ADF Graduation:
Implications for the AfDB and its Client Countries

Discussion Paper

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This paper does not necessarily reflect the views of the African Development Bank Group (AfDB or the Bank), its Board of Directors or the countries they represents. This paper was prepared for the fourth meeting of the African Development Fund (ADF or the Fund) Working Group held on 29-30 May, 2015. The views proposed in the paper are not meant to be exhaustive but to facilitate discussions among members of the ADF Working Group.

Executive Summary

Currently, forty (40) regional member countries (RMCs) are eligible to the African Development Fund (ADF or the Fund) – the soft-loan window of the African Development Bank Group (AfDB or the Bank). By 2022, thirty-seven (37) countries will remain eligible to the ADF. However, these numbers hide some nuances. In all likelihood, three (3) additional countries will have graduated to the African Development Bank (ADB) category, three (3) will be classified as “blend” countries and seven (7) will be classified as “gap” countries, while at the same time opening up access for these countries to potentially larger pools of resources on tighter terms. Africa will also be the home of the majority of poor people in the world, estimated to be one (1) billion.

The ADF will increasingly be dominated by fragile and conflict-affected states, characterized by weak state capacity and vulnerability to a range of shocks. However, while the increase in the needs of this subset of states (as well as that of the Bank’s other low income clients) are expected to continue, concessional aid is projected to remain limited. This situation underscores the continued need for concessional resources and the need to develop tailor-made mechanisms aimed at addressing the specific needs of ADF eligible countries.

This paper discusses some of the key implications of the potential country graduations from the Fund for ADF donors, for the Bank, and for its clients. Among other things, the paper highlights the need to strategize on the:

- Gradual shift from the ADF;
- Change in the ADF’s client base to increasingly comprise of fragile states;
- Projected increases in allocations for the remaining eligible countries on present trends;
- Potential effects of accelerated repayment of existing debt and termination of debt relief by or for ADF graduates;
- Need to address the pockets of poor populations in all the Bank’s client countries; and
- Need to rationalize the role of the ADF in the changing aid architecture.

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Abbreviations

ADF	African Development Fund
ADF-12	Twelfth General Replenishment of the African Development Fund
ADF-13	Thirteenth General Replenishment of the African Development Fund
ADF-14	Fourteenth General Replenishment of the African Development Fund
ADF-15	Fifteenth General Replenishment of the African Development Fund
AEO	African Economic Outlook
AfDB	African Development Bank
AIDI	Africa Infrastructure Development Index
APC	Accelerated Payment Clause
CPIA	Country Policy and Institutional Assessment
CRC	Credit Risk Committee
DSA	Debt Sustainability Assessment
DSF	Debt Sustainability Framework
FDI	Foreign Direct Investment
GDP	Gross Domestic Product
GNI	Gross National Income
HIPC	Heavily Indebted Poor Countries initiative
IDA	International Development Association
IMF	International Monetary Fund
LIC	Low Income Country
MDGs	Millennium Development Goals
MDRI	Multilateral Debt Relief Initiative
ODA	Official Development Aid
PBA	Performance-Based Allocation
PC/pc	Per Capita
PCG	Partial Credit Guarantee
PPF	Project Preparation Facility
PRG	Partial Risk Guarantee
PRGT	Poverty Reduction and Growth Trust funds
PSF	Private Sector Credit Enhancement Facility
RMC	Regional Member Country
SDG	Sustainable Development Goals
SSA	Sub-Saharan Africa
TSF	Transition Support Facility
UA	Unit of Account
USD	United States Dollar
VLP	Voluntary Loan Prepayment
WEO	World Economic Outlook

ADF GRADUATION: IMPLICATIONS FOR THE AFDB AND ITS CLIENT COUNTRIES[1]

1. Introduction

1.1. A number of the African Development Bank Group's (AfDB or the Bank) low-income regional member countries (RMCs) are slowly climbing up the income ladder, mobilizing increasing amounts of domestic resources, and in turn, enhancing their ability to access other kinds of finance beyond concessionary resources. Several of them are set to 'graduate' from concessionary finance over the coming decade. But that is just the beginning. Graduating from the ADF has various other implications for the Bank and its RMCs, both good and bad.

1.2. This paper updates the projected graduation scenario presented during the 3rd ADF Working Group meeting and examines some of the implications of this graduation for the Bank and its client countries. The focus period is between 2015 and 2022. At that time, the Bank will be concluding the ADF-15 cycle and preparing for the ADF-16 replenishment. The year 2022 will also mark the end of the Bank's current Ten Year Strategy 2013-2022 (TYS) at a time when Africa will be home for the majority of poor people in the world, i.e. nearly one (1) billion.

1.3. The paper projects that between this ADF-13 cycle and 2022 (i.e., at the end of the ADF15 cycle), three (3) additional countries will have graduated to the ADB category and three (3) will be classified as "blend" countries. However, for thirty-one (31) countries, the ADF will remain the main source of financing from the Bank. Collectively, the ADF countries will represent 639.8 million inhabitants of which 487.2 million will still living on less on USD 2.50 a day. At the same time, many of the remaining ADF-eligible countries will largely be fragile or post-conflict states, characterized by weak state capacity and acute vulnerability to a range of shocks. This evolving client base will have some implications for the ADF's and the AfDB's financial models and operational priorities vis-à-vis the fight against poverty. We summarize some of these implications in this paper.

1.4. The paper is presented in 4 sections. Following this introduction, section 2 provides an overview of Africa's economic trajectory over the past decade and some of the continent's enduring challenges in the medium-term. Section 3 briefly summarizes the ADF's graduation process and a summary of the results and methodology used to simulate projected graduations between now and 2022. Section 4 discusses some of the key implications of the graduation process for the Bank and its client countries. Section 5 concludes.

2. Africa's Economic Trajectory and Challenges

Economic Performance

2.1. The evolution in the Bank's client base through the projected ADF graduation in the next several years comes at the backdrop of the much-discussed decade of rapid growth across much of Africa. The continent registered close to 5% growth on average over the past ten (10) years, during which it became the second fastest growing continent in the world after Asia. Its growth has been broad, covering its vast regions, and including countries with marked differences in resource endowments. Furthermore, Africa's growth has been fairly resilient, notably during the 2008/2009 global recession, when growth contracted sharply elsewhere but remained impressive on the continent following a short-lived downturn.

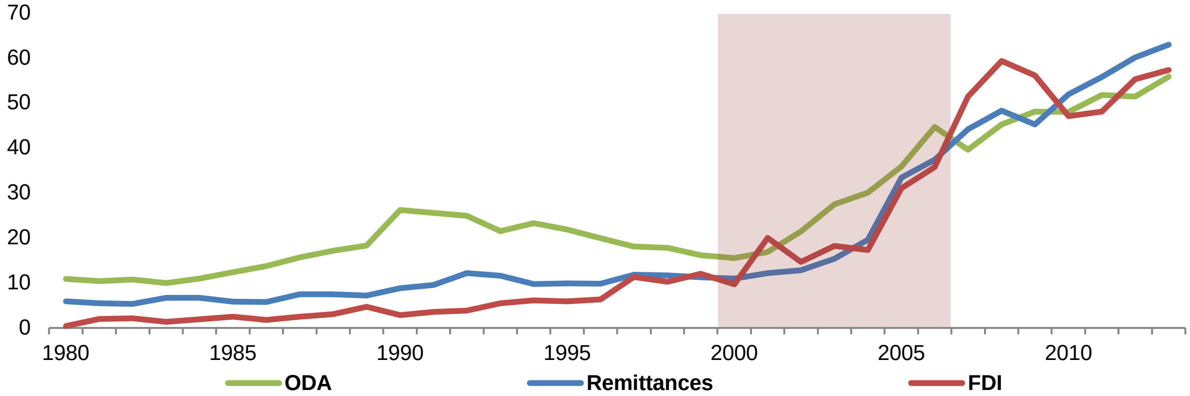
2.2. The remarkable progress of the continent can be explained by several factors. In addition to the improvement in macroeconomic management – which led to macroeconomic stability, increased domestic and foreign investment and international trade – there has been a large and unprecedented demand for Africa's natural resources from the emerging market economies. Moreover, the continent now has a sizeable middle class, about 300 million people, who are significantly affecting the consumption and investment patterns. Furthermore, following a

[1] A previous version of the paper was originally prepared at the request of the ADF Working Group for discussion during the third meeting of the Working Group that took place in London on 25 February, 2015. This updated version of the paper responds to various requests by Deputies at the London meeting as well as related updates.

decade of rapid growth and improved macroeconomic management, a number of the Bank's low-income RMCs are now slowly but progressively climbing up the income ladder and diversifying their sources of financing. These include increased foreign direct investment (from USD 12 billion in 2000 to USD 57.24 billion in 2013) and remittances (from USD 10 billion in 2000 to USD 61 billion in 2013) but also more access to the capital markets. As a result, although ODA continues to play a significant role, it is no longer a major source of financing for many African countries (Figure 1). Perhaps most prominent is the recent cohort of countries engaged in first time sovereign bond issuances as well as the coupons on those issuances (Annex I). RMCs are also accessing foreign direct investments (FDI) and steadily increasing domestic revenues.

Figure 1: Volume of External Flows to Africa (1980-2013)

Current prices, USD billion



Source: OCDE for ODA; UNCTAD for FDI; World Bank for remittances

2.3. According to our projections, Africa is set to continue its resilience in the face of slow recovery of the global economy. As shown in Table 1, the continent as a whole and sub-Saharan Africa (SSA) in particular, are projected to achieve economic growth rates of above 4% for at least the next ten years. Among other things, this will result in an increased number of current ADF countries exceeding the GNI per capita income threshold and thus changing to the gap classification status as explained later in Section 3.

2.4. In part because of the robust economic performance across the continent, Africa has also realized progress in key areas of social development. In the past decade, child mortality rates, HIV infections, and malaria deaths have all fallen sharply. Likewise poverty rates have also decreased across the continent. These outcomes have had a positive impact on average life expectancy, which rose by about 10% to reach fifty-five (55) years – an increase of seven (7) years compared to the early 2000s.

Table 1: Real Economic Growth Rate

(Percentage)

Region	2005	2010	2015 (estimation)	2020 (projection)	2025 (projection)
Sub-Saharan Africa	5.9	5.0	5.7	4.1	4.1
Africa	5.9	5.0	5.7	4.4	4.3

Source: African Economic Outlook for 2005, 2010 and 2015; staff projections for 2020 and 2025

Socioeconomic Challenges

2.5. Despite Africa's economic growth achievements, the continent still faces numerous socioeconomic constraints standing in the way of more inclusive growth. As measured by the Millennium Development Goals (MDGs), Africa's performance on the individual wellbeing of its inhabitants contrasts sharply with much of the existing glowing image that emphasizes economic growth. Indeed, since 2000, the continent has lagged behind the rest of the world on MDG progress, particularly in terms of poverty reduction, job creation and food security. The continent also exhibits a greater degree of inequality as six (6) of the world's ten (10) most unequal countries in recent years are in Africa (Namibia, South Africa, Lesotho, Botswana, Sierra Leone and Central African Republic).

2.6. Even as poverty rates have declined in recent years, nearly 50% of the population (corresponding to more than 450 million people) in SSA today lives on less than USD 1.25 a day, which represents the highest rate of extreme poverty in the world. Assuming a poverty head count of USD 2.50 a day, this would increase to 75.7% (corresponding to 743.8 million of people). The World Bank's 2014 Global Monitoring Report estimates that SSA is in fact, home to 41% of today's global poor, a share that could reach 81% by 2030 under a business-as-usual scenario.[2] This stark concentration of global poverty demands a focused response from African governments and its development partners, particularly as Africa's population is set to double to close to 2.3 billion people by 2050, due in large part, to improved health care. By then, about 43% of Africa's population will be under the age of 25, while the share of the 15-24 age cohorts will be the largest.

2.7. To be sure, there are numerous other risks and challenges that threaten the sustainability of Africa's recent growth experience, including: the lack of diversified economies, poor or underfunded infrastructure, over-dependence on natural resource rents for certain countries, unanticipated shocks such as pandemics, political instability and poor governance in some countries, and massive unemployment and under-employment, particularly among the continent's large youth population and low income countries. Although commendable progress has been achieved, long term debt sustainability remains also a key challenge as many African countries have a narrow export base limited to a few commodities, and therefore highly susceptible to shocks, including droughts and commodity price volatility (Annex II).

3. ADF Graduation Process and Projections for Graduation through 2022

ADF Graduation

3.1. ADF eligibility is based on two criteria: (a) per capita income (GNI) below a certain threshold (currently USD 1,215 for fiscal year 2014-2015)[3] and (b) the absence of credit-worthiness that prevents an RMC borrowing from the AfDB's non-concessional window. There are currently forty (40) countries that are ADF eligible as summarized in Table 2.

3.2. Because ADF countries have grown increasingly diverse in terms of their incomes, economic structures, natural resource bases, inequality and socio-economic development, the Fund changed the way it supports its RMCs during the negotiations for ADF13. ADF Governors agreed that ADF resources would continue to be channeled to the poorest RMCs and endorsed new country groupings and differentiated hardened financing terms (Annex III).

Creditworthiness and the Bank's Credit Policy

3.3. The amendment of the Credit Policy approved in May 2014 aims to assist low-income ADF RMCs, which have low or moderate risk of debt distress, to gain access to ADB sovereign window on a case-by-case basis, to enable them meet their development objectives while maintaining a sustainable debt position. The amended policy sets out clearly the eligibility criteria ADF countries must meet before accessing resources from the ADB sovereign window. Further, access to the AfDB window is subject to the fulfilment of 4 criteria: (i) sustainable debt profile, with low or moderate risk of distress; (ii) level of financing determined on the basis of the country's headroom analysis (DSA) & the Bank's Operational Country Limit; (iii) Sustainable macroeconomic position as determined by Management; and (iv) a positive recommendation by the Bank's Credit Risk Committee (CRC). The Credit Policy also includes a set of actions that the Bank must take for implementation: i) Special risk assessment; ii) project selection that ensures economic viability; iii) partnership and working with the IMF, World Bank and rating

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2 See, World Bank. 2014. Ending Poverty and Sharing Prosperity – Global Monitoring Report 2014. Washington, DC: World Bank. http:// www.worldbank.org/content/dam/Worldbank/gmr/gmr2014 /GMR_2014Full_Report.pdf).

3 The threshold updated annually on the basis of the World Bank Atlas methodology.

agencies; iv) capacity building in RMCs through advice on debt management and internally to improve debt sustainability analysis; v) monitoring and evaluation; and vi) periodic review.

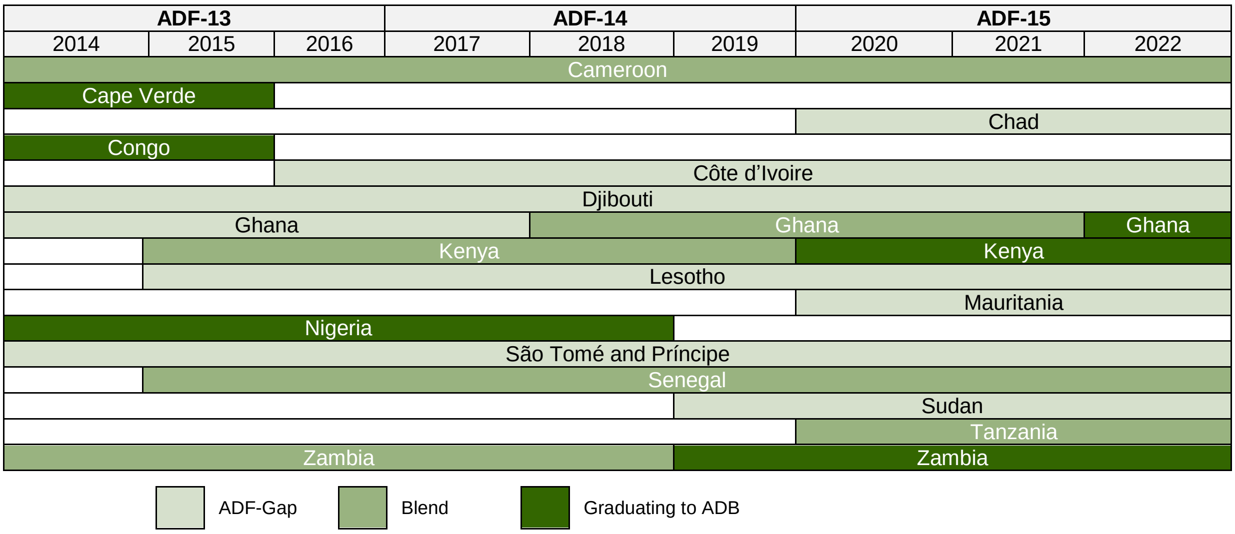
3.4. As of end December 2014, three (3) countries had been assessed, namely Rwanda, Uganda and Tanzania, and the respective special risk notes cleared by Credit Risk Committee (CRC). A road project in Rwanda (UA 50.4 million) and an agriculture project in Uganda (UA 57.5 million) were both approved by the Board in 2014 for financing from the ADB sovereign window. The positive diversification effect of extending non-concessional funding to creditworthy ADF RMCs via the amendment to the Credit Policy is expected to assume greater significance as additional high return public-sector projects are funded.

A Note on Methodology: Approach, Assumptions, Model, Scenarios and Results

3.5. Based on plausible assumptions and the best available data, we constructed a model for the 3rd ADF Working Group meeting in February 2015 to conduct various simulations based on the Bank's country credit classification and criteria (Annex IV). We used a set of criteria and assumptions which are uniform for all three ADF cycles (ADF-13, 14 and 15). For this version of the paper, we updated the consolidated graduation scenario based on two recent major developments namely the recently concluded credit assessment of Kenya (April 2015)[4]; and recent DSA published by the IMF[5].

3.6. Figure 2 and Table 3 present the results of our simulations vis-à-vis graduation. In sum: we project that by the end of the ADF-15 cycle (i.e., 2022) thirty-seven (37) countries will remain eligible to ADF. However, within these countries, seven (7) will potentially be classified as gap countries; three (3) as blend countries; and three (3) would be at different stages of graduation to the ADB category. Should this projected graduation scenario hold, it will represent a significant change as compared to (i) the beginning of ADF-12 (i.e., 2011) when thirty-seven (37) out of the forty-one (41) countries eligible to the Fund were ADF-only, or (ii) May 2015, when forty (40) countries are eligible to the ADF; thirty-one (31) are ADF-only, three (3) are graduating to the ADB category, two (2) are blend and four (4) are ADF gap countries.

Figure 2: ADF Countries' Ongoing Graduation and Graduation Projections Trend (ADF-13-14-15)



Note: Ghana, which is currently experiencing macroeconomic challenges, was recently classified as country in risk of debt distress. Therefore, the potential graduation of Ghana to the blend category is projected at best by 2018.

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[4] As Senegal credit assessment will be conducted in May-June, we maintained the country's projection to be graduated to the blend category in 2015.

[5] IMF, DSA list as of April 02, 2015 (https://www.imf.org/external/pubs/ft/dsa/lic.aspx).

Table 2: Current Classification as of May 2015

ADB countries (14)	ADF-eligible countries (40)				
	ADF-Gap# (4)	Blend^ (2)	Graduating to ADB (3)	ADF-only (31)	
Algeria	Djibouti	Cameroun	Cape Verde	Benin	Malawi
Angola	Ghana	Zambia	Congo	Burkina Faso	Mali*
Botswana	Lesotho		Nigeria	Burundi*	Mauritania
Egypt	São Tomé & Príncipe			Central African Rep.*	Mozambique
Equatorial Guinea				Chad*	Niger
Gabon				Comoros*	Rwanda
Libya				Congo DRC*	Senegal
Mauritius				Côte d'Ivoire*	Sierra Leone*
Morocco				Eritrea*	Somalia*
Namibia				Ethiopia	South Sudan*
Seychelles				Gambia	Sudan*
South Africa				Guinea*	Tanzania
Swaziland				Guinea-Bissau*	Togo*
Tunisia				Kenya	Uganda
				Liberia*	Zimbabwe*
				Madagascar*	

* *Fragile and conflict affected state, according to the harmonized list AfDB/WB.*

\# *Gap countries are ADF countries which GNI per capita has been above the operational cut-off for more than two years.*

^ *Blend countries are creditworthiness (generally measured by low debt ratios, fiscal balance position and sound financial sector) but with low GNI per capita.*

Table 3: Projected Classification by the End of ADF-15

ADB countries (17)	ADF-eligible countries (37)				
	ADF-Gap (7)	Blend (3)	Graduating to ADB (3)	ADF-only (24)	
Algeria	Chad	Cameroun	Ghana	Benin	Rwanda
Angola	Côte d'Ivoire	Senegal	Kenya	Burkina Faso	Sierra Leone
Botswana	Djibouti	Tanzania	Zambia	Burundi	Somalia
Cape Verde	Lesotho			Central African Rep.	South Sudan
Congo	Mauritania			Comoros	Togo
Egypt	São Tomé & Príncipe			Congo DRC	Uganda
Equatorial Guinea	Sudan			Eritrea	Zimbabwe
Gabon				Ethiopia	
Libya				Gambia	
Mauritius				Guinea	
Morocco				Guinea-Bissau	
Nigeria				Liberia	
Namibia				Madagascar	
Seychelles				Malawi	
South Africa				Mali	
Swaziland				Mozambique	
Tunisia				Niger	

4. Implications of Graduation for the Bank and its Clients

4.1. Graduation will have various implications on ADF's (and in turn, the entire AfDB) relationship with its clients and the countries projected to change credit status, i.e. Ghana, Kenya, Senegal, Tanzania and Zambia.

4.2. However, loss of eligibility to the ADF has implications well beyond the Fund itself as it is also a signaling mechanism for concessional funds and debt restructuring terms by other multilateral and bilateral institutions, several of whom use it as an informal proxy in their attempts to best target their aid resources.

Gradual Shift from the ADF

4.3. As the projected countries graduate from the ADF will eventually cease to have access to the ADF's highly concessional resources, they will most likely be eligible for ADB lending, under different loan and financing terms. Since the thresholds for eligibility are almost identical, loss of ADF funds is likely to also deprive graduating countries of access to concessional lending from the World Bank's IDA. And given that eligibility for the IMF's concessional financing is closely tied to IDA income thresholds, then the three (3) projected graduating ADF countries will potentially become ineligible for the IMF's Poverty Reduction and Growth Trust (PRGT) funds.

4.4. The move towards greater use of non-concessionary resources by graduating and blend RMCs will require that the Bank invest more effort in working with the respective countries along with other development partners on debt management capacity improvements as well as on the related issue of diversifying export bases of these RMCs. The need to closely monitor debt in RMCs is also critical as private capital flows to the continent are growing rapidly and many RMCs are accessing more and more the capital markets. This is particularly important as countries which already graduated or that will graduate in the coming ten (10) years from the ADF category will face steeper borrowing costs. Similarly, as private capital is highly volatile – as the supply is driven by global economic and even, geopolitical conditions that have little to do with local or regional markets in Africa – it can very quickly flee from the continent and lead to resource shortage for financing development.

4.5. The gradual shift away from concessional resources also implies that the Bank should redouble its efforts in assisting RMCs with improved domestic resource mobilization especially those set to graduate and face challenges to raise tax revenues. As a consequence, they remain vulnerable to external shocks and are highly dependent on external sources of financing for their development programs. The Bank will need to work with its partners as well as with governments in RMCs supporting efforts to (i) broaden the tax base, (ii) formalize the economies of RMCs most of which have huge shadow economies; and (iii) reform tax administration capacity.

4.6. Meanwhile, it is conceivable that as bilateral aid from the traditional donors falls, there will be growing interest from emerging donors. Many of these emerging donors' aid programs, for example that of China, tend to be more associated with commercial opportunities that are more numerous at a higher income level.

ADF Client Base to Increasingly Comprise of Fragile States

4.7. Given that the composition of ADF eligible countries will not change significantly by 2022, the demand for ADF resources is unlikely to drop. Some thirty-one (31) countries will remain ADF, compared to thirty-five (35) currently. However, within this category, the number of countries considered as fragile or conflict affected states is likely to remain the same as of today, i.e. eighteen (18). Consequently, as more and more RMCs graduate to middle income status, this will result in an increased proportion of fragile states among ADF countries (from 51% as of today to 60% for ADF-15).

4.8. The immediate result of the change in ADF countries profile is an increased share of ADF resources going to fragile or conflict-affected RMCs. For instance, the share of resources allocated to fragile states increased from 16.5% during ADF-12 to UA 28.9% during ADF-13. According to our projections, this progression will continue from ADF-14 onwards as non-fragile states graduate (Table 4 and Annex V.D).

4.9. The increased number of fragile or conflict affected countries among the group of ADF countries also raises questions about the adaptability of the current ADF allocation model and maintaining the various 'set asides'. Indeed, adjustments to the current PBA model will be needed as countries graduate, mostly to take into account the strategic orientations of the Fund in addressing the needs of ADF RMCs.

4.10. As part of the ADF-13 replenishment discussions, the possibility of introducing a fragility index in the PBA system was one of the options presented but not retained. Since ADF eligible countries will be increasingly fragile or post conflict, the PBA system could be adjusted to incorporate a fragility index. The pillars in the current Transition Support Facility (TSF) might have to be revisited, particularly Pillar I. Alternatively, the resource allocation model could be adjusted to ensure that more resources are channeled for countries with higher needs. These adjustments to the PBA model could be introduced after an assessment and lessons have been learnt from the recent inclusion of the Africa Infrastructure Development Index (AIDI) as part of the needs component in the PBA formula during ADF-13.

4.11. Another consideration may involve strengthening the existing Project Preparation Facility (PPF) by increasing its resources and scope to cover risks.[6] Specifically, the PPF and the various existing risk mitigation instruments (the PSF, the PRG and the PCG) could together form a package of products to ensure that selected infrastructure or private sector projects are fully bankable. Capacity building or specialized technical assistance may also be envisaged for beneficiaries, including companies or national entities in fragile or conflict affected states involved in particular projects.

4.12. In addition, in order to avoid the risk of having countries under this category graduating to another credit category while they are still facing structural vulnerabilities, adjustments to the current transition period of five (5) to say, seven (7) years might be necessary (Annex VII).

Increased Allocations for Remaining Eligible Countries on Present Trends

4.13. In order to determine the likely impact of the projected graduation scenario on countries' allocations, we conducted simulations based on the inputs used for the computation of the PBA for 2015.[7] As presented in Annex V.A, the share of PBA resources going to ADF-only countries is likely to decrease by 2022 as compared to 2014 and 2015. This is normal since the number of countries changing credit status (from ADF-only to blend or graduating) or that will become gap is expected to increase (Annex V.A). However, as the number of ADF-only countries will decrease from 31 to 24 during the same period, the average of PBA allocations per ADF-only country is projected to increase from UA 30 in 2015 to UA 34 in 2022 (Annex V.C). In the meantime, the average PBA allocation per capita is projected to increase among ADF-only countries during the same period (2015: UA 1.88; 2022: UA 2.39). Finally, the share of resources allocated to countries facing fragility or conflict situation is projected to increase from 16.5% for ADF-12 to 35.8% under ADF-15 (Annex V.D). In nominal terms, this represents UA +513.7 million that will be allocated to the sixteen (16) eligible transition states benefiting from the TSF Pillar I resources.

Table 4: PBA Estimates per Category of Countries

Country category	ADF-12		ADF-13		ADF-14		ADF-15	
	UA MM	%	UA MM	%	UA MM	%	UA MM	%
Gap, Blend, Transition	248.12	6.6%	551.76	17.8%	536.88	17.0%	725.63	23.0%
Gap	*22.10*	*0.6%*	*251.91*	*8.1%*	*236.47*	*7.5%*	*327.78*	*10.4%*
Blend	*194.40*	*5.2%*	*169.53*	*5.5%*	*260.71*	*8.3%*	*269.95*	*8.5%*
Transition	*31.63*	*0.8%*	*130.32*	*4.2%*	*39.70*	*1.3%*	*127.90*	*4.0%*
ADF-Only	3488.71	93.4%	2540.63	82.2%	2613.35	83.0%	2434.14	77.0%
Total	**3736.83**	**100.0%**	**3092.39**	**100.0%**	**3150.23**	**100.0%**	**3159.76**	**100.0%**
Fragile States	617.20	16.5%	892.92	28.9%	994.50	31.6%	1130.91	35.8%
Non Fragile States	3119.64	83.5%	2199.47	71.1%	2155.74	68.4%	2028.85	64.2%
Total	**3736.83**	**100.0%**	**3092.39**	**100.0%**	**3150.23**	**100.0%**	**3159.76**	**100.0%**

Source: Staff computations.

4.14. The impact of the projected graduation scenario on ADF eligible countries' PBA is presented in Annex VI. Except for ten countries that benefit from the minimum allocation, all ADF-only countries will see an increase in their PBA in 2022 as compared to 2015, ranging from a minimum of UA +1.1 million (Sudan) to a maximum of UA +24 million (Uganda). Out of the

[6] The PPF was established in 2000 (ADF-8) as a revolving fund (UA 19.2 million) to enhance the quality of the preparation of projects and provide an effective mechanism for prompt response to the project preparatory needs of the Fund's eligible countries. In 2013, Management revised the PPF's guidelines in order to allow an increase in the PPF advances, which now vary from UA 200,000 to a maximum of UA 1,000,000.

[7] These inputs are: CPIA scores, country portfolio performance assessment (PPA) ratings, GNI per capita, population, DSA, and AIDI. The same PBA envelope (UA 1,089.9 million per year) was considered.

current forty (40) ADF eligible countries, seventeen (17) countries will see their PBA increased by more than 25% if the projected graduation scenario is confirmed. The number of countries whose PBA will decrease is eight (8), all of which are countries graduating or that will graduate to the blend and ADB categories by 2022.

4.15. However, these gains may be undermined by overall ODA reductions as countries are graduating. This is because most ODA is focused on either the neediest countries or those with significant strategic interests and any graduation from ADF funding would most likely signal reductions of ODA funds over time. Given the ongoing fiscal austerity in many traditional donor capitals, graduation from the ADF will make defending continued allocations to affected countries, more politically arduous.

Speedier Repayment of Existing Debt and Termination of Debt Relief

4.16. Any country graduating out of the ADF not only ceases to receive funds from the ADF, but it may be required to pay off its existing debt at a faster rate. As part of ADF-13, a Voluntary Loan Prepayment (VLP) was also adopted to complement the Accelerated Payment Clause (APC). The VLP both enables and encourages the prepayment of ADF loans that do not currently contain an acceleration clause. The VLP allows the ADF to offer financial incentives to countries that have graduated, on a case-by-case basis, in the form of discounts on the prepayment of loans from the Fund.

4.17. Eligibility for certain debt relief and debt restructuring initiatives and institutions is tied only to ADF-eligible countries. For example, the Heavily Indebted Poor Countries (HIPC) Initiative and the Multilateral Debt Relief Initiative (MDRI), restrict debt relief to countries below operational cutoff of the World Bank's IDA-which is essentially, the same as the operational cutoff for the ADF. The "IDA-only" eligibility yardstick also applies to the Paris Club of bilateral creditors when it comes to concessional relief. Of the countries we project to either graduate from the ADF by ADF-15 or from ADF-only to 'blend', only Cameroun, Congo, Ghana, Senegal, Tanzania and Zambia have already benefitted from both HIPC and MDRI. They have received total debt relief from the AfDB Group of USD 579.4 million and USD 1,819.9 million, respectively. Whereas none of the projected countries set to graduate are under debt distress at the moment, they will be ineligible for future debt relief on the concessional terms that are conditional on ADF/IDA eligibility.

Addressing Pockets of Poor Populations in RMCs

4.18. Even the simplest projections suggest the continuing prevalence of mass-scale poverty across the continent over the next decade, including in countries set to graduate from the ADF. Tables 5 and 6 give a hint of what the new geography of poverty on the continent will look like in 2022 as compared to 2015. And based on projected population estimates from the UN, summarized in Table 7, we are talking about several hundred million people that will still be living in poverty within the countries that have already graduated or that are set to graduate to the ADB category by 2022. This is especially true for Nigeria given its size. Meanwhile the population of these countries is expected to continue to grow, rising by over 15% between now and the end of the ADF 15 cycle. Population growth alone is expected to further increase the poor population in ADF countries.

Table 5: Current and Projected Poverty Aggregates in Africa: 2015 vs. 2022

(USD 1.25/day poverty line)

Category	2015			2022		
	Total Pop. (million)	Headcount (%)	Headcount (Nominal)	Total Pop. (million)	Headcount (%)	Headcount (Nominal)
Africa	1,164.5	39.3	457.4	1,371.3	42.9	588.3
SSA	987.7	46.0	454.7	1,177.3	48.1	566.2
ADF countries	612.4	46.3	283.3	639.8	41.3	264.0
Blend and Graduating Countries	289.3	53.5	154.7	215.3	35.5	76.4

Source: United Nations, Department of Economic and Social Affairs, Population Division (2013). World Population

Prospects: The 2012 Revision, DVD Edition ; AfDB projections for headcount poverty line.

Table 6: Current and Projected Poverty Aggregates in Africa: 2015 vs. 2022

(USD 2.5/day poverty line)

Category	2015			2022		
	Total Pop. (million)	Headcount (%)	Headcount (Nominal)	Total Pop. (million)	Headcount (%)	Headcount (Nominal)
Africa	1,164.5	68.3	785.7	1,371.3	68.3	936.6
SSA	987.7	75.7	743.8	1,177.3	75.7	890.7
ADF countries (including Gap)	612.4	76.2	465.4	639.8	76.2	487.2
Blend and Graduating Countries	289.3	74.0	238.6	215.3	74.0	159.3

Source: United Nations, Department of Economic and Social Affairs, Population Division (2013). World Population Prospects: The 2012 Revision, DVD Edition ; AfDB projections for headcount poverty line.

Table 7: Total Population for 2015-2022 (million), Selected Countries

Country	2015	2016	2017	2018	2019	2020	2021	2022
WORLD	7,324.8	7,405.0	7,484.3	7,562.8	7,640.2	7,716.7	7,792.2	7,866.6
AFRICA	1,164.5	1,194.6	1,223.4	1,252.6	1,282.2	1,312.1	1,342.5	1,371.3
SSA	987.7	974.0	999.3	1,024.9	1,051.0	1,077.6	1,104.6	1,177.3
Congo	*4.7*	*4.8*	*4.9*	*5.0*	*5.1*	*5.3*	*5.4*	*5.5*
Kenya	*46.7*	*48.0*	*49.2*	*50.4*	*51.7*	*52.9*	*54.2*	*55.5*
Ghana	*27.0*	*27.5*	*28.1*	*28.6*	*29.2*	*29.7*	*30.3*	*30.9*
Nigeria	*183.5*	*188.6*	*193.8*	*199.2*	*204.6*	*210.2*	*215.8*	*221.7*
Zambia	*15.5*	*16.0*	*16.6*	*17.1*	*17.7*	*18.3*	*18.8*	*19.5*

Source: United Nations, Department of Economic and Social Affairs, Population Division (2013). World Population Prospects: The 2012 Revision, DVD Edition.

4.19. The persistence of pockets of poverty in RMCs will require special attention from the Bank and other development partners. As part of the ongoing debates under the Sustainable Development Goals (SDGs) post-2015 agenda, there is a shared consensus among all stakeholders that ODA will remain critical for reducing poverty and achieving sustainable economic growth, notably in Africa where the challenges are the most important.

4.20. While increasing financing for development is important, reforming the current existing instruments is also critical. As other multilateral development banks have done, the Bank may consider adding to the PBA formula a poverty index to monitor ADF countries' improvements in per capita GNI alongside reductions in poverty pockets. Another option would be to create a dedicated separated transition facility dealing with the issue of pockets of poverty and that will support those countries graduating from the ADF category. These measures may be combined with a revision of the current Credit Policy and the Transition Framework for Changing Credit Status (Annex VII) by considering a higher per capita GNI threshold than the one of IDA and an extended transition period, say from five (5) to seven (7) years. This will avoid countries graduating from the ADF category while a significant proportion of their population in poverty remains high.

Need to Rationalize the Role of the ADF in the Changing Aid Architecture

4.21. As countries graduate out of the ADF, and by definition, out of IDA, the latter is set to become overwhelmingly African. The clear implication of that is that any current distinctions between the two sister institutions will begin to fade. Already, the old model of cooperation where the ADF mostly co-financed IDA-prepared projects has long disappeared. The current justification for having both an IDA and an ADF is that they each bring special strengths, with the former as a global institution and the latter as an African one with particular regional expertise. Moreover, in recent years, particularly with the adoption of its Ten Strategy 2013-2022, the Bank has largely focused its portfolio on its comparative advantage in infrastructure while at the same time purposefully pulling out from certain areas such as health and education, where its other development partners are perceived to have a comparative advantage.

4.22. The change in ADF clients profile will also coincide with at least four major changes impacting the aid architecture and ADF donors. First, the absolute number of poor (living on less than USD 2.50 a day) in Africa will increase, making it the number one continent in the world in terms of number of poor people, i.e. close to 1 billion. Second, Africa will also be the only continent with a significant number of countries relying on concessional aid as a main source of financing for development. Third, the emergence of non-traditional donors (e.g. New Development Bank, philanthropic, foundations, etc.) is not only set to diversify the type and volume of financial instruments, but is also likely to impact the very business and operating models of aid. Four, the merging of the two financing windows of the Asian Development Bank (AsDB) and the change in IDA client base by 2025 may result in increased donor focus in Africa.

5. Conclusion

5.1. A number of ADF-eligible RMCs of the AfDB are likely to either graduate outright from the Fund, or transition towards 'blend' status. This will have implications—both positive and potentially negative—for the Fund (and the Bank) and their relationship with this sub-set of countries, the rest of the RMCs, peer institutions such as IDA, and several other stakeholders.

5.2. This anticipated graduation of some RMCs will leave the ADF client base dominated by countries in fragile situations or conflict affected countries. The demand for ADF resources is therefore unlikely to drop dramatically—something that underscores the continuing relevance for concessional resources. Likewise, the development of tailor-made mechanisms to address the varying needs of countries will be important and the AfDB will have to continue adjusting to a changing international environment and to take steps to ensure the sustainability and resilience of its concessional window. Adjustments, such the Bank's Credit Policy are aimed at taking into consideration the new profiles of ADF countries, while still remaining cognizant of the prevailing vulnerability and possibility of relapse by some countries. Several RMCs are already benefitting from the amendments to the Credit policy.

5.3. The major changes in the aid architecture as well as the recent and forthcoming graduations from the World Bank's IDA – more than 80% of its clients will be in Africa by 2025 – will impact the relationship between IDA and ADF. The developments call for even greater cooperation and coordination between the two than has ever been the case, in order to benefit from synergies and avoid duplication. A division of labor would be helpful, if it is agreed upon, to improve efficiency and help to differentiate these two separate windows which are both funded by sovereign donors. To achieve the AfDB's twin objectives of inclusive growth and transitioning to green growth, the ADF's focus could be on infrastructure development, regional integration, private sector development, governance and accountability, skills and technology. The ADF could also consider greater emphasis on countries in fragile situations.

5.4. As concessional financing cannot be viewed in isolation, it will be critical to examine other sources of finance on the continent including the provision of additional support for domestic resource mobilization and the strengthening of regulatory environments to enhance the business climate and reduce corruption. The evolving global financial architecture in which both IDA and the ADF will have a similar clientele calls for enhanced dialogue and synergies in the mobilization and implementation of concessional financing.

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Annex I: Recent Bond Issues in Africa, Select Countries

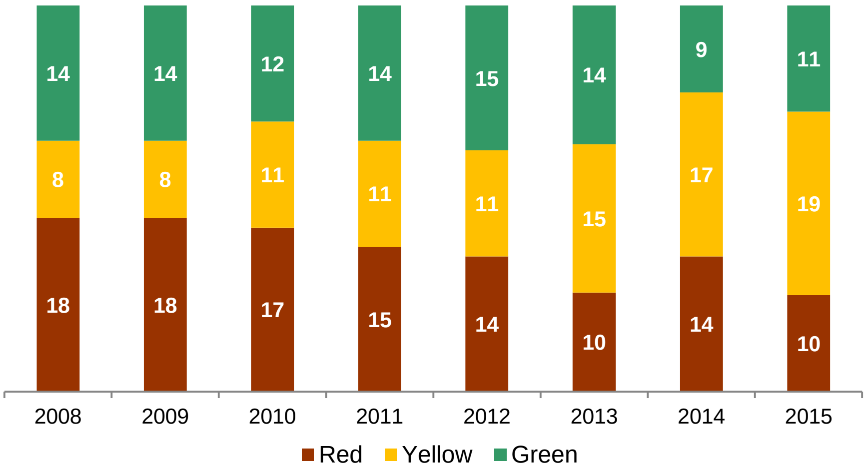
Country	Year	Value (USD million)	Use
Gabon	2007	1,000	Debt restructuring (buy back at a discount of 15% the country's outstanding debt to Paris Club creditors).
	2013	1,500	USD 610 million to replace existing debt for better debt management.
Ghana	2007	750	Fund several projects, mainly in energy and transport.[8]
	2013	750	For capital expenditure and refinancing public debt to reduce the cost of borrowing
Cote d'Ivoire	2010	2800	Debt restructuring in the context of the HIPC Initiative - Issued bonds in exchange for defaulted bonds they had issued before, as part of commercial debt restructuring.
	2014	750	Used to finance public investment, especially in areas such as healthcare and education
	2015	1,000	Used for financing the Country's National Development Plan (NDP) which focuses on infrastructure, improving education and healthcare and reducing poverty
Ethiopia	2014	1,000	To invest in infrastructure, notably the Renaissance Dam
Kenya	2014	2,000	Financing iinfrastructure projects and repayment of a $600 million loan that matured in August 2014.
Namibia	2011[9]	500	Diversify the source of financing and promoting employment and economic growth.
Nigeria	2011	500	Ensuring Nigeria's presence in the international market, (2) helping to attract foreign direct investment by increasing information disclosure, and (3) providing a benchmark for sovereign, subnational, and corporate issuances.
	2013	1,000	To finance projects in the electricity sector, which is undergoing privatization; to support the shift from domestic borrowing towards cheaper foreign credit?
Rwanda	2013	400	Construction of a 28-megawatt hydropower plant, the construction of a hotel and payment of some of state-owned RwandAir's debt.
Senegal	2009	200	To finance energy and road projects.
	2011	500	To finance energy and road projects.
	2014	500	Construction of a major highway and the upgrading and repairs of the country's energy infrastructure.
South Africa	2013	2,000	Extend maturity of debt, use low financing costs, finance roads and power.
Tanzania	2013	600	Test Market Appetite: This issuance by private placement allowed Tanzanian authorities to gauge potential demand and pricing ahead of the Eurobond issuance initially planned for the end of fiscal year 2013/14. This was postponed to 2015. The proceeds were intended to be used for building roads, boost power generation and refurbish the nation's railways.
Zambia	2012	750	Promoting infrastructure development (energy, roads and railways) and the social sector (health and education).
Seychelles	2006	200	Debt restructuring (clearing arrears to multilateral and commercial creditors).

[8] Source: IMF at http://www.imf.org/external/pubs/ft/dp/2014/afr1402.pdf
[9] Source: Standard and Poor's at http://www.standardandpoors.com/spf/upload/Ratings_EMEA/2013-05-06_TheGrowingAllureOfEurobonds.pdf

Annex II: Debt Sustainability Challenges in ADF-eligible Countries

Following the launch of the Heavily Indebted Poor Countries Initiative (HIPC initiative) in 1996, and the Multilateral Debt Relief Initiative (MDRI) in 2007, debt burdens of beneficiary countries were substantially lowered resulting in marked improvements in solvency. In addition, as part of the HIPC and MDRI initiatives, the Debt Sustainability Framework (DSF) was developed to support the Low Income Countries' (LIC) efforts to achieve their development goals without creating future debt problems. The most recent debt sustainability analysis[10] (IMF, April 2015) indicates that the risk of external debt distress is low or moderate for most of African LIC. The number of countries classified as "high risk to debt distress" dropped from 18 in 2008 to 10 in 2015.

Figure II-1: Countries by DSA Traffic Light Classification (2008-2015)



Source: IMF; AfDB for Eritrea, Somalia and South Sudan for 2014 and 2015

While the risk of external debt distress appears manageable, the trend in debt accumulation by some beneficiaries of debt relief is worrying and is already threatening to wipe all the gains made by the debt relief. Long term debt sustainability remains a key challenge as many sub-Saharan (SSA) countries remain vulnerable to external shocks.

The risk of falling again in debt burden could also result from too optimistic growth prospect scenarios based on the revision of the GDP. The recent revisions to GDP that have increased the size of some economies like Nigeria, Ghana and Kenya have helped lower debt-to-GDP ratios. As more countries revise their GDP's, it is expected that debt distress will be lower. However, the revisions may also give the countries an opportunity to start accumulating more debt.

Robust economic growth is not sufficient to ensure debt sustainability if not accompanied by sound macroeconomic policies. The recently downgraded credit rating of Ghana and Zambia by Fitch due to their high deficit levels reflects this risk. Going to the market with low credit ratings increases the cost of debt as higher risks are incorporated in the prices.

In addition, recent trends and developments indicate that external push factors are becoming less favourable to countries in SSA. First, global interest rates are projected to increase following the tapering in the United States, meaning that countries will have to allocate larger proportions of their budgets toward paying interest, while paying off less of their debt. Second, risk appetites of foreign investors, may fall when global interest rates increase and growth rates decline. Third, the price of crude oil has fallen significantly to about $60. As a result, SSA countries will face a higher cost of borrowing as their revenue projections decline worsening economic performance.

[10] Debt Sustainability Analysis is conducted regularly by the IMF/World Bank to determine country's level of risk of debt distress. Countries are classified by a 'traffic light' system: red - high risk of debt distress; yellow - moderate risk of debt distress; and green - low risk of debt distress.

Annex III: Country Differentiation and Lending Terms for ADF Loans

ADF countries currently fall into one of two sub-groups ("Regular" and "Advance" ADF-only countries) based on their per capita GNI. RMCs with a per capita GNI above the average of all ADF-only countries are included in the "Advance" group, and all RMCs with a GNI per capita below the average are in the "Regular" group. Second, differentiated ADF loan financing terms are now applied between regular and advance ADF-only countries, and blend, gap and graduating countries starting ADF-13.

ADF countries with per capita income below the threshold enjoy the most concessional borrowing terms, with 40-year maturity, 10-year grace period, and service charges of only 0.75%. ADF countries with a high-risk of debt distress receive only grants, those with medium risk receive half grants and half concessional loans, and those deemed with low risk receive loans on standard ADF terms.

Countries that are below the ADF operational cut-off but that are deemed creditworthy for limited ADB borrowing are eligible for ADF lending under slightly harder "blend" terms. Currently 2 countries fall in this category, and have access to both ADB and ADF financing.

Table III-1: Differentiated Financing Terms for ADF Loans

Country Classification		Maturity (Years)	Grace Period (Years)	Service charge (%)	Commitment Fee (%)	Interest rate (%)
ADF-Only	*Regular*	40	10	0.75	0.50	0
	Advance	40	5	0.75	0.50	0
Blend, gap and graduating		30	5	0.75	0.50	1%

Annex IV: Methodological Note for the Graduation Forecasting Model

As part of the documents presented during the third meeting of the ADF 14 WG and to project which countries will graduate from ADF to the Blend and ADB categories during the ADF-13, 14 and 15 cycles, we constructed a model based on the Bank's Group country credit classification and a set of uniform criteria and assumptions, two main criteria were considered regarding the methodology and assumptions:

- The IDA gross national income per capita (GNI per capita) cut off, which estimated values are presented in table IV-1 below. Using the estimated GNI per capita operational cut off, we then determines which countries could potentially graduate from the ADF or would remain but become gap, by comparing GNI per capita projections based on the AEO and IMF World Economic Outlook (WEO) data for the period 2013-2022.

Table IV-1: Previous and Estimated IDA's GNI per Capita Threshold (2011-2022)

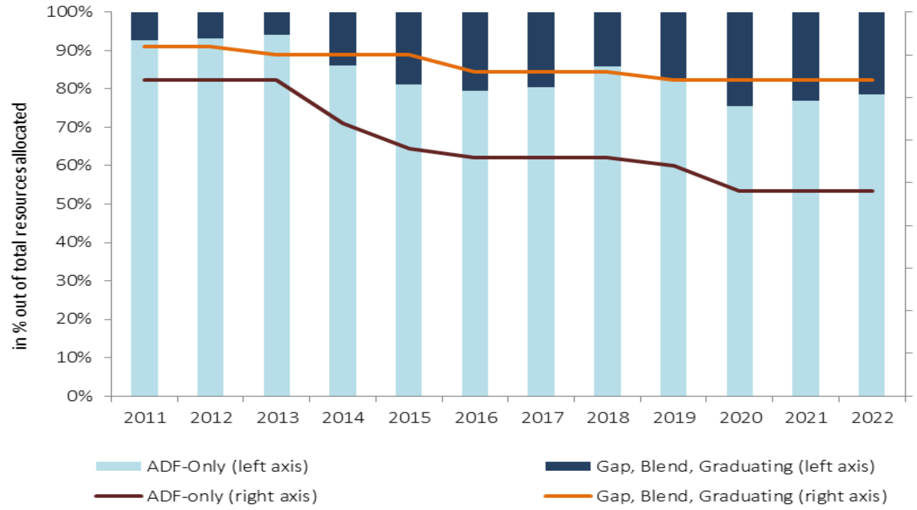
Previous Values					Estimated Values							
2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
1,165	1,175	1,195	1,205	1,215	1,240	1,265	1,290	1,315	1,340	1,365	1,390	1,415

- The extent to which a country is deemed creditworthy. The creditworthiness assessment methodology addresses factors that affect an independent government's long term willingness and ability to service its debt on time and in full. The model considers a combination of indicator as a proxy for the "formal" Bank creditworthiness assessment. The composite cumulative indicator (i.e. all four criteria must be met all the time during an ADF cycle for a country to graduate from ADF) combines four variables, to assess whether a country would graduate to the Blend category by ADF-13, ADF-14 or ADF-15:
    - General government gross debt as a percentage of GDP, as a proxy for total debt;
    - Total debt servicing as a percentage of total exports;
    - CPIA score for cluster "A" assessing economic management ($CPIA_A$). Based on the average CPIA ratings from 2004 to 2014, a linear trajectory going forward for all countries was assumed;
    - GNI per capita as a proxy of income level.

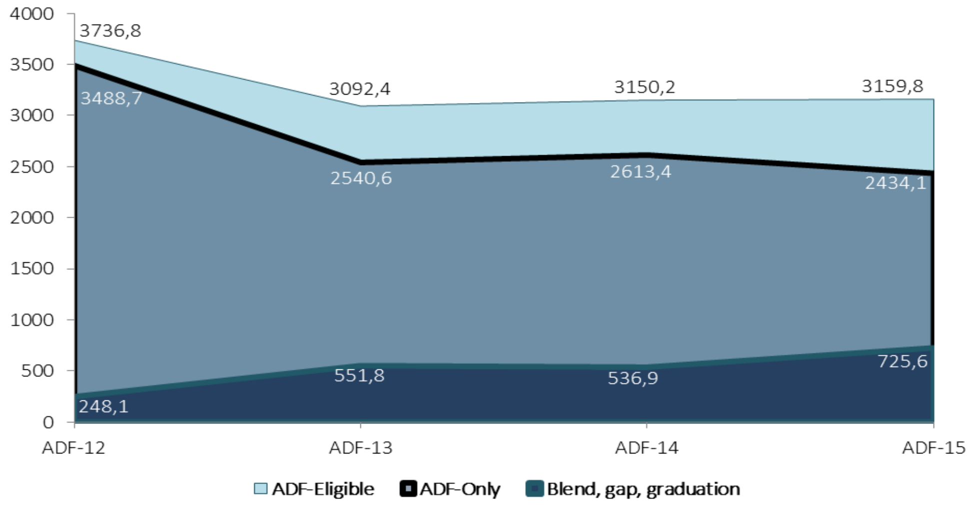
Based on the three scenarios considered (baseline, conservative and optimistic), a consolidated scenario was defined. In addition to the criteria above, recent developments such as the rebasing of the GDP of some countries, the historical performance in managing debt but and the most recent Debt Sustainability Analysis (DSA) of the IMF/World Bank were taken into account.

Annex V: Graduation Impact Estimates on Country Allocations

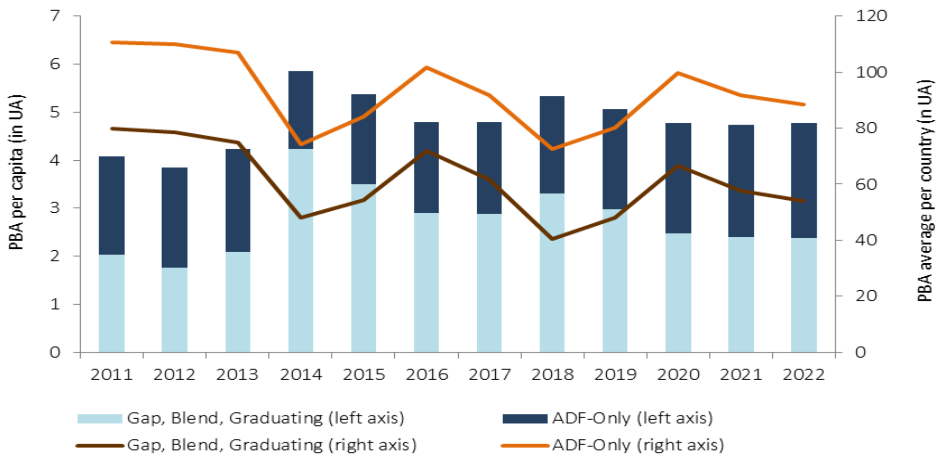
A. PBA Simulations per Country Category (2011-2022)



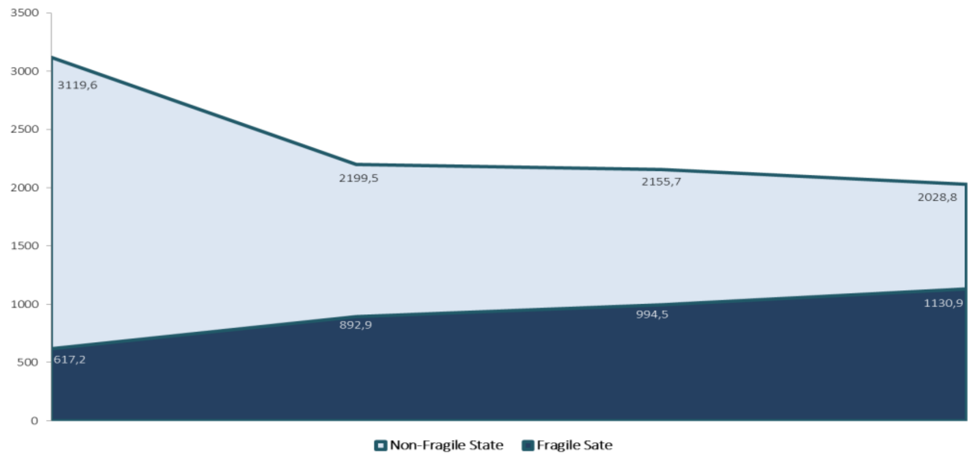
B. PBA Simulations per Country Category – ADF 12 to ADF 15



C. PBA Simulations – per Capita and Average per Country



D. PBA Simulations – Fragile States vs. non-Fragile States



Annex VI: Impact of the Projected Graduation on Countries' Performance Allocations

Country	Country Credit Category (2015)	Projected Country Credit Category (2022)	2015	2022	Nominal Variation	Variation in %
Benin	ADF-only	ADF-only	23.5	32.2	8.7	36.8
Burkina Faso	ADF-only	ADF-only	43.3	56.4	13.2	30.5
Burundi	ADF-only	ADF-only	15.8	20.2	4.3	27.5
Cameroon	Blend	Blend	14.9	17.8	2.9	19.4
Cape Verde	ADB-Graduating	ADB	0.2	0.0	-0.2	- 100.0
Central African Republic	ADF-only	ADF-only	5.0	5.0	0.0	-
Chad	ADF-only	ADF-Gap	9.9	19.5	9.7	98.2
Comoros	ADF-only	ADF-only	5.0	5.0	0.0	-
Congo DRC	ADF-only	ADF-only	111.8	110.1	-1.7	- 1.6
Congo, Rep. Of	ADB-Graduating	ADB	2.3	0.0	-2.3	- 100.0
Cote d'Ivoire	ADF-only	ADF-Gap	27.2	38.7	11.5	42.2
Djibouti	ADF-Gap	ADF-Gap	5.0	5.0	0.0	-
Eritrea	ADF-only	ADF-only	5.0	5.0	0.0	-
Ethiopia	ADF-only	ADF-only	113.8	114.5	0.8	0.7
Gambia	ADF-only	ADF-only	5.0	5.0	0.0	-
Ghana	ADF-Gap	ADB-Graduating	65.9	19.6	-46.3	- 70.3
Guinea	ADF-only	ADF-only	18.2	23.5	5.4	29.6
Guinea-Bissau	ADF-only	ADF-only	5.0	5.0	0.0	-
Kenya	ADF-only	ADB-Graduating	44.6	16.2	-28.4	- 63.7
Lesotho	ADF-Gap	ADF-Gap	5.0	5.4	0.4	8.6
Liberia	ADF-only	ADF-only	9.2	11.9	2.7	29.7
Madagascar	ADF-only	ADF-only	25.6	35.0	9.4	36.7
Malawi	ADF-only	ADF-only	28.1	36.4	8.3	29.6
Mali	ADF-only	ADF-only	22.8	32.4	9.6	42.2
Mauritania	ADF-only	ADF-Gap	5.0	5.0	0.0	-
Mozambique	ADF-only	ADF-only	38.2	51.3	13.1	34.1
Niger	ADF-only	ADF-only	49.6	64.0	14.4	28.9
Nigeria	ADB-Graduating	ADB	41.9	0.0	-41.9	- 100.0
Rwanda	ADF-only	ADF-only	58.0	74.6	16.5	28.5
Sao Tome & Principe	ADF-Gap	ADF-Gap	5.0	5.0	0.0	-
Senegal	ADF-only	Blend	10.5	12.2	1.6	15.6
Sierra Leone	ADF-only	ADF-only	9.8	13.0	3.2	32.8
Somalia	ADF-only	ADF-only	5.0	5.0	0.0	-
South Sudan	ADF-only	ADF-only	5.0	6.1	1.1	21.5
Sudan	ADF-only	ADF-Gap	22.6	33.3	10.7	47.5
Tanzania	ADF-only	Blend	114.6	47.0	-67.6	- 59.0
Togo	ADF-only	ADF-only	7.0	10.0	3.0	43.2
Uganda	ADF-only	ADF-only	75.7	99.7	24.0	31.7
Zambia	Blend	ADB-Graduating	6.8	1.5	-5.2	- 77.1
Zimbabwe	ADF-only	ADF-only	5.0	5.0	0.0	-

ADF-only ADF-Gap Blend ADB-Graduating ADB

Annex VII: Transition Framework – Criteria and Period for Changing Credit Status

The Bank Group has developed a framework to accompany RMCs changing credit status.[11] The framework recommends that for each country changing credit status, a transition program be drawn up, defining the modalities of Bank Group support (such as specialized analytical work, policy advice and dialogue, technical assistance) and the Bank Group's role in specific areas (for example, in the field of private sector development). The transition period of up to 5 years is meant to ensure a smooth, predictable and sustainable transition to their new borrowing status. This period also enables RMCs to continue to access concessional resources to address lingering issues of poverty and other socio-economic challenges on appropriate financing terms, before completely moving to the non-concessional window.

To smoothen the transition, a phasing out/phasing in period of an appropriate length is determined on the basis of objective criteria. For graduating RMCs, ADF resources are gradually phased out and ADB resources progressively phased in. The Transition Framework offers incentives for voluntary acceleration of graduation. Graduating RMCs that prefer more and faster access to ADB resources have the option to forego ADF resources in exchange for ADB resources. However, any acceleration of the graduation has to respect the objective of ensuring a smooth and sustainable transition for the country. However, the Bank would need to be much more engaged with such RCMs, interacting more regularly with policy makers and helping them to invest in facilities that improve their capacity to boost their resources, while at the same time monitoring closely to ensure they don't become debt laden.

Table VII-1: Criteria for Changing Credit Status

		Creditworthiness to Sustain ADB Financing	
		No	**Yes**
Per capita income above the ADF / IDA operational cut-off for more than 2 consecutive years	**No**	Countries below cut-off and not creditworthy: **ADF-only countries** on regular ADF terms	Countries below cut-off and creditworthy: **Blend countries** eligible for ADB resources and for ADF resources subject to a cap and blend terms
	Yes	Countries above cut-off but not creditworthy: **Gap countries** not eligible for ADB resources but eligible for ADF resources on blend terms	Countries above cut-off and creditworthy: Only eligible for ADB resources. Exceptionally, **graduating countries** are eligible for ADF resources on blend terms during a 2 to 5-year phasing-out period

Table VII-2: Criteria Guiding the Length of the Transition Period

Issue	Criteria	Cut-off	Duration
Initial transition length	-	-	2 years
Poverty and human development	Proportion of population living below the poverty line (USD 1.25 dollar / day) or Lowe relative level of human development Insular (i.e. island or landlocked)	Greater than 50% In bottom two quintiles of African countries on the Human Development Index	+ 1 year
Rate of economic growth	Average economic growth rate of the past five years	Lower than 10%	+ 1 year
Financial need / use of resources	Use of the previous ADF resources	More than 80%	+ 1 year
Final transition length	-	-	Potentially up to 5 years

[11] See, Transition Framework for Countries Changing Credit Status (ADF/BD/WP/2011/14/Rev.2)