience that were used to develop the approach. Chapter IV presents the proposed approach including possible parameters for ADB engagement in (i) strategic and operational planning, (ii) business processes, (iii) modalities and instruments of assistance, and (iv) institutional management and support. Chapter V discusses the resource implications of the approach and Chapter VI concludes with a request for donor guidance.

² Consistent with precedents set during the ADF IX negotiations, ADB will continue to use the term weakly performing countries (WPCs). While WPCs may exhibit aspects of fragility, the primary focus on weak performance is consistent with the performance-based allocation (PBA) systems of the Asian Development Bank, African Development Bank, and the LICUS approach of the World Bank.

³ *World Bank Group Work in Low-Income Countries in Stress: A Task Force Report*; report of a Task Force chaired by Dr. Ngozi Okonjo-Iweala, then a Vice President at the World Bank; page 12, September 2002.

⁴ Lisa Chauvet & Paul Collier: *Development Effectiveness in Fragile States: Spillovers and Turnarounds*; Centre for the Study of African Economies, Department of Economics, Oxford University; December 1, 2004.

II. IDENTIFYING AND DEFINING WEAK PERFORMANCE AND FRAGILITY

A. Definitions of Weak Performance and Fragility

5. *Definitions of poor performance:* The LICUS initiative classifies countries based on quantitative measures of performance. The World Bank refers to LICUS as “fragile states characterized by a debilitating combination of weak governance, policies and institutions, indicated by ranking among the lowest on the Country Policy and Institutional Assessment (CPIA).” Performance is measured on a continuum ranging from “strong” (DMCs that make effective use of development assistance) to “weak” (DMCs that are unable to do so). Strong performers can absorb higher levels of aid and are likely to be more effective in converting aid into economic growth and poverty reduction. In contrast, weak performers are less likely to be able to use aid effectively. Weakly performing governments often cannot deliver a minimal set of public sector functions to their citizens, i.e., safety and security, protection of established rights, control of borders, effective management of public resources, and basic human services.⁵ Weak performance provides fertile ground for stagnation, for sharp economic and social reversals, and for political insecurity.

6. *Definitions of weak, failing, or failed states:* The United States Agency for International Development (USAID) uses the term “fragile states” to refer to a broad range of failed, failing, and recovering states. USAID’s Fragile States Strategy, which emphasizes security, political, economic, and social factors, has four interrelated priorities: (i) enhanced stability; (ii) improved security; (iii) institutional and policy reform; and (iv) developing institutional capacities.⁶ USAID differentiates between states that are vulnerable (“unable or unwilling to adequately assure the provision of security and basic services to significant portions of their populations and where the legitimacy of the government is in question”) and those in a state of crisis (“the central government does not exert effective control over its own territory or is unable or unwilling to assure the provision of vital services to significant parts of its territory, where legitimacy of the government is weak or nonexistent, and where violent conflict is a reality or a great risk”). From this perspective, the government’s inability to provide basic services contributes to economic instability, food insecurity, social chaos, and armed conflict, all of which can create fertile ground for terrorism. Similar conceptualizations are provided by the Center for Global Development⁷ and the United Nations (UN).⁸ The UN defines “threats” broadly to include “economic and social threats, including poverty, infectious disease and environmental degradation; internal conflict, including civil war, genocide and other large-scale atrocities; nuclear, radiological, chemical, and biological weapons proliferation; terrorism; and transnational organized crime.”⁹

7. *Definitions that emphasize political economy and the importance of partnerships:* This approach emphasizes the difficulties of working with WPCs in which the so-called “Monterrey case” (i.e., a government with strong capacity and reasonable political will) does not exist.¹⁰ The United Kingdom’s Department for International Development (DFID) emphasizes a “drivers of change” model that relies on analyzing and understanding a country’s history, culture, and

⁵ DFID 2005. *Why We Need to Work More Effectively in Fragile States*.

⁶ US Agency for International Development, January 2005. *Fragile States Strategy*.

⁷ Commission on Weak States and US National Security, 2004. *On the Brink: Weak States and US National Security*, Washington: Center for Global Development.

⁸ United Nations 2004. *A more secure world: Our shared responsibility*. Report of the High-level Panel on Threats, Challenges, and Change.

⁹ United Nations *High Level Panel on Threats, Challenges, and Change*.

¹⁰ DFID, Poverty Reduction in Difficult Environments Team 2004. *Fragile States: Defining Difficult Environments for Poverty Reduction*.

people¹¹ to develop interventions with reference to political incentives and the institutions through which reform must occur. The Australian Aid Agency AusAID defines fragile states (which it previously referred to as poor performers¹²) as, "...countries that face particularly stark poverty and development challenges and are vulnerable to further decline—or even state failure. Weak governance, failed institutions, instability or conflict result in dismal growth prospects. The state fails to deliver critical services to the broader population, with a particular impact on the poor."¹³ AusAID emphasizes the importance of conflict prevention, the key role of service delivery, and a "whole of government" approach that takes into account the development, security, and political aspects of state fragility. The focus of Australia's aid to fragile states is on good governance to help ensure the political stability and security required for economic growth and poverty reduction.¹⁴ The Organisation for Economic Co-operation and Development's Development Assistance Committee (OECD-DAC) distinguishes "difficult partnerships" from cases where the partner government is making a best effort yet in which "performance, in the sense of outcomes, is weak."¹⁵ The "difficulties" involved often revolve around a DMC's lack of focus on poverty reduction, weak institutions, and/or lack of financial or human capacity to implement and manage development projects. OECD-DAC defines fragile states as, "...countries where there is a lack of political commitment and insufficient capacity to develop and implement pro-poor policies."¹⁶

B. Classification Schemes

8. Three classifications are shown in Table 1: (i) the World Bank's LICUS classification; (ii) an elaboration of LICUS data by DFID; and (iii) the Failed State Index (FSI) which was developed jointly by the Fund for Peace (a Washington DC-based think tank) and *Foreign Policy* magazine. Results show that of 14 lower-income countries currently classified as LICUS, four are in the Asia-Pacific region (Afghanistan, Myanmar, Solomon Islands, and Uzbekistan). The second column shows the results of a DFID analysis of LICUS data for 1999–2003 presented as an appendix in DFID's approach to fragile states.¹⁷ DFID analyzed World Bank CPIA ratings and identified all countries that appeared at least once in the fourth and fifth quintiles between 1999 and 2003 to define a "proxy list of fragile states." Of 46 countries so identified, 15 are in the Asia-Pacific region. The third column shows FSI classifications based on 12 indicators measuring social, political, and economic variables reflecting state failure or near failure. In all, 148 countries were ranked, and the 60 most vulnerable were classified into three at-risk categories: 15 of them are in the Asia-Pacific region. Five countries in the region were classified as "critical" (Afghanistan, Bangladesh, Myanmar, Nepal, and Pakistan), six as "in danger" (Bhutan, Indonesia, Krygyz Republic, Lao People's Democratic Republic [LaoPDR], Sri Lanka, and Uzbekistan), and four as "borderline" (Cambodia, Papua New Guinea [PNG], Tajikstan, and Turkmenistan). Comparison of these three classification schemes shows that three countries were identified as fragile on all three indices (Afghanistan, Myanmar, and Uzbekistan), and seven were identified on two of the three (Cambodia, Indonesia, Lao PDR, Nepal, PNG,

¹¹ DFID 2005. *Why We Need to Work More Effectively in Fragile States*.

¹² AusAID. *Australian Aid: Investing in Growth, Stability, and Prosperity*. (September 2002)

¹³ AusAID. *Australian Aid: An Integrated Approach*, p. 11.

¹⁴ Australia's significant financial commitments, in the context of its whole-of government approach, are reflected in the Australian-led Regional Assistance Mission to Solomon Islands and the Enhanced Cooperation Program in Papua New Guinea.

¹⁵ OECD-DAC, 2001. *Poor Performers: Basic Approaches for Supporting Development in Difficult Partnerships* [DCD/DAC(2001)26/REV1]. See <http://www.oecd.org/dataoecd/26/56/21684456.pdf>

¹⁶ Karim Morcos, *Chair's Summary*. Senior Level Forum on Development Effectiveness in Fragile States. London (January 2005).

¹⁷ DFID 2005. *Why We Need to Work More Effectively in Fragile States*.

Solomon Islands, and Tajikistan). The remaining 10 countries in the table were identified on only one index (Azerbaijan, Bangladesh, Bhutan, Kiribati, Krygyz Republic, Pakistan, Sri Lanka, Timor-Leste, Tonga, Turkmenistan, and Vanuatu).

Table 1: Comparison of Three Classification Schemes

Country	LICUS	DFID-LICUS	Failed States Index
Afghanistan	X	X	X
Azerbaijan		X	
Bangladesh			X
Bhutan			X
Burma/Myanmar	X	X	X
Cambodia		X	X
Indonesia		X	X
Kiribati		X	
Krygyz Republic			X
Lao PDR		X	X
Nepal		X	X
Papua New Guinea		X	X
Pakistan			X
Solomon Islands	X	X	
Sri Lanka			X
Tajikistan		X	X
Timor-Leste		X	
Tonga		X	
Turkmenistan			X
Uzbekistan	X	X	X
Vanuatu		X	

C. Factors Underlying Weak Performance

9. ADB's operational experience in WPCs and a review of relevant literature suggest that five factors often underlie weak performance.¹⁸

- (i) *Weak policy, policy implementation, and management capacity:* Many WPCs lack the ability to formulate, implement, and evaluate a consistent set of sound policies. Important public sector institutions in such countries often lack the capacity to enforce the rule of law or to provide an enabling environment for private sector development. In many cases, the situation is exacerbated by poor governance (i.e., corruption in the public sector and/or government that represents one or more narrow interest groups rather than the population as a whole).
- (ii) *Small, isolated market conditions:* Some WPCs are small island economies or landlocked nations with poor transport links to larger markets. While small size in and of itself is not necessarily an obstacle to strong performance, small countries that have developed quickly tend to have natural transportation links to larger markets. However, isolated nations with small markets are frequently unable to

¹⁸ ADB 2004. *ADB's Approach to Weakly-Performing Developing Member Countries*. Information paper for ADF IX Negotiations, Seoul, May 2004.

exploit economies of scale and comparative advantages. While they tend to rely on commodity exports, their competitiveness is jeopardized by inefficient scales of production and high transport costs. Development practitioners need to develop a deeper understanding of the way small states and societies operate, cooperate, and compete to better understand their political economies. This understanding should be derived from the country itself and not from a project.

- (iii) *Physical and social disruption linked to violent conflict:* Countries in conflict or post-conflict often have sharp social divisions and weakened infrastructure. Post-conflict countries typically have (i) suffered massive destruction of livelihoods and social capital; (ii) severe disruptions in basic social services; (iii) weakened or even absent government institutional capacity and state authority; (iv) and have experienced the disintegration of mutual confidence and trust among diverse population groups (e.g., ethnic, religious, political).
- (iv) *Meager public sector resources:* Weak performance is also associated with the limited resources typically available to governments of WPCs. The gap in public sector expenditure between a developed country and a low-income WPC is considerable. Average per capita public sector spending often exceeds \$10,000 per annum in OECD countries compared with \$100–200 in many developing countries.
- (v) *Volatility and unpredictability of aid:* Aid to WPCs is more volatile and unpredictable than to other low-income countries. As a group, WPCs received less aid per capita than would be predicted based on their populations, poverty levels, and performance during 1992–2002.¹⁹ There is also evidence that WPCs receive insufficient aid even after controlling for their capacity to absorb it.²⁰ At the extreme, WPCs may become “aid orphans” receiving less aid per capita than other countries at similar levels of development. These countries often get little media or diplomatic attention and are at high risk of becoming unstable.

These factors are not mutually exclusive; in some DMCs more than one of these conditions is present.

¹⁹ Levin, Victoria and David Dollar 2005. *The Forgotten States: Aid Volumes and Volatility in Difficult Partnership Countries (1992–2002)*. Summary paper prepared for DAC Learning and Advisory Process on Difficult Partnerships. World Bank.

²⁰ McGillivray, Mark. *Aid Allocation and Fragile States*. Background paper for the Senior Level Forum on Aid Effectiveness in Fragile States. London (January 2005).

III. THE ASIAN DEVELOPMENT BANK'S INSTITUTIONAL FRAMEWORK AND RELEVANT COUNTRY EXPERIENCE

A. Policies and Engaging the International Community

10. *ADB's performance-based allocation system:* ADB links ADF financial assistance for eligible WPCs to performance through the Performance-Based Allocation (PBA) Policy²¹ that is also based on country needs. The revised PBA policy harmonized methods for assessing country performance with those of the World Bank and introduced public disclosure of the ratings. In addition to determining allocations, PBA assessments provide useful data for country programming, policy dialogue, and the design of program lending, and they track annual trends, facilitating early identification of deteriorating performance. The PBA system is intended to provide incentives for ADF-borrowing DMCs to improve country performance in key areas, especially governance.

11. *Institutional commitment to good governance:* ADB collaborates with development partners to support WPCs in building and sustaining effective institutions and capacity, in eliminating corruption, and in providing adequate public services. Since 2001, ADB has used country governance assessments (CGAs) to identify measures for inclusion in country strategies and programs (CSPs) and to provide objective data for developing and implementing program approaches and road maps. Their effectiveness has, however, been mixed.²² While CGAs have raised the awareness of institutional issues in DMCs and improved the understanding of the machinery of government among ADB staff and DMC stakeholders, a 2003 review of CGAs found that their impact on CSPs and on ADB operations in general has been limited. Furthermore, CGAs have had only a limited impact on long-term governance and institutional development programs and strategies. These weaknesses were recognized in the recent *Review of the Implementation of ADB's Governance and Anti-corruption Policies*. In order to address them and implement more effective approaches, the Second Governance and Anticorruption Action Plan (GACAP II) was developed.²³

12. *Anticorruption Initiatives:* Corruption is a particular risk in WPCs. ADB's anticorruption policy requires that all ADB-financed activities adhere to the highest financial and ethical standards and includes an investigative function within the Office of the Auditor General. To strengthen the supervision and management of its project audits and anticorruption awareness activities, ADB upgraded the Anticorruption Unit to the Integrity Division in early 2005. ADB participates actively in the multilateral development bank (MDB) Working Group on Anti-Corruption, Governance and Capacity Building. Designing anticorruption projects in WPCs requires paying special attention to corruption risks with appropriate mitigation incorporated in project designs. While an increasing proportion of CSPs now discuss corruption openly, which represents significant progress, there is considerable variation in the way issues are presented. Under GACAP II ADB is continuing to build internal capacity for assessing corruption risks and to strengthen its systems to minimize those risks.

13. *ADF IX grant program:* Grant financing was introduced in ADF IX. Very poor, debt-vulnerable or post-conflict countries may not be able to afford loans even on highly concessional terms. Recognizing this, grants represent up to 21% of total ADF IX operations to (i) help reduce the debt burden of the poorest countries of the region; (ii) assist poor and weakly performing

²¹ ADB 2004. *Policy on Performance-Based Allocation of ADF Resources*.

²² ADB 2005. *Review of the Implementation of the Governance and Anti-Corruption Policies*. Manila.

²³ ADB 2006. *Second Governance and Anticorruption Action Plan (GACAP II)*. Manila.

countries in accelerating their transition from post-conflict to peace and stability; (iii) combat HIV/AIDS and other infectious diseases; and (iv) undertake priority technical assistance. The ADF IX Grant Allocation Framework identified nine countries eligible for program grants.²⁴

14. *Disaster and Emergency Assistance Policy:* The major disasters of the last 2 years (the tsunami and the South Asian earthquake) have raised awareness among development institutions of the importance of managing disaster risks. Dealing with disasters involves both development activities (disaster preparedness, risk mitigation, post-disaster reconstruction) and humanitarian activities often in settings in which weak performance is a key issue. In 2004, ADB's Board approved a comprehensive disaster and emergency assistance policy for rehabilitation and reconstruction assistance after natural and non-natural disasters, including conflicts, and for assisting DMCs with preventing, preparing for, and mitigating the impact of future disasters.²⁵ The policy emphasizes the crucial importance of working in close collaboration with development partners; particularly important are developing risk and vulnerability assessments, monitoring social and economic trends, and prioritizing damage and needs assessments after emergencies occur. ADB coordinates its activities closely with development partners, has engaged in informal consultations with the other MDBs, and participated in the 2006 ProVention Consortium Forum.²⁶

15. *ADB's involvement in the global dialogue:* Since the completion of ADF IX negotiations in mid-2004, the international community has pursued a range of initiatives to achieve greater policy coherence and development effectiveness in fragile states. That work has provided ADB with a valuable basis for developing a framework for differentiating WPCs based on country context. In late 2004, ADB cosponsored two regional workshops on harmonization, alignment, and managing for development results (MfDR) for which case studies of Afghanistan and Sri Lanka were prepared that identified effective approaches and tools for working in post-conflict countries. In January 2005, ADB senior staff attended the Senior Level Forum on Development Effectiveness in Fragile States. ADB also participated in a seminar hosted by the Center for Global Development (May 2005) during which the Director of USAID's Office of Conflict Management and Mitigation presented that institution's efforts to mainstream conflict prevention into its activities and country programs. As part of a "core group of donors," ADB has been actively involved in piloting OECD-DAC's Principles of Good Engagement in Nepal (an effort spearheaded by DFID).²⁷ In 2006, ADB participated via video link in meetings of OECD-DAC's Fragile States Group.

16. *ADB and the Paris Declaration:* In March 2005 at the Second High-Level Forum on Aid Effectiveness (HLF-2), ADB's President delivered the speech, "Aid Effectiveness in Complex Situations: Fragile States and Emergency Responses." The President stressed the importance of country ownership while noting that a long process of consensus building is generally required to engage governments, the private sector, civil society, and other partners. During HLF-2, ADB also endorsed (along with over 100 ministers, heads of agencies, and other senior officials) the Paris Declaration which included commitments to increase efforts in building

²⁴ The nine countries eligible for ADF IX grant financing on a program basis are Afghanistan, Cambodia, Krygyz Republic, Lao PDR, Nepal, Solomon Islands, Sri Lanka, Tajikistan, and Timor-Leste. Note that most of these DMCs have exhibited evidence of weak performance over the last few years.

²⁵ ADB 2004. *Disaster and Emergency Assistance Policy*. Manila

²⁶ ProVention is an international consortium that works in partnership to, "...build safer communities and reduce the impacts of disasters in developing countries."

²⁷ ADB's Nepal Resident Mission serves as a key liaison between donors and the government. However, the recent change in government has slowed progress, and to date implementation and actual piloting remain in the planning stage.

country ownership, harmonization, alignment, and MfDR. ADB has since been actively involved in implementing and monitoring the Paris Declaration in MDB working groups including monitoring MDB progress on implementing MfDR under the common performance assessment system (COMPAS). This active and ongoing engagement will play a key role in implementing ADB's approach to engaging WPCs in development.

B. Operations in Difficult Environments

17. ADB has considerable experience with operations in small, isolated, and vulnerable economies and in much larger countries that are making the transition from a closed economy to market-led development or that are emerging from conflict. That experience and OECD-DAC's initial Twelve Principles for Good Engagement with Fragile States have provided useful guidance for formulating a more systematic and concerted approach to assisting WPCs. The following country thumbnail sketches describe the key aspects of ADB operations in WPCs. ADB's assistance has included close collaboration with the governments and with development partners in conducting joint assessments, developing trust funds, rehabilitating infrastructure, supporting sound public administration, and building capacity.

18. *Afghanistan:* By the time the Taliban were forcibly removed in 2001, long-term hostilities had done extensive damage to Afghanistan's social and economic structures and institutions. Physical infrastructure and social services had largely collapsed, and Afghanistan had some of the worst social and human indicators in the world. In November 2001, ADB, the United Nations Development Programme (UNDP), and the World Bank carried out a preliminary needs assessment that provided the basis for \$4.5 billion in donor assistance mobilized around agreed sector priorities and policy and institutional frameworks. ADB has since supported the Government-led Consultative Group Structure and has worked closely with the government to develop a country-owned and country-driven approach to post-conflict assistance (see Box 1). Donors have engaged in a series of joint portfolio reviews. Building on the findings of comprehensive needs assessments, sector-specific coordination among partners has improved significantly. Recognizing that achieving benefits from regional cooperation would require the rehabilitation of Afghanistan's badly damaged roads, in 2005 ADB approved a \$55 million ADF grant to rehabilitate one of the last major unpaved stretches of the "ring road" that circles the country and links Afghanistan to its neighbors. ADB is also supporting the development of a road development master plan through a \$2 million technical assistance grant.

Box 1: The Afghanistan Reconstruction Trust Fund

The Afghanistan Reconstruction Trust Fund (ARTF), a coordinated financing mechanism, is jointly managed by the Asian Development Bank, Islamic Development Bank, the United Nations Development Programme (UNDP), and the World Bank (which is administrator). Twenty-four donors have contributed to the ARTF. The ARTF (i) promotes transparency and accountability of reconstruction assistance; (ii) reinforces the national budget as the vehicle to align the reconstruction program with national objectives; (iii) reduces the burden on limited government capacity while building capacity over time; and (iv) helps fund recurrent budgetary expenditures required for the government to function effectively. The ARTF helps fund vocational training, strengthen fiduciary capacity, increase financial stability, and it makes government service a viable alternative for qualified Afghans. Among other things, the ARTF funds priority projects and programs to rebuild Afghanistan, facilitates the return of skilled expatriate Afghans to the country, and provides short-term emergency funding for salaries of civil servants. For example, between March 2003 and April 2004, funds for the education of 220,000 doctors, nurses, teachers, and water specialists have been channeled through ARTF, as have funds for hospital supplies, textbooks, fuel, and telecom equipment.

19. *Cambodia*: After more than two decades of international isolation and conflict ended in 1991, Cambodia was faced with depleted physical, social, and human capital; the country essentially had to start from scratch in rebuilding its infrastructure and institutions. ADB's initial assistance focused on meeting the country's urgent needs for the immediate rehabilitation of key infrastructure components. ADB responded quickly with the Special Rehabilitation Assistance Project, the first international donor assistance after the signing of the Paris Accord in October 1991.²⁸ The project, prepared as an emergency loan, assisted the government in restoring and repairing essential physical and social infrastructure in four sectors: transport, power, agriculture, and education. From 1992 to 2002, ADB's country assistance programs included 26 public sector loans totaling approximately \$675 million in ADF resources and averaging about \$61 million annually.²⁹ The nonlending program included 29 project preparatory technical assistance activities (about \$15 million) and 68 advisory and operational technical assistance projects (about \$52 million). Many projects featured pro-poor designs that contributed to poverty reduction. For example, the country assistance program evaluation (CAPE) reported a 40% increase in primary school enrollment in the poorest 300 communes and a 30% increase in household incomes among the rural poor attributable to better access to rural roads. Although important economic and social gains have been made over the past decade, urban-rural inequality is increasing and rural areas continue to suffer from economic stagnation and inflation. In the Greater Mekong Subregion, cooperation has had a moderating effect on potential spillovers. ADB's experience in post-conflict Cambodia suggests that larger investments could have been focused on institutional capacity building during the early stages of reconstruction. Furthermore, the effectiveness of aid coordination was rated only "partly satisfactory" due to (i) lack of an agreed development agenda among funding agencies and (ii) the complicated government structure of aid coordination. In this regard, the CAPE concluded that, "Funding agencies should coordinate more closely and encourage government leadership in developing a country-led, comprehensive development framework. This framework should be results-based, driven by intermediate target indicators in the sectors under agreed priority areas, linked to the overriding poverty reduction objective and other MDGs. With this framework, assistance can be divided among funding agencies to reach intermediate sector targets in a coherent manner."

20. *Nepal*: Since democracy was restored in 1991, Nepal has experienced major internal conflict and regime change. An estimated 12,000 people have been killed and some 300–400,000 rural families have been displaced. The costs to the government, estimated at \$400 million, include damage to infrastructure, lost business opportunities, declining tourism, the withdrawal of financial institutions, and the closure of private schools.³⁰ In these difficult circumstances, ADB has remained actively engaged. According to the 2004 CAPE, ADB approved 48 loans from 1998 to 2003 to help finance 47 projects/programs.³¹ An analysis of 37 projects showed that most were selected and designed within the priorities of the operational strategies covering that period; they generally addressed key crosscutting issues, had a positive development impact, and were relatively successfully implemented. Although the CAPE recognized that institutional and governance issues often delayed or impeded implementation, most projects were nonetheless successful, and some were outstanding. The overall effect of

²⁸ Loan 1199-CAM[SF]. Total project cost was \$80.8 million, financed by a loan of from ADB's Special Funds, two technical assistance grants to finance project implementation consultants (including cofinancing from the Swedish International Development Cooperation Agency (\$3.2 million). The project was implemented from 1993 to 1997, delayed by one year.

²⁹ ADB 2004. *Country Assistance Program Evaluation for Cambodia*. January 2004.

³⁰ Ra, S. and B. Singh 2005. Nepal Resident Mission Working Paper Series No. 2. *Measuring the Economic Costs of the Conflict*.

³¹ ADB. 2004. *Country Assistance Program Evaluation for Nepal*. September 2004.

ADB's lending program was positive in terms of social, environmental, economic, and direct poverty impact. During the development of Nepal's results-based CSP for 2005–2009, inclusive social development was identified as a strategic pillar for ADB's operations in Nepal with an emphasis on assisting poor women, disadvantaged ethnic and caste groups, and the rural poor. ADB has assisted the Government of Nepal in developing its medium-term expenditure framework that has helped (i) increase allocations for priority projects; (ii) protect key projects and programs from shortfalls in resources; (iii) maintain fiscal discipline; and (iv) link annual budget activities with the national development plan. Given that poverty in Nepal remains concentrated among the rural poor, women, and disadvantaged ethnic and caste groups, ADB's assistance has included a \$10 million loan for a gender equality and empowerment project that facilitates economic, social, legal, and political empowerment among poor women and a \$685,000 technical assistance grant (2006) aimed at improving the socioeconomic status of disadvantaged groups and the removal of sociocultural and financial constraints that keep poor women from participating in rural development projects.³² Other ADB assistance focuses on rural poverty (the Regional Development Strategy [2005] and Enhancing the Poverty Impacts on Roads Project [2006]). ADB is refining its assistance program following regime change in April 2006.

**Box 2: Responding to the Priorities of the Poor:
A Pacific Strategy for the Asian Development Bank 2005–2009**

The Asian Development Bank's (ADB's) Pacific Strategy 2005–2009 identifies policy and institutional constraints that exist in many Pacific developing member countries (PDMCs) and takes into account limited country capacities, weak policy formulation and implementation, and inadequate rule of law. The strategy, which provides overall guidance for ADB operations in 14 PDMCs and supports Pacific regional cooperation, emphasizes the key role of collaboration and coordination among development partners. ADB's analytical work in preparation for the strategy included (i) participatory poverty assessments, (ii) studies of governance and private sector development, and (iii) thematic studies on the environment and gender. Formulation of the strategy involved a 3-month consultation phase with PDMC governments, private sector groups, civil society organizations, Pacific regional organizations, and other development partners. ADB's web site was used to solicit direct feedback from the interested public. The strategy differentiates the quite diverse economies. In better performing PDMCs, the focus is on supporting policy and institutional enhancements and infrastructure investments that accelerate current economic growth rates and raise the quality of services. In more poorly performing PDMCs, a key emphasis is on addressing the declining quality of governance and institutions and the associated loss of capacity. In the Solomon Islands, for example, a long-term focus on rebuilding basic institutions is appropriate, while in Timor-Leste strengthening new institutions is a key goal.

21. *Solomon Islands*: Significant, organized violence during the period 1998–2002 reflected the country's colonial history, weak institutions, ethnic rivalries, and conflict over land.³³ Escalating violence exacerbated by a large decrease in gross domestic product, endemic corruption, and a government default on loan interest led to near state-failure by 2003.³⁴ The country continues to lack adequate social infrastructure and services, especially in rural areas, and poor people have extremely limited access to income-generating opportunities. There is little formal employment outside Honiara, a situation exacerbated by a high population growth rate and increasing incidence of HIV/AIDS. The security and stability situation has improved

³² This grant was provided by the Poverty Reduction Cooperation Fund, financed by the Government of the United Kingdom.

³³ Lowy Institute for International Policy. *The Testament of Solomons: RAMSI and International State-Building*.

³⁴ Due to debt-servicing arrears, ADB suspended operations between February 2002 and September 2003.

since the establishment of the Australian-led Regional Assistance Mission to Solomon Islands.³⁵ Since re-establishing operations, ADB has reactivated the Post-Conflict Emergency Rehabilitation Project³⁶ to rehabilitate vital roads, bridges, local administrative centers, and water supplies (providing a highly visible “peace dividend”).³⁷ An \$800,000 technical assistance project has assisted the government in improving state-owned enterprise arrangements, accountability, and performance.³⁸ Solomon Islands is eligible for the ADF IX grant program; of the country’s 2005–2006 ADF allocation of \$720,000, up to \$378,000 can be provided as a grant. The grant portion is being used to develop transportation infrastructure and services, consistent with the government’s high priority on revitalizing the rural economy. ADB and its development partners continue to address major challenges such as (i) shifting the focus of assistance from short-term stabilization to implementing medium- and longer-term measures; (ii) building credible, capable public institutions (see Box 2); (iii) creating and sustaining a sound enabling environment in which private business can develop; and (iv) addressing root causes of conflict.

22. *Tajikistan:* Shortly after independence in 1991, Tajikistan descended into a civil war (1992–1997) that caused widespread physical damage (estimated \$7 billion) and the loss of as many as 50,000 lives. Despite the economic and social damage resulting from the breakup of the Soviet Union and the civil war, Tajikistan began to recover in 1998 after a peace agreement was reached. ADB’s assistance strategy in Tajikistan has emphasized rehabilitating basic infrastructure and strengthening rural development and regional cooperation³⁹ and addresses core governance issues, particularly as related to the government’s social sector program. ADB has also played a role in agriculture sector reforms with DFID providing cofinancing to assist the government in implementing its farm debt resolution strategy. In 2005, ADB provided a package of assistance comprising the Farm Productivity Improvement Project and Farm Analysis and Awareness Raising for Debt Resolution. In 2006, a new project has been proposed on a standby basis to support the implementation of the new tax and customs code that became effective in 2005.

23. *Timor-Leste:* When citizens voted overwhelmingly for independence in 1999, an estimated 70% of the country’s physical infrastructure had been largely destroyed and nearly 80% of the population had been displaced. A joint poverty assessment undertaken by the government, ADB, Japan International Cooperation Agency, UNDP, and the World Bank provided the basis for preparing the country’s first national development plan in May 2002. That plan included a national poverty reduction strategy focused on (i) promoting opportunities for the poor; (ii) improving access to basic social services; (iii) enhancing security including reducing vulnerability to shocks and improving food security; and (iv) empowering the poor. In September 2005, ADB approved the first ADF IX grant to Timor-Leste (\$10 million for the Road Sector Investment Project). The project will rehabilitate about 123 kilometers of important roads in isolated rural areas with insecure food supplies. The project has a gender component to ensure

³⁵ at the invitation of the Government of the Solomon Islands and under the auspices of the Pacific Islands Forum. Consistent with the Whole of Government approach, AusAID works closely with the Departments of Foreign Affairs and Trade, Finance, Treasury, and Defense.

³⁶ ADB 2000. *Report and Recommendation of the President to the Board of Directors on a Proposed Loan to Solomon Islands for the Post-Conflict Emergency Rehabilitation Project*. Manila. (Loan No. 1823, approved in December 2000 for \$10 million).

³⁷ Australia and New Zealand have committed funds for an extension of the project and are working with ADB to prepare a long-term road rehabilitation program.

³⁸ ADB 2004. *Technical Assistance for State-Owned Enterprise Reforms and Private Sector Participation*. Manila. (TA No. 4482-SOL, approved in December 2004 for \$800,000).

³⁹ ADB has collaborated with the World Bank in joint portfolio performance reviews.

women's involvement in project activities including rehabilitation and maintenance of selected roads, community empowerment initiatives, and combating HIV/AIDS.

C. Strategic Operational Planning

24. *The country strategy and program and the (new) country partnership strategy:* ADB's Long-Term Strategic Framework⁴⁰ and the new business processes⁴¹ place the CSP and CSP update (CSPU) at the core of ADB operations. CSPs/CSPUs have played a key role in channeling resources to sectors that support poverty reduction, especially through governance interventions. ADB has recently replaced the CSP with the country partnership strategy (CPS) and a 3-year rolling operational business plan.⁴² All new CSPs are results-oriented, including feeding the findings of joint needs assessments and policy dialogue with stakeholders into their development.⁴³ ADB seeks to minimize the reporting burden on governments by harmonizing indicators and reporting formats with its development partners. ADB works closely with governments and partners to formulate performance frameworks that emphasize rewards for good outcomes rather than punishments for poor ones.

25. *Analysis of CSPs in DMCs exhibiting evidence of weak performance:* In order to assess the extent to which recent CSPs have dealt directly with weak performance and fragility, CSPs/CSPUs for eight WPCs (Afghanistan, Cambodia, Lao PDR, Nepal, PNG, Solomon Islands, Tajikistan, and Uzbekistan) were examined (see Table 2). Results show that in general, performance and fragility have not featured prominently in CSP formulation which may reflect the fact that these issues were not as widely discussed when the CSPs/CSPUs were developed as they are now. For example, among the eight, there is only one reference to the ADF IX paper on weakly performing countries (in the PNG CSPU for 2005–2006; 22 September 2005). However, all the CSPs and CSPUs identified weak governance and corruption as perhaps the most difficult constraints to pro-poor, sustainable economic growth.

⁴⁰ ADB 2001. *Long-Term Strategic Framework 2001-2015*. Manila.

⁴¹ ADB 2002. *New Business Processes for the Reorganized ADB*. Manila.

⁴² The recent revision to the business processes on country strategies and programs included a change in the title of the document to "country partnership strategies." However, this report will maintain the old nomenclature to avoid confusion when referring back to the Donors' Report.

⁴³ Even in a WPC with limited capacity, developing a results-based CPS has value in the discipline involved in in-depth analysis, participatory process, and putting in place a sound monitoring framework.

Table 2: Analysis of Country Strategies and Programs for Developing Member Countries Classified as “Fragile” in Two of Three Classification Schemes

Country	LICUS-World Bank	DFID-LICUS	Failed States Index	ADB consideration
Afghanistan CSP (02-04) 07-05-02 CSPU (06-08) 10-08-05	X	X	X	<input type="checkbox"/> Post-conflict <input type="checkbox"/> Least developed
Cambodia CSPU (04-06) 31-07-03 CSP (05-09) 25-01-05		X	X	<input type="checkbox"/> Poorest country <input type="checkbox"/> Poor-debt stressed DMC
Lao People’s Democratic Republic CSP (02-04) 27-07-01 CSPU (06-08) 09-08-05		X	X	<input type="checkbox"/> Least developed country (Government’s statement)
Nepal CSP (05-09) 01-09-04 RB CSP Doc Mar 06		X	X	<input type="checkbox"/> Conflict ongoing <input type="checkbox"/> Poorest country <input type="checkbox"/> Low incomes
Papua New Guinea CSPU (05-06) 22-09-05		X	X	<input type="checkbox"/> ADB’s WPC
Solomon Islands CSPU (05-06) 17-08-04	X	X		<input type="checkbox"/> Least developed PDMCs <input type="checkbox"/> Post-conflict
Tajikistan CSP (04-08) 01-10-03 CSPU (06-08) 19-07-05		X	X	<input type="checkbox"/> “Former” post-conflict <input type="checkbox"/> Low-income country <input type="checkbox"/> Poorest country
Uzbekistan CSPU (05-06) 24-09-04 CSP (06-10) 23-02-06	X	X	X	<input type="checkbox"/> B2 DMC (former C) <input type="checkbox"/> DMC in Transition

Note: LICUS = low-income country under stress; DFID=Department for International Development of the United Kingdom; DMC=developing member country of ADB; WPC=weakly performing country; PDMC=Pacific developing member country

D. Global Best Practices

26. *Application of the Paris Declaration in WPCs:* The Paris Declaration points out that: “while the guiding principles of effective aid apply equally to fragile states, they need to be adapted to environments of weak ownership and capacity and to immediate needs for basic service delivery.”⁴⁴ Building capacity and effective institutions in WPCs requires that both partner countries (DMCs) and donors make significant commitments. Partner country commitments in the Declaration revolve around good governance, ongoing dialogue, sound (yet simple) planning tools, and stakeholder participation. Donor commitments, all of which ADB strongly adheres to, focus on harmonization, alignment, avoiding activities that undermine national institutional building, and using an appropriate mix of aid instruments. These principles were discussed at length during the Senior Level Forum on Aid Effectiveness in London (January 2005) and eventually evolved into the Twelve Principles for Good Engagement in Fragile States. ADB’s approach to engaging with WPCs is both consistent with and supportive of the Paris Declaration.

⁴⁴ Paris Declaration, paragraphs 37-39.

27. *The Twelve Principles of Good Engagement*: OECD-DAC's Fragile States Group (formerly the Learning and Advisory Process on Difficult Partnerships) has developed 12 principles for good international engagement in fragile states (see Table 3).⁴⁵ These principles are high-level statements that require interpretation in any particular country setting.⁴⁶ For example, Principle 5 ("recognize the political-security-development nexus") in countries emerging from conflict would ensure that interventions are sensitive and supportive of peace-building. In a WPC recovering from conflict, the principle might imply support for government budget and service delivery while in a prolonged crisis the same principle might imply supporting service delivery through nongovernment entities or mechanisms with the objective of an eventual transition to government delivery.

Table 3: Organisation for Economic Co-operation and Development's Development Assistance Committee's Twelve Principles of Good Engagement

1. Take context as the starting point. All fragile states require sustained international engagement, but analysis and action must be calibrated to particular country circumstances.
2. Move from reaction to prevention. Action today can reduce the risk of future outbreaks of conflict and other types of crises and contribute to long-term global development and security.
3. Focus on state-building as the central objective. State-building requires focus on three pillars: (i) the capacity of state structures to perform core functions; (ii) their legitimacy and accountability; and (iii) their ability to provide an enabling environment for strong economic performance to generate incomes, employment, and domestic revenues.
4. Align with local priorities and/or systems. Where governments demonstrate the political will to foster development but lack the capacity, international actors should align assistance behind government strategies.
5. Recognize the political-security-development nexus. The political, security, economic, and social spheres are interdependent; failure in one risks failure in all others.
6. Promote coherence between donor government agencies. Close links on the ground between the political, security, economic and social spheres require policy coherence within the administration of each international actor.
7. Agree on practical coordination between international actors. Important areas include upstream analysis; joint assessments, shared strategies; coordination of political engagement; multi-donor trust funds; and establishment of joint offices and common financial reporting.
8. Do no harm. International actors should avoid activities which undermine national institution-building, such as bypassing national budget processes or setting high salaries for local staff which undermine recruitment and retention in national institutions.
9. Mix and sequence aid instruments to fit the context. Fragile states require a mix of aid instruments and long-term support for health, education, and other basic services are needed in countries facing stalled or deteriorating governance.
10. Act fast... Assistance to fragile states needs to be capable of flexibility at short notice to take advantage of windows of opportunity and respond to changing conditions on the ground.
11. ...But stay engaged long enough to give success a chance. Investments in development, diplomatic, and security engagement may need to be of longer duration than in other low-income countries; capacity development in core institutions will normally require an engagement of at least ten years.
12. Avoid pockets of exclusion ("aid orphans")

⁴⁵OECD-DAC, Development Cooperation Director, LAP, 2006. *Principles for Good International Engagement in Fragile States*.

⁴⁶ OECD-DAC 2005. *Piloting the Principles for Good International Engagement in Fragile States*.

28. *Strategic operational planning and operations vis-à-vis the 12 principles:* The principles provide a valid reference point for ADB's approach. Table 4 analyzes ADB's capacities (strengths and gaps) with reference to each of the 12.

29. *Continuing engagement:* Despite the challenges of operating effectively in difficult environments, ADB has continued to operate in weakly performing DMCs through its lending operations and technical assistance; country programming; and ongoing dialogue with governments, stakeholders, and development partners. Technical assistance continues to be important even when lending levels decline. The PBA policy has been implemented comprehensively and with integrity; as a consequence, there has been a reduction in resources. but there has been no disengagement. The PBA policy provides some protection for certain WPCs in particular through the allocation for the Pacific Islands⁴⁷ and funds set-aside (e.g., for Afghanistan and Indonesia).

⁴⁷ a separate pool equal to 4.5% of ADF resources

Table 4: Asian Development Bank Strengths and Gaps vis-à-vis Organisation for Economic Co-operation and Development's Development Assistance Committee's Twelve Principles of Good Engagement

Principle	Strengths	Gaps
1. Take context as the starting point.	Country strategies and programs (CSPs) are based on in-depth analysis of the country context.	More joint analytic work recommended. Political economy analysis should be deepened.
2. Move from reaction to prevention.	The Asian Development Bank (ADB) seeks to engage at earlier phases of fragility (i.e., before a downward spiral occurs).	Slow processing time makes it difficult to react quickly.
3. Focus on state-building as the central objective.	ADB emphasizes good governance and strengthening institutions. CSPs in weakly performing countries (WPCs) often feature significant policy reform as a prerequisite for effective aid.	Charter issues and the institution's mandate raise reservations. However, ADB recognizes the importance of institutional strengthening and good governance.
4. Align with local priorities and/or systems.	ADB works closely with partners to help governments and stakeholders articulate their concerns and needs.	ADB has rigorous business processes and requirements; using country systems in WPCs is problematic.
5. Recognize the political-security-development nexus.	ADB's "whole of institution" approach involves relevant departments/offices to jointly support operations in WPCs.	ADB has traditionally focused on development issues. Working with United Nations (UN) agencies will be increasingly important.
6. Promote coherence between donor government agencies.	ADB recognizes the validity of the whole of government approach and seeks to engage with a broad range of agencies and other institutions.	ADB lacks the resources to coordinate with diverse government agencies; this needs to be done in the context of development partnerships.
7. Agree on practical coordination among international actors.	ADB's approach is firmly grounded in strategic partnerships; this translates into both policy coherence and on-the-ground coordination.	Coordination is often challenging given weak government and institutions. International actors must understand one another's institutional objectives and find common ground.
8. Do no harm.	ADB takes into account potential risks in all its project designs. ADB's country analysis includes consideration of potential unintended consequences of interventions.	Analysis may not be comprehensive enough to allow full identification of all unintended consequences.
9. Mix and sequence aid instruments to fit the context.	ADB is committed to a sequential approach based on country analytics, consideration of absorptive capacity, and appropriate sequencing.	ADB's traditional instruments and modalities may not allow for optimal responsiveness.
10. Act fast...	ADB works closely with governments and development partners to begin designing interventions when early warning signs of fragility appear.	ADB's existing instruments and modalities are still cumbersome and slow to implement.
11. ...But stay engaged long enough to give success a chance	ADB engages with its DMCs on a long-term basis as long as the government requests such support.	Given ADB's relatively small portfolios in WPCs, obtaining measurable results is a long-term endeavor.
12. Avoid pockets of exclusion	ADB does not move in and out of countries; it remains there as a development partner. ADB's investment decisions are not driven by foreign policy or political considerations.	ADB has not adequately adopted its business processes and forms of engagement to deliver the optimal country program possible within constrained resource envelopes.

30. ADB is aware of and participates in the global dialogue on weak performance and fragility. ADB continues to (i) refine its approach to identifying and defining weak performance, (ii) re-think its operational planning, and (iii) adapt its business processes and instruments to ensure that its engagement is suitable and effective in the context of individual WPCs.

IV. THE ASIAN DEVELOPMENT BANK'S APPROACH TO ADDRESSING WEAK PERFORMANCE

A. Overview

31. *Continued relevance of original two pillars:* The challenges involved in working effectively in WPCs were discussed during ADF IX negotiations.⁴⁸ ADB's initial approach was based on two pillars that remain relevant as the core of its approach.

- (i) *Selectivity and focus:* ADB must be realistic in its objectives and develop selective, focused, and inclusive programs in WPCs. ADB assistance in WPCs will generally support a limited number of major reforms and establish and sustain inclusiveness among opposing constituencies. Effective programs often have a smaller absolute number of projects featuring relatively larger projects or sector-wide approaches consistent with priority public investment programs. Interventions will include a consistent focus on policy and institutional reform and achieving short-term benefits ("quick wins"). Given ADB's generally small portfolios in WPCs and the necessity for operating within the PBA policy, the likelihood of achieving development and poverty reduction objectives will be realistically assessed given resource constraints and the prevailing situation.⁴⁹
- (ii) *Strategic partnerships:* Consistent with the Paris Declaration⁵⁰ and other global commitments to harmonization and alignment, ADB collaborates closely with its development partners to avoid duplication of effort and to allow each institution to focus on its respective comparative advantages. Partnerships among donors enhance the effectiveness of aid by reducing the government's compliance costs and by minimizing duplication and wasted resources. Most importantly, partnerships can help establish and sustain country ownership and alignment with the national development plan.

32. *PBA and ADB's approach to WPCs:* Discussions in ADF IX made it clear that ADB's approach to engaging with WPCs is to be grounded in PBA:

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. ADB has already adopted a PBA system that rewards countries with appropriate development policies and institutions and the ability to use ADF funds effectively. This implies that strict application of PBA will lead to some countries receiving a diminishing share of ADF resources. This is already happening. Donors,

⁴⁸ ADB 2004. *ADB's Approach to Weakly-Performing Developing Member Countries*. Information paper for ADF IX Negotiations, Seoul, May 2004. ADB, 2004. *ADF IX Donors' Report: Development Effectiveness for Poverty Reduction*. Manila.

⁴⁹ In larger WPCs, a somewhat broader focus may be required.

⁵⁰ *Paris Declaration on Aid Effectiveness: Ownership, Harmonization, Alignment, Results and Mutual Accountability*. 2 March 2005, High-Level Forum on Aid Effectiveness.

however, emphasized that the needs of countries should be addressed within the PBA framework.⁵¹

Given that PBA is based on performance assessment, WPCs are likely to receive progressively lower allocations as performance deteriorates. The PBA system provides a basis for determining the nature of engagement, areas of support, and modalities for support to ADF countries including those identified as weak performers. In this context, the PBA is the necessary starting point for (i) identifying weak performance including by area/type, (ii) addressing gaps, and (iii) reinforcing areas of good performance.

33. *Application of LICUS methods to ADB DMCs:* According to the World Bank's LICUS methodology, weak performance is associated with CPIA scores of less than 3.0. As noted earlier, the LICUS group includes four ADF-eligible DMCs;⁵² however, applying LICUS methods to 2005 ADB country data (using CPIA methods to aggregate country scores and CPA individual cluster scores) yields no ADB DMC with an overall rating below 3.0. The two lowest scoring DMCs using this method are Solomon Islands (3.0) and PNG (3.1). The World Bank's 2005 CPIA scores, however, identify three ADB DMCs with scores less than 3.0: Republic of the Marshall Islands (RMI) (2.9), Solomon Islands (2.8), and Tonga (2.9). In addition to absolute scores, it is useful to look at relevant scores. Analysis of ADB country data using the LICUS method shows that two DMCs fall into the fifth quintile (PNG and Solomon Islands) and eight DMCs are in the fourth quintile (Cambodia, Kiribati, Lao PDR, RMI, Tonga, Tuvalu, Uzbekistan, Vanuatu). Of these ten countries, five have populations of fewer than 1 million (Kiribati, RMI, Solomon Islands, Tonga, Vanuatu).

34. *ADB's evolving interpretation:* ADB's approach to engaging WPCs in development adapts concepts from several of the definitions discussed in Chapter II, with the AusAID, DFID, LICUS, and OECD-DAC approaches being particularly relevant. ADB continues to focus on country performance as reflected in indicators such as negative growth rates and inadequate provision of public goods. Even if a WPC's performance improves and the country moves from the fifth quintile to the fourth (or the fourth to the third), that improvement may or may not reflect less fragility. ADB's approach in this regard is pragmatic and recognizes that performance lies on a continuum. Whether or not a particular DMC is formally classified as a WPC, it is important to recognize and take into consideration elements of both weak performance and fragility.

35. *Methodology to classify WPCs:* ADB will identify WPCs based on CPA rankings and conflict considerations. In order to be considered a "weak performer," a DMC would be either (a) ranked in the fourth and fifth quintiles on CPA assessments for 2 of the most recent 3 years or (b) considered to be in conflict or post-conflict and thus vulnerable.⁵³ This classification will be done on a rolling basis and will not be publicly disclosed. It is also important to note that weak performance and fragility do not disappear when a country shows a small improvement in performance scores that might move it above an arbitrary cut-off point such as a CPIA score of less than 3.0.⁵⁴ ADB recognizes this "spectrum of performance and fragility" and will encourage country teams in countries that might not be classified as WPCs but that exhibit evidence of weak performance to consider the tools, instruments, and modalities included in this approach. This classification is not intended to impair in any way the country's position as a member of ADB;

⁵¹ ADF IX Donors Report, para. 66

⁵² Although Myanmar currently has no access to ADF

⁵³ Using this methodology with data from the most recent PBA assessment yields 12 indicative WPCs: Afghanistan, Federated States of Micronesia, Kiribati, Lao PDR, Nepal, Papua New Guinea, Republic of Marshall Islands, Solomon Islands, Sri Lanka, Tajikistan, Timor-Leste, and Vanuatu.

⁵⁴ World Bank. 2005. *Low-Income Countries Under Stress: Update*. December 19 2005.

rather, the designation of weak performance is intended to draw attention to the challenges the country faces and to improve the effectiveness of ADB assistance in terms of developing capacity and helping it achieve its development objectives.

36. *A systematic and concerted approach is needed:* While ADB's approach to WPCs links allocation to performance, it also takes other dimensions into account. The following elements reflect ADB's experiences and global best practices. They should be seen as a "menu" from which ADB staff in regional departments can choose as appropriate in future operational planning.

B. Conceptual Framework: Differentiating the Country Context

37. While the governing principles and elements of ADB's approach are applicable to some extent in most WPCs, there is considerable variation in terms of political economy, development needs, capacity constraints, and reform orientation. Thus, it is important to determine, in any particular country, which elements are most relevant.

38. *Willingness to reform:* WPCs may be differentiated into three categories based on the willingness of the government to reform.

- (i) *Key leaders are committed to reform and are willing to serve as "champions:"* In these countries, development assistance may be accelerated. CSPs can be developed in collaboration with development partners, and priority investments can be identified and financed. Participatory processes can generate civil society support for reform, while capacity development can focus on improving public sector management and service delivery.
- (ii) *Commitment to reform is less advanced:* In these countries, efforts to raise public and stakeholder awareness of the need for reform are essential. This might involve policy dialogue and forums to help government and development partners clarify priorities and work with emerging champions to build a coalition for reform.
- (iii) *No commitment to reform exists and appears unlikely to emerge in the short term:* Engagement in these countries may be more limited with interventions focusing on monitoring to identify signs of support for reform, continuing policy analysis of key issues, and promoting government-civil society engagement.

39. *Size:* The development challenges in WPCs differ considerably by size of country. In the case of smaller WPCs, typically Pacific island countries, the focus of programming and donor coordination is likely to be on the country as a whole, while in larger WPCs assistance is more likely to be structured around particular sectors. In such countries, ADB's country programs would likely involve participation in program-based approaches and sector-wide approaches.

Table 5: Differentiation of Weakly Performing Countries by Model of Engagement and Possible Responses

Country Situation	Programming Issues	Probable Emphases of Program	Capacity and Accountability
Prolonged crisis or impasses	<ul style="list-style-type: none"> • Maintaining operational readiness for re-engagement • Supporting reconciliation dialogue • Analysis of socio-economic issues to identify entry points 	<ul style="list-style-type: none"> • Small grant-based financing supporting local economic development • Possibly working through non-government partners 	<ul style="list-style-type: none"> • Focus on institutional analysis, dialogue, counterpart training
Post-conflict or governance transition	<ul style="list-style-type: none"> • Rebuilding state capacity and accountability • Delivering “quick wins” • Focusing on public administration and service delivery 	<ul style="list-style-type: none"> • Joint needs assessment and planning for broad-based recovery • Linking political, social, economic, and security recovery • Critically evaluating instruments and modalities 	<ul style="list-style-type: none"> • Institutional strengthening • Supporting leadership and civil society • Transitional CDD and local interventions
Deteriorating governance or rising conflict risk	<ul style="list-style-type: none"> • Halting decline in governance and social services • Multi-donor conflict prevention efforts • Limited new financing 	<ul style="list-style-type: none"> • Use community approaches, private sector partners, nongovernment organizations, and ring-fenced mechanisms (possibly including service delivery and local economic development) 	<ul style="list-style-type: none"> • Focus on transparency, dialogue, and maintaining institutional capital to facilitate eventual turnaround • Focus on community-level conflict prevention and governance reform
Gradual reform process	<ul style="list-style-type: none"> • Build state capacity and accountability • Support ongoing reforms • Focus on public administration and service delivery 	<ul style="list-style-type: none"> • Boosting reform efforts • Supporting leadership • Communications initiatives • Capacity development 	<ul style="list-style-type: none"> • Sector and capacity building initiatives with oversight mechanisms

40. *Model for engagement:* Recent work by OECD-DAC and the World Bank has emphasized that a uniform approach will not and cannot be applied to all WPCs.⁵⁵ In this regard, they identify four models for engagement.

- (i) *Countries in prolonged political crisis:* These WPCs in many cases have arrears with MDBs, and there is seldom a consensus between development partners and the government on a development strategy or on poverty reduction objectives.
- (ii) *Countries in post-conflict or political transition:* These have highly fluid policy environments and opportunities for rapid reform often attributable to peace agreements and the potential for quick wins combined with national reconciliation or renewed international engagement.

⁵⁵ World Bank. 2005. *Fragile States: Good Practice in Country Assistance Strategies. Operations Policy and Country Services*, December 19, 2005. See also *Low Income Countries Under Stress, Update* December 19, 2005.

- (iii) *Countries with deteriorating governance or rising conflict risk:* There is often a lack of consensus among development partners and government about development strategies.
- (iv) *Countries going through a gradual process of reform:* These have at least some government leadership although reform is still gradual and periodic setbacks are likely.

Table 5, adapted from the LICUS/OECD-DAC work, shows potential programming issues, probable emphases, and capacity and accountability issues by model for engagement.

C. Operational Planning at the Country Level

41. *Determining with whom to work:* Country ownership and leadership are important in aid programs; however, given the weak ownership and accountability in many WPCs, determining how to proceed is a major early challenge. While ADB has traditionally provided development assistance to sovereign entities, generally national governments, operating effectively in WPCs requires the engagement of other partners such as subsovereign entities, nongovernmental organizations (NGOs), civil society organizations, and the private sector. In addition to playing a key role in institutional capacity assessments, NGOs can assist in joint strategy development, institutional capacity building, and project design and implementation (particularly in the social sectors). NGOs are also important for representing marginalized groups and for providing alternative perspectives on development.⁵⁶ ADB works with such partners to support increased government involvement, leadership, and ultimately ownership. NGOs can also (in some cases) help deliver essential public services; however, in such cases it is important to assess the implications of strengthening alternative channels of service delivery for the public sector, the labor market, social welfare, and poverty reduction.⁵⁷

42. *Special challenges for harmonization and alignment:* While improving harmonization and alignment is especially important in WPCs,⁵⁸ implementation is problematic. Governments in many WPCs lack the capacity to accurately identify and document development priorities and face challenges in coordinating aid, for example (i) coordinating funds, agencies, and technical assistance across donors; (ii) developing information systems for monitoring and evaluating programs; (iii) establishing financial control and procurement systems; and (iv) directly managing a limited portfolio of national programs. Development partners may thus find they are seeking to align with a government development strategy that does not exist. In such situations, innovative approaches such as “shadow alignment” (e.g., aligning donors’ systems with local planning and budgeting cycles) can help support eventual alignment with national systems. Development partners also may find that while using parallel systems and relying on project implementation units may be essential for designing and managing projects, they may also undermine government capacity and jeopardize long-term sustainability. Donors must usually work harder at coordination given the fact that many agencies are typically active in WPCs, each operating using its own systems.

⁵⁶ ADB 1998. *ADB’s Policy on NGO Cooperation*. Manila.

⁵⁷ DAC Fragile States Group 2005. *Service Delivery in Fragile States: Advancing Donor Practice*. Concept note prepared by USAID and UNICEF.

⁵⁸ Overseas Development Institute 2005. *Harmonization and Alignment in Fragile States*. Discussion paper for the Senior Level Forum on Development Effectiveness in Fragile States.

43. *Getting harmonization and alignment started:* During the early stages of engagement, the first steps toward improved harmonization are often taken by a small group of like-minded donors. In some cases, the government is relatively disengaged due to political disorder, institutional breakdown, or the many other difficult circumstances that occur in WPCs. As country leadership of aid coordination improves, adjustments are likely to be needed. While the ideal is for the government to lead, it is also important for donors to coordinate among themselves.

44. *Supporting and nurturing country ownership:* Supporting and nurturing country ownership in a WPC is challenging. Case studies developed for the 2006 Asian Regional Forum on Aid Effectiveness suggest a number of tactics that are useful in this regard. Policy dialogue should focus on advising DMCs how to achieve their development objectives rather than being prescriptive. Capacity development initiatives aim to support central policy-making and budget functions. Country ownership is also supported through ADB's role as an agent of change and a knowledge institution. ADB is open and sensitive to changes in the global development environment and helps governments and other stakeholders in WPCs create models and solutions appropriate to their environments. This knowledge function includes providing governments with tools to assist them in improving the quality of their own diagnostic assessments. It is also important to respect the political constraints that exist in WPCs and work toward incremental change. Furthermore, consistent with OECD-DAC principle #11 ("stay engaged long enough to give success a chance"), ADB invests in long-term relationships and to sustain engagement over extended periods of time.

45. *Joint analyses:* Ideally, key areas for donor collaboration include (i) initial needs assessments and political economy analyses; (ii) joint diagnostic studies of processes and systems; and (iii) identifying an overarching set of properly sequenced interventions; however, in many WPCs, donors conduct their own country assessments and can potentially reach differing conclusions⁵⁹ resulting in conflicting policy positions and in programs that are less than complementary. Thus, it is important to find ways to harmonize the findings of country assessments. Development partners can collaborate, or a single agency might conduct the analysis. In the case of the latter, it is important that the other institutions relying on that analysis have inputs into the assumptions, design and methodology.

46. *Getting the diagnostics right:* It is essential to develop a clear understanding of the development issues in the country using tools such as poverty analyses, sector analyses, thematic analyses, and conflict sensitivity assessments. These analyses provide an accurate diagnosis of the country's economic, social, cultural, and political dimensions. One potentially useful tool is scenario planning, a method for understanding the nature and impact of the most uncertain and important driving forces affecting the future. While this method was originally developed as a strategic management tool in the private sector, in the context of ADB operations in WPCs, scenario planning provides a useful tool for adapting the country program to a dynamic and less predictable environment.

47. *Challenges to systematic analyses:* The challenges for conducting such analyses in WPCs, however, are many. It is desirable that the government take ownership of and guide national development and poverty reduction objectives—whether or not there is a formal process for developing a poverty reduction strategy. Given typical gaps in capacity, this may not be feasible. Thus, it is important that donors support governments in setting clear priorities, in

⁵⁹ Such inconsistent findings may be attributed to factors such as greater experience; use of differing methodologies; and/or differing institutional priorities and areas of attention.

developing realistic estimates of timeframes and costs of interventions, and in identifying parameters of donor coordination (including country programming and capacity development). While all ADB development assistance aims to generate economic growth and reduce poverty, aid in WPCs may serve other important development objectives. For example, well-coordinated interventions help prevent instability and the escalation of conflict, improve human rights, slow or reverse deterioration in basic human development indicators, and prevent spillovers to neighboring countries. It is also important to assess the impact that strengthening alternative channels of service delivery may have on building capacities in the public sector.

48. *Assessing absorptive capacity:* Capacity in WPCs is likely to be limited by underdeveloped human resources, deteriorating infrastructure, and security concerns. Thus, investments in capacity development that are premature or excessive are unlikely to have the desired impact. Careful sequencing of technical assistance to build capacity (generally prior to other types of financial assistance) is vital. As capacity is developed in government agencies, the ability to effectively use additional technical assistance may improve. For example, absorptive capacity in post-conflict countries has remained relatively low during the first 3 years or so after the cessation of hostilities, followed by dramatic improvements by the end of the first decade post-conflict.⁶⁰

49. *Operating in conflict and post-conflict environments:* Conducting a conflict assessment early on is important; there are a number of valid, useful tools for this purpose. For example, USAID's Conflict Assessment Framework⁶¹ seeks to analyze and understand the root causes of conflict, then maps existing development programs to them. The World Bank's Conflict Prevention and Reconstruction Unit also provides useful tools, including social assessments that focus on, "patterns of distribution of resources within a society" and inclusiveness as key dimensions.⁶² The World Bank's Conflict Analysis Framework assesses the causes and consequences of conflict, determines a country's resilience in the face of conflict, and supports development of appropriate, conflict-sensitive development programming.⁶³ The analysis also assesses a country's resilience to conflict and how it can be strengthened through development assistance. Also useful is the Peace and Conflict Impact Assessment developed by the Canadian International Development Agency and the International Development Research Centre.⁶⁴ Security issues must also be addressed.⁶⁵ In a WPC involved in a conflict or in its immediate aftermath, security concerns emerge in support for the delivery of badly needed health services or for high-impact infrastructure projects. It is important that donors constantly communicate with one another, especially given the differing mandates and roles of international agencies.

⁶⁰ Collier, Paul and Anke Hoeffler. *Aid, Policy and Growth in Post-Conflict Societies*, World Bank Working Paper, Oct. 2002.

⁶¹ USAID Office of Conflict Mitigation and Management 2005. *Conducting a Conflict Assessment: A Framework for Strategy and Program Development*. The toolkit provided with the framework includes components for Youth and Conflict, Land and Conflict, Minerals and Conflict, Livelihoods and Conflict, and Forests and Conflict.

⁶² World Bank 1998. Holtzman, Steven, Ann Elwan, and Colin Scott. *Post-conflict Reconstruction: The Role of the World Bank, Volume 1*.

⁶³ World Bank Social Development Department, Conflict Prevention and Reconstruction Team. *Conflict Analysis Framework*. Draft 11 April 2005.

⁶⁴ Research Center for Constructive Conflict Management. *Peace and Conflict Impact Assessment Methodology*.

⁶⁵ In some high-risk environments, ADB, UN, and NGOs have had to withdraw due to security concerns for staff.

D. Modalities and Instruments of Assistance

50. In order to address the unique circumstances and needs of each WPC, ADB should explore new and more flexible modalities and instruments of assistance. Following are some innovative choices that will enhance the responsiveness and effectiveness of ADB's programs in WPCs.

51. *Feasibility and appropriateness of CSPs in WPCs:* Many WPCs lack the necessary capacity to take full ownership of the CSP, particularly given the expertise required for developing a results-based CSP. Thus, ADB will in some cases relax expectations for CSPs and selectively accept other, less extensive programming documents. In countries in which operations have been suspended, ADB will consider the use of a re-engagement note developed jointly by development partners to define broad objectives, interventions, and methods for working together. For example, in Somalia, one of world's most fragile countries, the World Bank and UNDP developed a re-engagement note with a structure much simpler than the usual country assistance strategy⁶⁶ focusing on (i) organizing principles of re-engagement; (ii) strategic entry points; (iii) roles and responsibilities; (iv) financing; (v) partnerships; and (vi) risk considerations. The note also clearly defined the development objectives of providing basic public goods, accelerating socio-economic recovery, and creating an enabling environment for long-term institutional and policy change.

52. *Project implementation units:* In WPCs where local capacities are insufficient to handle program or project administration, ADB may expand use of these units in the interest of achieving quick wins. Notwithstanding the aspirations in the Paris Declaration, such units are likely to be the only realistic option in many WPCs, particularly where significant improvements in essential services are urgently required. However, steps need to be taken to ensure that they are progressively and fully integrated into public sector service delivery systems. A 2005 ADB Special Evaluation Study⁶⁷ found that approximately 90% of ADB's investment projects are managed using some type of project implementation unit. The study pointed out that they are a legitimate and justifiable tool for improving project implementation, but are not generally intended to build human or institutional capacities. ADB will reduce the risk that freestanding units might undermine public sector capacity by identifying possible overlaps with the functions of the parent agency, staff composition, and exit strategies during project design.

53. *Expanded use of grants:* In many WPCs, limited debt-servicing capacity severely constrains the amount of debt that can be assumed, including concessionary ADF resources. Indeed, in some WPCs, the government may be unable to make a decision to borrow, so even a small provision of grant financing can enhance the level of engagement. This may take one of three forms.

- (i) Debt-stressed ADF countries identified as WPCs that are eligible for the ADF IX grant program (under any grant allocation framework) could be encouraged to take full advantage of their grant allocations.⁶⁸
- (ii) ADB might judiciously enter into innovative co-financing agreements in which bilateral donors finance activities that are managed by ADB in a trust fund. Administering multidonor trusts funds that could be approved and disbursed

⁶⁶ UNDP/World Bank, Somalia. *Country Re-Engagement Note*. April 2003

⁶⁷ ADB 2005. *Special Evaluation Study of the Role of Project Implementation Units*.

⁶⁸ However, there is no intention to modify the donor-agreed ADF IX grant allocation framework.

outside the PBA framework permits ADB to remain engaged and provide meaningful assistance in WPCs. In some highly-indebted countries, such grant funds may be used to help service debt or possibly repay part of arrears (including to lenders like ADB). ADB will, as requested, provide policy advice and technical assistance to help countries establish such trust funds with the appropriate governance arrangements. ADB will also consider using its concessional funding resources to provide seed money for the establishment of trust funds, with the aim of attracting larger contributions from other donors or from the government itself.⁶⁹

- (iii) ADB will, in some cases, help WPCs create endowment trust funds in which the principal is invested by professional fund managers and only the annual income or revenue or a portion thereof is used for priority expenses. This approach helps a country preserve windfall revenues (including transfers from donors) or revenues from non-renewable resources instead of using them for unsustainable and nonproductive expenditures (e.g., expanding the size of the civil service or increasing public sector salaries). There is also the risk that such revenues would finance low-yielding or high-risk project investments. An endowment fund can also help a country ensure that priority expenditures are sustained for essential social services or for infrastructure maintenance.

In the case of either multidonor trust funds or endowment trust funds, relatively small multi-purpose grants (up to \$1 million) could be established and cleared for disbursement within a short period of time to allow interventions to begin while a more comprehensive program is formulated.

54. *Adapting elements of the Innovation and Efficiency Initiative (IEI)*: The IEI has introduced new modes for ADB operations, although largely for middle-income countries. However, certain aspects of the IEI are relevant for use in WPCs. For example, the multitranche financing facility can assist WPCs in better managing their debt while sustaining long-term engagement. Also relevant are streamlined procurement policies (including for consulting services) and enhanced cost-sharing and expenditure-eligibility criteria, including financing for recurrent expenditures.

55. *Community involvement*: ADB will increasingly use project and program design methods that increase the role of intended beneficiaries in the absence of an adequately performing government. It is essential that beneficiaries be involved in planning and in decisions regarding investments in local development projects.⁷⁰ Such community involvement plays a key role in situations where the national government is not functioning and local government units lack capacity. However, it should also be recognized that community projects in a WPC with unstable governance or security conditions can be problematic and may be difficult to scale up given lack of capacity at higher levels.

56. *Multiyear, longer-term, technical assistance*: Medium- to long-term technical assistance projects can play an important role in building the capacities of central and sector agencies. ADB will develop innovative project designs, including government-wide, multisector, and single-sector approaches. Such technical assistance provides a useful tool for strengthening weak institutions that lack the capacity for policy formulation and basic service delivery and

⁶⁹ ADB has provided such advice and seed money, using ADF resources, in the case of the Federated States of Micronesia, the Republic of the Marshall Islands, and Tuvalu.

⁷⁰ ADB. 2006. *A Review of Community-Driven Development and its Application to the Asian Development Bank*.

would not supplant the public sector. Consistent with the Paris Declaration, this new instrument will be implemented in partnership with both multilateral and bilateral institutions, including through cofinancing.

57. *Non-accrual status:* Some ADF-eligible DMCs that exhibit weak performance may be in non-accrual status. Under current ADF policy, the existence of arrears would preclude resuming ADF financing. Given the possibility of grant financing under ADF IX, Management or Board decisions might be required on whether such sanctions would be applicable only to ADF loans or to grants as well. In this regard, there are two key considerations: (i) WPCs in arrears are likely to have pressing needs for ADF grant assistance; and (ii) grant financing might be used to clear those arrears from ADF.

E. Business Processes

58. ADB's approach to engaging with WPCs recognizes that existing business processes sometimes constrain effective operations. In order to be effective, ADB will develop and implement innovative approaches, both in terms of sustaining the effectiveness of existing operations and in deploying new types of assistance. The capacity constraints and weak public sector management characteristic of WPCs also require that interventions be designed and implemented quickly, that is, within a timeframe shorter than ADB's usual processing and project cycle. Each country is unique and will require different responses and instruments. ADB will continue to use its normal business processes where they can be used effectively. However, in WPCs in which such standard methods are unlikely to meet pressing development needs, relaxing some constraints and introducing innovative instruments will be required.

59. *Relaxation of business process requirements:* With the approval of Management or the Board of Directors, as appropriate, some of ADB's existing business processes could be relaxed, including procurement, disbursement, project appraisal requirements, and project processing. This flexibility will include a willingness to recognize or apply procedures of other institutions (as is already done to some extent for current multidonor trust funds). Relaxation is particularly important when coordinating with bilateral partners providing a relatively large amount of assistance that have expressed an interest in partnering with ADB; it is in the institution's interest to find ways to work together and not to delay interventions. Such flexibility would make it easier for ADB to participate in joint donor programs, to pursue program-based approaches, and to otherwise react more quickly and flexibly in WPCs. Some areas in which selective relaxation of ADB's requirements will be considered include:

- (i) *Rates of return on program/project feasibility assessments:* Programs and projects in WPCs should not be expected to always yield the same financial and economic rates of return as would be expected in stronger performing DMCs. If ADB wishes to stay engaged in providing development assistance in WPCs, it must recognize that the financial and economic risks of investments are higher and that lower returns are likely.
- (ii) *Administration fees:* For sector-wide approaches or program-based approaches where donor funds would be pooled and where there are sound arrangements to account fully for the use of donor funds, ADB will consider waiving its usual administration or partial administration fee; however, the waiver would depend on the specific circumstances of the cofinancing arrangement.

- (iii) *Project accounts*: ADB will consider waiving its requirement for separate accounts for its funds in situations where there are sound arrangements in place to account for its contribution.
- (iv) *Counterparts*: In implementing technical assistance or investment projects, local counterparts will be required wherever possible. This is particularly the case when the WPC has excessive or redundant employment in its civil service. However, in some cases, competent counterparts may not be available, or it may not be possible to retain qualified individuals given out migration and other factors. In such cases, ADB will consider requesting the government to outsource the counterpart requirement to civil society, including local businesses, local NGOs, or faith-based groups.
- (v) *Monitoring, reporting, and auditing arrangements*: In situations where adequate reporting systems and auditing arrangements are in place, ADB may not require separate arrangements. Such requirements often create a significant burden on governments of WPCs, particularly given the administrative demands of managing a multidonor program.
- (vi) *Eligibility and modes of procurement*: ADB might consider relaxing its eligibility rules for the procurement and engagement of consultants in situations where doing so would contribute to a harmonized approach among donors. In general, this greater flexibility will ease project implementation.

F. Institutional Management and Support

60. *Formal understanding with partners*: Several of ADB's partnerships are formalized in memoranda of understanding (MOUs) that lay out parameters for collaboration.⁷¹ The ADB-UNDP MOU, for example, identifies collaboration on capacity building for good governance (including anticorruption) and civil society participation and development as high priorities; these are important areas for collaboration for development institutions working in WPCs. More specifically, the MOU commits the respective institutions to review the potential for cooperation (and where possible to implement cooperation) in (i) post-conflict rehabilitation and reconstruction activities in Timor-Leste and/or the Solomon Islands and (ii) the further development of UNDP's multi-user database for monitoring post-disaster rehabilitation and reconstruction in Indonesia, Maldives, Sri Lanka, and Thailand. ADB will continue to enter into such formal agreements with development partners, including country-specific MOUs or other agreements that clearly define the roles and commitments of partners in WPC development objectives.

61. *Capacity development for MfDR*: ADB is committed to MfDR in all of its operations. Implementation is being guided by the MfDR action plan that proposes an incremental and phased approach to facilitate learning.⁷² The plan acknowledges the capacity limitations for MfDR in DMCs in general; this observation is even more relevant for WPCs. In WPCs, results frameworks need to accommodate longer time frames and set realistic targets. There are many cases where the impact on poverty alleviation or on key social and economic indicators may be

⁷¹ ADB now has MOUs with the World Bank, the United Nations Economic and Social Commission on Asia Pacific (UNESCAP), the International Labour Organization (ILO), and the United Nations Development Programme (UNDP).

⁷² ADB 2006. *Managing for Development Results in ADB: Revised Action Plan*. Draft, June 2006.

achieved only after a decade or more. Over the short to medium term, there are likely to be only incremental changes in institutional capacities, public awareness, political commitment, conflict resolution, stakeholder involvement, and the existence of a critical mass of agents for change—all factors that have important implications for monitoring and reporting indicators. Capacity development in WPCs requires long-term commitment and appropriate customizing of approaches and tools. As part of this effort, ADB identifies potential champions and key practitioners and provides them with concrete support. To help build capacity, ADB's results management unit (SPRU) has implemented a community of practice in MfDR, a virtual learning network to promote knowledge exchange among public managers, organizations, executing agencies, and practitioners. There are currently 13 participating DMCs, at least four of which have exhibited evidence of weak performance (Cambodia, Lao PDR, Nepal, and Tajikistan). It is also important to build capacity in national planning and statistical ministries. In that regard, the Development Indicators and Policy Research Division of ADB's Economics and Research Department has supported capacity building in national statistical organizations for years and now focuses on lower-income and weakly performing DMCs.⁷³

Box 3: Supporting Policy Coherence through the Transitional Results Matrix

One useful tool in weakly performing countries is the transitional results matrix (TRM), a multidonor coordination and monitoring tool that helps to identify and monitor realistic priorities, while improving coherence of overall aid across political, security, economic, development, and humanitarian domains.⁷⁴ The World Bank and the United Nations Development Programme used a TRM in Timor-Leste to (i) manage investments, (ii) clarify government and partner expectations and (iii) provide guidance for resource mobilization and sector allocations. Partners developed their programs consistent with an action matrix discussed at biannual meetings. The action matrix allowed country-level monitoring of development activities, including areas outside the mandate of the multilateral development banks (i.e., conducting elections, supporting adoption of a constitution, maintaining security). The use of the TRM has several benefits, including providing a planning and coordination tool for the government, stakeholders, and donors; prioritizing activities; avoiding gaps and fragmentation of assistance (harmonization); and serving as a results-based framework for enhanced efficiency.

62. *Staff incentives:* ADB Management is aware that staff may not be overly motivated to work in WPCs given that that lending pipelines are often smaller and that the degree of effort required to accomplish many tasks is greater than in less difficult environments. In some WPCs, ADB will focus mainly on process and change management rather than on activities for which progress is more easily measurable through loans disbursed, technical assistance activities processed, or improved development indicators. Thus, appropriate mechanisms will be devised to evaluate and recognize staff performance in countries where progress is slow and often discouraging and where significant development impact is unlikely to be achieved in even the medium term. Staff will be recognized for solving complex development problems, building strategic partnerships, and developing innovative approaches that effectively address demand in WPCs (see Box 3). Steps will also be taken to ensure that modest lending levels due to fragility and difficult environments do not lead to negative staff performance evaluations. In this regard, ADB's performance development plan introduced in 2005 provides a tool for assessing and managing staff performance and for focusing work outputs on measurable results with specific reference to WPCs.

⁷³ ERD also produces numerous statistical reports that support ADB operations and that represent a public good for DMCs and the development community.

⁷⁴ United Nations Development Group and World Bank, *An Operational Note on Transitional Results Matrices: Using Results-Based Frameworks in Fragile States*, January 2005.

63. *Resident missions:* The effectiveness of ADB's approach to WPCs hinges on responsiveness and flexibility. The resident missions (RMs) in WPCs represent ADB's "eyes and ears" and monitor situations that can change dramatically. RMs must play a central role in implementing the approach and provide leadership at the country level, including coordinating with other donors. RMs are also responsible for in-country resource mobilization, participating in the policy dialogue, and engaging with civil society. ADB recognizes the challenges of working in the most difficult environments and has provided special support for staff assigned to, for example, the Afghanistan RM. ADB's Resident Mission Policy, adopted in February 2000, recognized that the increased complexity of the development agenda and ADB's focus on poverty would require expanded capacity in DMCs.⁷⁵ According to the review,⁷⁶ measurable progress has been made in implementing the mandate of the policy; however, there is considerable variation across RMs, and the skill mix in many RMs in WPCs is likely to require refinement. Headquarters staff may be temporarily assigned to RMs to provide training in such areas as governance, anticorruption, and conflict assessment. ADB will review the competency profiles of staff posted to RMs in WPCs with consideration given to assigning staff experienced with analytic work, policy dialogue, policy and institutional reform, and change management (see Box 4).

V. RESOURCE IMPLICATIONS OF THE APPROACH

64. ADB's approach will be implemented within the prevailing operational resource budget, including ADF allocations determined by the PBA system, and other resources will be mobilized as appropriate. The key will be more focused mobilization and allocation to improve development effectiveness.

65. *Probable increased demand for technical assistance:* The emphasis on capacity development will likely lead to expanded demand for nonlending products including technical assistance to build capacity and, on a case-by-case basis, to support growth-oriented projects providing a "development dividend," subject to commitment to reform. ADB's increased engagement with NGOs/civil society may also generate additional demand for technical assistance resources; RMs will identify efforts to support additional resources integrated into normal strategic planning (e.g., work program and budget framework). Further, as evidenced in Afghanistan and Cambodia, in some cases large injections of both loan and grant financing are needed to supplement technical assistance.

66. *Importance of partnerships for mobilizing resources:* Innovative arrangements with partners are important for leveraging resources, whether cash or in-kind. Creative cofinancing arrangements will be explored. Resources may also be provided by donors in the form of trust funds. If such funds are established, they will not be country specific; rather, fund resources will be available to any WPC. Such funds will be open for multidonor contributions and be managed as a regular part of ADB's technical assistance portfolio. The determination of the circumstances/conditions under which ADB engages in cofinancing and other relationships with bilateral partners rests with the regional departments. The same processes and procedures that apply to normal ADB operations are applicable—any deviations from the norm will be dealt with on a case-by-case basis.

⁷⁵ ADB 2000. *Resident Mission Policy*. Manila. The objective of the RM Policy was to provide a framework within which RMs could (i) more effectively support the implementation of ADB's strategic agenda (and especially the PRS); (ii) strengthen in-country knowledge, expertise, and activity; and (iii) ensure greater country focus.

⁷⁶ IN.157-02. *Review of Progress in Implementation of the Resident Mission Policy*. 8 July 2002.

Box 4: Changing Profile of ADB Professional Staff

The profile of professional staff has changed significantly over the last few years as many younger and less experienced people have been recruited. Many mission leaders are now younger and less experienced than has historically been the case. During the 1980s and early 1990s when the development agenda was somewhat less complex, operations departments could afford to give less experienced staff (new hires) time to “feel their ways” and “grow into” the job. However, since the adoption of the Poverty Reduction Strategy and the emergence of a more demanding development agenda, the pressures on staff have grown exponentially.⁷⁷ The combination of less experienced team leaders, scarce human resources, and a more complex agenda creates challenges for the organization—especially in a fragile or difficult environment.

67. *Staffing and skill mix:* Working in WPCs requires skill sets and competencies that will continue to challenge ADB staff. To build internal capacity, both at Headquarters and in RMs, ADB will survey available “toolkits” and training programs and adapt them as appropriate. The regional departments will plan ahead for the skill mix required to implement operations in WPCs; this is an operational decision with implications for professional staffing. RMs seeking to augment country operations may mobilize new resources through technical assistance or cofinancing. Additional staff requirements will be met in one of several ways. If staff with expertise in working in WPCs are available, they could be deployed to RMs. Specialized staff could also serve as a resource for staff in other departments (i.e., a role similar to that of lead sector specialists). Operational capacity could be enhanced through redeployment or innovative arrangements with partners; this might include secondments or other arrangements. Such assignments of non-ADB staff should be to specific countries, with engagements based on a clear scope of work and a finite timeframe. Another option would be to establish a dedicated unit or position to support ADB’s operations in WPCs. Staffing could be provided by member countries that choose to sponsor a staff consultancy for a fixed period or through additional resources provided by member countries. Such a unit/position would support implementation of the approach, including coordinating ADB engagement in global forums, supporting partnerships with other development organizations and civil society, and driving knowledge transfer and capacity building.⁷⁸ In this case, regional departments would retain primary responsibility for implementing ADB’s approach in WPCs but would receive coordinated support from the dedicated unit/position.

VI. CONCLUSION AND REQUEST FOR GUIDANCE

68. This paper has described ADB’s experiences in WPCs over the last 3 years and has presented ADB’s approach as it has evolved since ADF IX negotiations. The approach has been widely reviewed within ADB. Regional departments (including RMs) and other offices reviewed earlier drafts and provided extensive feedback. The approach has been discussed with Management, and their comments and guidance have been incorporated. It has also been discussed informally with members of the Board. It is in this context that ADB welcomes the feedback and guidance of donors during the discussions at the ADF IX mid-term review.

⁷⁷ ADB, 2003. *Implementation of the Reorganization of the Asian Development Bank* (IN.138-03), 25 June. Manila.

⁷⁸ The World Bank has a dedicated LICUS unit to support implementation of the LICUS initiative, provide advice to operations, and promote the use of fragile states approaches across the bank.