

ADF-14

Resource Allocation Framework

Discussion Paper

ADF-14 Second Replenishment Meeting
June – July 2016
Abidjan, Cote d'Ivoire



AFRICAN DEVELOPMENT FUND

Executive Summary

This paper presents the framework for the allocation of the resources of the Fourteenth General Replenishment of the African Development Fund (ADF-14).

The current resource allocation framework has worked well and its reforms have been efficiently implemented during the Thirteenth General Replenishment of the African Development Fund (ADF-13). Management remains committed to allocating the overall majority of ADF resources through the Performance-Based Allocation (PBA) system, which has proven an effective mechanism for directing more resources to stronger performing countries since its adoption in 1999. However, Management believes there is a need to reinforce the current framework under ADF-14 to better serve the Fund's institutional characteristics and its client base within the following proposals:

- Management proposes to undertake the Country Policy and Institutional Assessment (CPIA) exercise every two years starting from ADF-14. This will allow for sufficient time to learn from each evaluation and to strengthen the resulting policy dialogue, given especially that the frequency of institutional and legal reforms and the time needed for their implementation in the various African countries usually takes at least two years.
- Management recommends keeping the flexible qualitative eligibility assessment for the Transition Support Facility (TSF) during the ADF-14 cycle as elaborated in the *“Role of the ADF-14 in Supporting Fragile Situations”* paper. This will allow greater effectiveness of the Bank's engagement in fragile situations. Management also proposes increasing the unallocated reserve of the TSF's Pillar I from 10 to 15%. Likewise, Management proposes to allocate UA 20 million and UA 60 million to Pillar II and III, respectively, from ADF-14 resources. Management estimates the volume of ADF-14 resources required for the three TSF pillars at UA 614.05 million.
- Management proposes to maintain the current 21% set aside for the Regional Operations (RO) envelope. ADF-13 experience has shown that not only do two thirds of submitted projects end up postponed because of a lack of funding, but also countries tend to prioritize national projects over regional ones. Management thus proposes to decrease the leveraging ratio ceiling for the contribution of the RO envelope to the PBA contribution to a maximum ratio of 1:1.5 for TSF-eligible countries, and 1:1 for other countries—a proposal that would help reduce the number of postponed projects.
- Management recommends the allocation of an additional contribution of UA 200 million from ADF-14 resources to the Private Sector Credit Enhancement Facility (PSF) as separately elaborated in the *“Role of the ADF in Private Sector Development”* paper. This will maintain the facility's current moment in supporting the Bank Group's Non-Sovereign Operations in under-served segments in ADF-eligible countries.
- Management recommends keeping the current PBA formula unchanged.

Finally, this paper also presents the share of the PBA envelope and the various set-asides under four replenishment scenarios as set out separately in the *“ADF-14 Financing Framework”* paper. These scenarios take into account the impact of Concessional Donor Loans (CDLs) and Bridge Loans (BLs) presented in the *“Financing Innovations under ADF-14”* paper. Under these scenarios, the percentage of resources allocated directly or indirectly on the basis of the PBA will remain approx. 90 percent, as was the case in ADF-12 and ADF-13. Within these proposals, performance would remain the fundamental principle for the allocation of ADF-14 resources.

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Abbreviations

ACC	Advanced Commitment Capacity
ADF	African Development Fund
ADF-11	Eleventh General Replenishment of the African Development Fund
ADF-12	Twelfth General Replenishment of the African Development Fund
ADF-13	Thirteenth General Replenishment of the African Development Fund
AfDB	African Development Bank
AIDI	Africa Infrastructure Development Index
AIKP	African Infrastructure Knowledge Program
BL	Bridge Loan
CDL	Concessional Donor Loan
CPA	Country Performance Assessment
CPIA	Country Policy and Institutional Assessment
GNI	Gross National Income
GNIpc	Gross National Income per capita
MDB	Multilateral Development Bank
MTR	Mid-Term Review
PBA	Performance-Based Allocation
PCG	Partial Credit Guarantee
PIDA	Program for Infrastructure Development in Africa
PPA	Portfolio Performance Assessment
PPP	Public-Private Partnership
PRG	Partial Risk Guarantee
PSF	Private Sector Credit Enhancement Facility
RIPOS	Regional Integration Policy and Strategy
RMC	Regional Member Country
RO	Regional Operation
RPG	Regional Public Good
SOE	State Owned Enterprises
TSF	Transition Support Facility
UA	Unit of Account
USD	United States Dollar
WB	World Bank

1. Introduction

1.1. This paper provides an update on the allocation and use of ADF-13 resources. It also presents Management proposals for fine-tuning the ADF-14 allocation framework. The proposals assess the Performance-Based Allocation (PBA) system, Regional Operations (RO) envelope, and Transition Support Facility (TSF). Management also makes recommendations to streamline the Country Policy and Institutional Assessment (CPIA) exercise.

1.2. This paper is organized as follows. Section 2 provides an update on the implementation of the ADF-13 resource allocation framework. It highlights key institutional arrangements on the various reforms agreed with Deputies under ADF-13 negotiations. Section 3 presents several proposals for ADF-14 for the PBA system, the TSF, the RO envelope, and the Private Sector Credit Enhancement Facility (PSF). Section 4 presents various ADF-14 resource allocation scenarios incorporating these proposals. Section 5 concludes and makes recommendations to Deputies.

2. Update on the ADF-13 Resource Allocation

ADF-Eligibility and Envelopes

2.1. Eligibility for ADF is determined by a country's Gross National Income per capita (GNIPC) and its creditworthiness. Under ADF-13, 40 countries were eligible for ADF resources in 2014 and 2015. During those two years, Cameroon and Zambia were blend (category B) and Congo Republic, Nigeria, and Cape Verde were in transition towards graduation to the ADB window (category C). In 2016, following the end of the transition periods of Congo Republic (2 years) and Cape Verde (5 years), 38 countries remained eligible for ADF resources, including Kenya as a newly reclassified blend country (in addition to Cameroon and Zambia) (Annex I).

Overall ADF-13 Resources

2.2. The ADF-13 resource allocation framework consists of 4 envelopes:

- (i) ***The Regional Operations (RO) envelope*** provides funding for regional operations. Since its inception, its size is a percentage of total ADF allocable resources. That percentage was increased to 21% in ADF-13;
- (ii) ***Supplementary resources allocated to transition and post-conflict countries through the 3 pillars of the Transition Support Facility (TSF)***. Pillar I provides supplemental financing to 17 countries experiencing fragility and meeting the eligibility criteria, Pillar II supports the clearance of arrears, and Pillar III funds technical assistance and capacity building available for the full range of the 18 countries;
- (iii) ***The Private Sector Credit Enhancement Facility (PSF)*** provides guarantees for ADB private sector operations in ADF-eligible countries; and
- (iv) ***National allocations for all ADF-eligible countries determined through the Performance-Based Allocation (PBA) system.***

Following ADF-13 replenishment negotiations, expected resources amounted to UA 5,372.79 million. Resources available from commitments – including internally generated resources and payments received from donors' subscriptions – stood at UA 5,320.06 million on May 17, 2016. Out of this amount, UA 3,302.61 million (62%) has been committed to:

- UA 1,904.8 million (64%) for 68 national projects under the PBA framework;

- 25 regional operations (out of 39 prioritized ones) amounting to UA 879.78 million (84%) under the RO envelope;
- UA 416.79 million (71%) committed for 35 projects under Pillar I; and
- UA 40.04 million for targeted support under Pillar III.

Table 1 provides a snapshot of ADF-13 resources as of May 17, 2016.

Table 1: ADF-13 Resources and Usage at May 17, 2016 (UA Million)

	Expected ADF-13 Resources ¹	Resources Available for Commitment	Committed Resources ²	Balance
Performance-Based Allocation Resources	3,108.55	2,975.96	1,905.80	1,070.16
Regional Operations Envelope	1,046.10	1,046.10	879.78	166.32
Transition Support Facility	661.80	1,048.00	457.16	590.84
<i>Pillar I: Supplemental Financing</i>	<i>571.80</i>	<i>590.88</i>	<i>416.79</i>	<i>174.09</i>
<i>Pillar II: Arrear Clearance</i>	<i>30.00</i>	<i>392.62</i>	<i>0.33</i>	<i>392.29</i>
<i>Pillar III: Targeted Support</i>	<i>60.00</i>	<i>64.50</i>	<i>40.04</i>	<i>24.46</i>
Partial Risk Guarantee	-	109.31	-	109.31
Partial Credit Guarantee	-	21.72	-	21.72
Project Preparation Facility	-	14.51	5.181	9.32
Private Sector Facility	165.00	165.00	54.69	110.31
Contingencies	391.34	-60.53	-	-60.53
Total	5,372.79	5,320.06	3,302.61	2,017.45

2.3. The overall ADF-13 balance available for commitment stood at UA 2,017.45 million at mid-May 2016. With a strong pipeline of projects for approval up to end 2016, Management expects all resources to be fully committed by the end of the ADF-13 cycle.

2.4. Next, the paper provides a brief status of the main reforms and innovations under the ADF-13 resource allocation framework.

ADF-13 Reforms and Innovations

The Performance-Based Allocation System

2.5. During ADF-13 discussions, Deputies agreed to introduce adjustments aiming to address the changing development context for African countries and to reinforce alignment between the allocation tool and the Bank's priorities. These adjustments included:

- adding 'Cluster E', which assesses the regulatory frameworks enabling infrastructure development and regional integration in the Country Policy and Institutional Assessment (CPIA) questionnaire, with a weight of 6% in the performance component of the PBA formula;
- adding the Africa Infrastructure Development Index (AIDI) as a needs component in the PBA formula with an exponent of -0.25;
- increasing the minimum allocation from UA 5 million to UA 15 million per cycle; and
- increasing the performance component in the PBA formula from 4 to 4.125.

¹ African Development Fund, 25 January 2016. *2016 Performance-Based Allocations under ADF-13*. ADF/BD/IF/2016/12.

² Include surcharges on grants as derived from the Statement of Commitment Capacity.

These adjustments became fully operational starting from the first year of the ADF-13 cycle and have been effectively implemented (Annex II).

Regional Operations Envelope

2.6. Under ADF-13 discussions, Deputies endorsed the use of the Fund's comparative advantage by creating greater support for regional infrastructure, Regional Public Goods programs (RPGs), and capacity building (with a particular focus on countries experiencing fragile situations). More specifically, 21% of ADF-13 resources were allocated to the RO envelope, with a 15% ceiling of resource channelled to RPGs. For the cost-sharing mechanism, in order to allow ADF-13 to support a higher number of transformational projects at a regional and sub-regional level, the standard multiplier of the RO envelope to PBA allocation was set at 1.5 times (a ratio of 1:1.5). A special arrangement applies to countries eligible for TSF Pillar I, with a differentiated multiplier of 2 times (a ratio of 1:2) and the possibility of using TSF Pillar I allocations to leverage funding from the RO envelope. In addition, countries with small PBAs contribute at least 40% of project costs, up to 10% of their PBA for each regional project, in order to incentivize them to partake in regional projects.

2.7. As agreed under ADF-13 discussions, a new Regional Integration Policy and Strategy (RIPOS) was approved in 2014 for implementation during the period 2014 to 2023.³ During the ADF-14 period, the Bank will continue to implement the priorities in the RIPOS in accordance to the Bank's long-term support to Africa's economic integration. The RIPOS has three mutually reinforcing pillars: (i) supporting regional infrastructure development; (ii) enhancing trade and industrial development; and (iii) strengthening country and regional mechanisms and institutional capacities (a cross-cutting pillar).

Box 1: Regional Operation Prioritization Framework

According to the RO Prioritization Framework approved in April 2014, the selection of RO projects follows a two-step process:

Step 1 (Project Alignment/eligibility)

It aims at ensuring country ownership at the same time as strategic alignment with the regional priorities, the Bank Regional Integration Strategy and its Papers, and major continental commitments such as PIDA. It also requires the inclusion of a policy component in projects.

Step 2

- **For a cost-sharing RO project:** the project is assessed through a scorecard based on three indicators related to (i) the performance of countries involved (CPIA and Portfolio Performance), (ii) a country's commitment to regional integration, and (iii) two indicators related to the project (Expected Development Outcome, ADOA, and quality and readiness).
- **For RPG project:** the scorecard is based on indicators concerning non-rivalry and non-excludability; public interest and ownership; regional dimension; strategic alignment; catalytic role; incremental benefit in cooperation; and the development impact.

A RO prioritization team composed of representatives of four Bank departments (ONRI, FMRB, ORQR, and EDRE) generates the scores and the ranking of each project. The final decision of selection is made by the Operation Steering Committee (OPSCOM).

2.8. Regional Operations are subject to rigorous selection and prioritization through the Regional Operations Selection and Prioritization Framework (see Box 1) which was approved by the Board on

³ African Development Fund, 10 September 2014. *Bank Group Regional Integration Policy and Strategy (RIPoS) 2014-2023*. ADF/BD/WP/2014/98.

April 2014.⁴ Based on this framework, during 2014 the three-year ADF-13 pipeline included 56 RO projects and 30 RPGs with a total cost estimated at UA 3,098 million for RO and UA 215 million for RPGs, representing close to 3 times the available envelop. Requests coming from transition state countries represented approximately 54%.

Transition Support Facility

2.9. Drawing on its long-standing experience of operating in fragile situations, the Bank was the first multilateral institution to switch from a binary and typically state-centred view of fragility (i.e. fragile vs. non-fragile states) to approach fragility from a multi-dimensional risk perspective (political, security, economic, social and environmental risks) that is not strictly state-centred. As a consequence, the Bank has since adapted its business model to take into account this multi-dimensional “fragility-lens”. Lessons learned under ADF-13 have shown the importance of better capacity and processes to assess fragility, but also revealed institutional gaps in ensuring swift responses to assessments, particularly in volatile and insecure environments.

Table 2: TSF Pillar I Allocations and Total Allocations under ADF-13 (UA Million)

Country	Pillar I Allocation	Pillar I Allocation plus Three-year PBA
Burundi	25.42	60.83
Central African Rep.	14.84	28.84
Chad	10.00	43.79
Comoros	10.00	25.00
Congo Democratic Rep.	60.00	348.70
Cote d'Ivoire	60.00	132.54
Guinea	25.00	70.30
Guinea-Bissau	13.32	28.32
Liberia	36.23	57.03
Madagascar	60.00	119.04
Mali	60.00	116.93
Sierra Leone	16.01	37.72
Somalia	11.20	26.20
South Sudan	21.94	36.94
Sudan	60.00	117.94
Togo	39.68	56.33
Zimbabwe	44.91	62.50
Total	568.55	1,368.95

2.10. In addition to the AfDB/WB harmonised list of Fragile Countries (which is drawn on the basis of a CPIA score of 3.2 or less, or the presence of peacekeeping or peacebuilding mission in the last 3 years), it was agreed under ADF-13 that eligibility for the TSF also follows a qualitative assessment that demonstrates whether there is a substantial degree of fragility despite a high CPIA (for example through analysis of internal or external fragility factors not captured by the CPIA), or marginal improvements over the CPIA cut-off threshold of 3.2, or a substantial declining trend of the CPIA over the previous three years.

2.11. Resources through Pillars II and III continue to be allocated in the form of grants. However, under ADF-13, Deputies endorsed the adjustment of the financing terms of Pillar I allocations to match the loans and grants mix of PBAs as calculated in the first year of the cycle. They likewise agreed to

⁴ African Development Fund, 2 April 2014. *Revised Regional Operations Selection and Prioritization Framework*. ADF/BD/WP/2014/32.

keep a 10% unallocated portion of Pillar I as a reserve to meet emergencies or to provide resources to countries that may not have qualified as beneficiaries at the beginning of the cycle.

2.12. To date, 17 countries benefited from Pillar I assistance under ADF-13 with a total amount of UA 568.55 million (Table 2). This also includes Guinea, which, following the Ebola outbreak emergency, became eligible in the course of the cycle and was granted access to UA 25 million from the 10% reserve pool. Similarly, in 2016, an additional eligibility assessment allowed Chad to access UA 10 million of the Pillar I resources.

2.13. Additional resources are made available to qualifying countries under Pillars II and III. Pillar II resources are earmarked for arrears clearance and are currently targeted at Somalia, Sudan and Zimbabwe on a first-come, first-served basis. Pillar III resources are used to support capacity building and technical assistance for activities that cannot otherwise be provided through the Bank's existing instruments and programs.

Innovative Instruments under ADF-13

2.14. Under ADF-12, Deputies agreed to introduce the **Partial Risk Guarantee** (PRG). The instrument aims to increase the impact of the PBA and leverage resources from the private sector and other co-financiers for ADF countries, including countries in fragility situations. Since inception, the PRG has supported two projects in Kenya and one in Nigeria. With a total guarantee face value of UA 146 million, it has helped catalyse over USD 2.7 billion in investments. Although its uptake has been slow, its attractiveness lies in its ability to insure private lenders against well-defined political risks, related to government failure or the failure of government-related entities to honour specified commitments.

2.15. Another leveraging instrument, the **Partial Credit Guarantee** (PCG), was approved and launched under ADF-13. PCGs are meant to help catalyse more resources on more reasonable terms. The instrument targets ADF countries assessed as at low risk of debt distress and having adequate debt management capacity. During the ADF-13 Mid-Term Review (MTR), Deputies agreed to extend the PCG eligibility to ADF countries at moderate risk of debt distress. The instrument is also available for use by State Owned Enterprises (SOEs) in ADF countries, to help mobilize domestic and external commercial financing, and thereby improve access to more affordable financing. Two PCG transactions were approved under ADF-13: a first one on March 2016 with a total guarantee exposure of USD 40 million for Madagascar and a second PCG of USD 4 million for Tanzania Mortgage Refinance Company recently approved on May 2016.

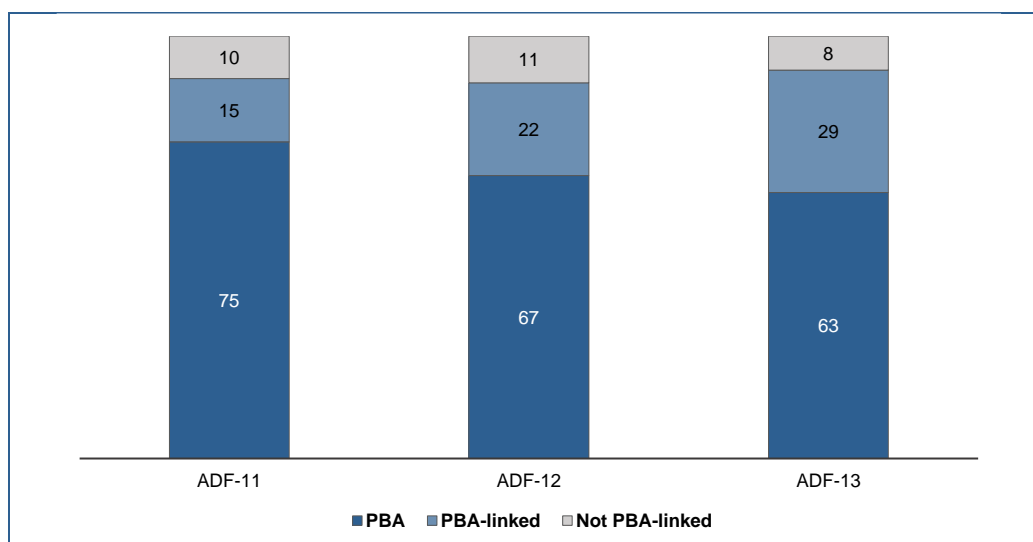
2.16. Annex III provides an extensive update on the current implementation status of the PRG and the PCG. It also details institutional and operational arrangements within the Bank and gives an outlook for ongoing demands for the two instruments.

2.17. The **Private Sector Credit Enhancement Facility** (PSF) aims at increasing private financing in low-income countries (LICs). It was launched – on a pilot basis – under ADF-13 in 2015. The PSF operates as a captive credit enhancement vehicle, participating in the credit default risk of the ADB's non-sovereign guaranteed operations, enabling the ADB to prudently stretch its risk capital in LICs. Backed by a seed liquidity reserve of UA 165 million from ADF-13 resources, the facility's structure has been designed to enable a "BBB" equivalent level of credit enhancement to cover exposures amounting to UA 495 million. Utilization of the PSF has been proceeding steadily under ADF-13. As at the end of 2015, approximately UA 160 million of exposures have already been allocated to 15 transactions at diverse stages of implementation, more than 50% of which are in fragile states. More details on the implementation of the PSF under ADF-13 are provided in the *"Role of ADF in Private Sector Development"* paper.

ADF-13 Performance-Linked Allocations

2.18. Under the ADF-13 allocation framework, the cost-sharing mechanism of ROs and the top-up factor of the TSF Pillar I allocations enable a strong link to PBAs. Therefore, although the TSF, the RO envelope, and the PSF are particular allocations, country performance still remains the anchor around which most ADF resources are allocated. As shown in Figure 1, around 92% of expected ADF-13 resources would be directly or indirectly allocated on the basis of performance.

Figure 1: Share of Allocations Linked to the PBA System under ADF-11, 12, and 13 (Percentage)



Notes: PBA = Performance-Based Allocations
PBA-linked = TSF Pillar I + ROs (with cost-sharing)
Not PBA-linked = TSF Pillar II & III + ROs (exempted from cost-sharing) + PSF (for ADF-13)

3. Proposed Changes in the ADF-14 Resource Allocation Framework

3.1. What follows below is a series of specific proposals by Management focused on fine-tuning the resource allocation framework under ADF-14. These deal with the PBA framework, the TSF eligibility and allocations, and the RO envelope and its cost-sharing mechanism.

Proposals Dealing with the PBA Framework

Moving to a Biennial CPIA Exercise

3.2. Under the current ADF resource allocation process, the CPIA exercise is conducted annually for all 54 RMCs of the Bank Group. In view of the frequency of institutional and legal reforms in the various countries, as well as the time needed for their implementation, yearly assessments are not the most effective. This particularly applies for most areas covered by the CPIA questionnaire such as structural policies (Cluster B), social policies (Cluster C), and even public sector management (Cluster D). Annual evaluations of countries' policies on these dimensions may not adequately capture progresses achieved by any country, given the lag time normally associated with most institutional reforms and their effective implementation. Moreover, despite technical improvements in recent years, the exercise is time-consuming and resource-intensive for the Bank, RMC authorities and the various other parties that are consulted.

3.3. **Management therefore proposes that the CPIA exercise is undertaken every two years.** This will allow for sufficient time to learn from each evaluation and to strengthen the resulting policy dialogue. Given that the latest CPIA exercise was conducted at Q4 of 2015, Management proposes that starting from ADF-14, the next CPIA is undertaken in Q4 of 2016, and the subsequent exercise in Q4 of

2018 covering the assessment of the 2017-2018 period. The Bank reserves the right to undertake exceptional assessment when there is a need to re-evaluate the CPIA of a given country outside of the regular biennial exercises.

3.4. **Under the proposal, the annual PBA computation exercise would use the latest CPIA scores available.**

3.5. Figure 2 shows the proposed schedule for the next three ADF cycles. The computation of the 2017 and 2018 PBAs would be based on the 2016 CPIA scores, and the PBAs for 2019 would rely on the 2018 biennial CPIA assessment.

Figure 2: Proposed Schedule for the Upcoming ADF Allocation Processes

Cycle	ADF-13			ADF-14			ADF-15			ADF-16		
Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025
CPIA		■	■	■	■	■	■	■	■	■	■	■
PBA		↓	↓	↓	↓	↓	↓	↓	↓	↓	↓	↓

Addressing Fragility in the PBA System

3.6. During the first ADF-14 replenishment meeting, a technical note presenting options addressing fragility in the PBA system was discussed. While there was common support for ADF engagement to address fragility, a specific request was made for further simulations of including fragility in the PBA formula. Annex IV summarizes key findings of these requested simulations.

3.7. As was the case at the first meeting, these simulations suggest that adding a fragility component to the PBA formula would not significantly scale-up the current resource allocations for countries experiencing fragility. Therefore, **Management recommends keeping the current PBA formula unchanged.**

Proposals Dealing with the TSF

3.8. The “*Role of ADF-14 in Supporting Fragile Situations*” paper proposes various recommendations for increasing the effectiveness of the Bank’s engagement in fragile situations under ADF-14. Without repeating the underlying arguments, next we focus on country eligibility to the TSF and the financial implications of these recommendations on the three TSF pillars.

Eligibility to TSF under ADF-14

3.9. Eligibility to TSF is mainly driven by the harmonized MDB list of fragile situations. The latest list available for FY16 (Annex V), suggests 18 ADF countries are potentially eligible. Pending the publication of the FY17 MDB harmonized list, which will be released in July 2016, and as part of the flexible approach introduced in ADF-13, **Management intends to undertake additional qualitative eligibility assessments for Guinea, Malawi and Niger** that are not included in the current version of the harmonized list. The assessments would be presented to the Board by Q4, 2016.

3.10. Likewise, Management also intends to inform the ADF Board of the plan to **remove Cote d’Ivoire from the pool of countries eligible for TSF** in view of the rapidly improving situation of the country that may not warrant further resource allocations from this facility.

Pillar I Envelope under ADF-14

3.11. To access the TSF Pillar I resources, a country has to be both eligible for TSF (classified in fragile situation), and meet the specific two-stage eligibility criteria agreed under ADF-13 negotiations

(Annex VI). Management suggests a list of 15 countries based on ADF-13 eligibility and the FY16 harmonized list (Table 3).

3.12. This eligibility list (Table 3) is used to estimate the required ADF-14 Pillar I envelope. The size estimated for Pillar I is based on the same assumptions of the allocation methodology agreed under ADF-13,⁵ as detailed in the “*Role of ADF-14 in Supporting Fragile Situations*” paper. **Management suggest to increase the unallocated Pillar I reserve from 10 to 15% under ADF-14.** As detailed in Annex VII, **calculations suggest that Pillar I size required under ADF-14 would be UA 534.05 million.**

Table 3: Preliminary Pillar I Eligibility under ADF-14 based on the Two-Stage Criteria

Country		First Stage Criteria					Second Stage Criteria
		Peace & Security Commitment	GDP per Capita (in 2005 constant USD) ⁶			2014 HDI Bottom Quintile	
			1995	2014	Change (%)		
1	Burundi	■	172.8	152.7	-11.6	0.400	●
2	Central African Rep.	■	345.7	266.4	-34.5	0.350	⦿
3	Chad	▣	383.2	766.4	100	0.392	●
4	Comoros	■	602.4	596.9	-0.9	0.503	●
5	Congo Democratic Rep.	■	287.3	283.5	-1.3	0.433	●
6	Guinea-Bissau	▣	500.7	420.2	-16.1	0.420	⦿
7	Liberia	■	69.6	226.7	225.8	0.430	●
8	Madagascar	■	277.3	271.6	-2.1	0.510	⦿
9	Mali	■	338.4	458.2	35.4	0.419	⦿
10	Sierra Leone	■	292.3	513.4	75.7	0.413	●
11	Somalia	■	-	-	-	-	⦿
12	South Sudan	■	-	-	-	0.467	●
13	Sudan	■	481.8	972.8	101.9	0.479	⦿
14	Togo	■	377.7	429.8	13.8	0.484	●
15	Zimbabwe	■	645.0	458.1	-29.0	0.509	⦿

■ Fully confirmed commitment to consolidate peace and security

□ Commitment to be confirmed after full assessment

● Second stage criteria fully met

○ To be confirmed after full assessment

Pillars II Envelope under ADF-14

3.13. **It is proposed that UA 20 million is allocated to Pillar II to clear the total of Somalia’s arrears to the ADB under ADF-14.** Based on the recent progress made by Somalia, it is reasonable to assume that the country’s arrears could be cleared during ADF-14. In the case of Sudan, the prospects remain uncertain and will be reassessed during the ADF-14 Mid-Term Review. Should Sudan make progress towards arrears clearance under an internationally coordinated program during this period, the Bank will explore all options to mobilize funding for clearing the country’s arrears to the ADB. For Zimbabwe, an update on the prospects of clearing the country’s arrears under ADF-13 will be provided ahead of

⁵ African Development Fund, 16 January 2015. *Operational Guidelines for the Implementation of the Strategy for Addressing Fragility and Building Resilience in Africa and for the Transition Support Facility*. ADF/BD/WP/2014/Rev.3/Approved.

⁶ For ADF-14, as part of the first stage criteria dealing with social and economic needs, the 1995-2014 period is considered to observe contraction of real GDP per capita.

the third ADF-14 replenishment meeting. If Zimbabwe's arrears are not cleared under ADF-13, **it is recommended that the unutilised resources should be rolled over to Pillar II under ADF-14.**

Pillar III Envelope under ADF-14

3.14. While pursuing the current approach of using Pillar III resources for building institutional capacity, **Management proposes to use also this window to support private sector development through targeted investment facilitation.** Building on this and in view of the projected utilisation of remaining Pillar III ADF-13 resources, **Management recommends the allocation of UA 60 million to the pillar from ADF-14 resources.**

Total TSF Resource Allocation under ADF-14

3.15. As highlighted in Table 4, with the proposals for the TSF envelopes, Management estimates that the volume of ADF-14 required for the TSF would be **UA 614.05 million.**

Table 4: Estimated Allocation of ADF-14 Resources to the TSF (UA Million)

	Envelope (UA million)
Pillar I (15 countries)	534.05
<i>Country-allocated</i>	<i>453.94</i>
<i>Unallocated (15%)</i>	<i>80.11</i>
Pillar II (3 countries)	20.00
Pillar III (all TSF-eligible countries)	60.00
Total TSF Envelope	614.05

Proposals Dealing with the RO Envelope

3.16. The demand for funding regional integration projects under the RO envelope have been steadily increasing. While ROs represented only 6% of total approvals in 2000, they accounted for 15% in 2010, and an estimated 25% in 2015. In 2015, the pipeline for the remaining ADF-13 cycle amounted to UA 1,703.8 million – including UA 1,424 million for RO and UA 279.8 million for RPG – out of surcharge. Given these positive outcomes, **Management recommend to maintain the Resources envelop for RO at 21% of the resources available for allocation under ADF-14.**

Reducing the RO Contribution Leveraging Ceiling

3.17. The RO envelope has been essential in bridging the financial gap for regional projects. However, close to two third of projects submitted are postponed because of a lack of funding. Lessons learnt indicate that without any incentive contributions from the RO envelope, countries continue to prioritize national interventions versus regional ones, and are reluctant to undertake more regional integration projects, despite their obvious development impact.

3.18. In order to reduce the number of postponed projects, and to maintain the role of the Bank as lead financier, **Management proposes the reduction of the leveraging ratio ceiling for the contribution of the RO envelope to the PBA contribution to a maximum ratio of 1:1.5 for TSF countries, and 1:1 for other countries.** Analysis indicates that this will not deter the incentive nature of the envelope, and may increase co-financing and leveraging of other resources available to undertake more RI projects and serve more countries.

Proposals for the PSF

3.19. Since effectiveness in May 2015, a third of the PSF's exposure capacity has already been allocated to 15 ADB private sector transactions, of which more than 50 % were in fragile states by end

of 2015. Robust interest for PSF participation from fragile states and regulated sectors (power, transport and renewable energy) suggest an expected increase of PSF utilization rate to 40% by end of Q2, 2016. The pilot phase of the PSF has allowed the Bank to free up risk capital and undertake higher risk/high return operations especially in countries in fragile situations. This has helped overcome some of the key constraints in reaching under-served segments through Non-Sovereign Operations. The significant take-up over the past year indicates the importance of augmenting the resources available over the next ADF cycle.

3.20. **Management recommends an additional contribution of UA 200 million to the PSF from ADF-14 resources.** Moreover, a number of strategic design options have been identified to enhance the impact of the PSF beyond its pilot period and are discussed in the *“Role of ADF in Private Sector Development”* paper.

4. ADF-14 Resource Allocation Scenarios

Allocation Methodology

4.1. In the following scenarios, the allocation of ADF-14 resources to various envelopes are calculated using a methodology based on the following formulas:

Total ADF-14 resources	(A) = (1) + (2)
Total donor contribution (subscribed amounts)	(1)
Internally generated resources (ACC)	(2)
Add carry-overs from previous replenishments	(B) = UA 389.00 million
Less upfront deductions	(C) = (3) + (4)
Exchange rate contingency on unpaid subscriptions	(3) = 1% × (1)
Contingency for qualified and late subscriptions	(4) = UA 375.10 million
Add impacts of innovative financing instruments	(D) = (5) + (6)
ACC from Bridge Loans and Concessional Donor Loans	(5)
Concessional Donor Loans	(6)
ADF-14 resources available for allocation	(E) = (A) + (B) – (C) + (D)
Transition Support Facility (TSF)	(7) = UA 614.05 million
Regional Operations envelope (RO)	(8) = 21% × (E)
Private Sector Facility (PSF)	(9) = UA 200.00 million
Country Performance-Based Allocations (PBA)	(10) = (E) – (7) – (8) – (9)

4.2. In this ADF-14 resource allocation methodology, in addition to a contingency for qualified and late subscriptions estimated at UA 375.10 million, there is allowance of a technical contingency of 1% of donor contributions related to the exchange rate on potential unpaid subscriptions. The methodology also assumes expected total carry-overs (including qualified and late subscriptions from previous cycles) of UA 389.00 million under ADF-14.

4.3. The proposals dealing with Concessional Donor Loans (CDLs) and Bridge Loans (BLs) presented in the *“Financing Innovations under ADF-14”* paper, the potential impacts of these instruments on the internally generated resources of the Fund – through the Advance Commitment Capacity (ACC) –and on donor contributions are also taken into account in this methodology as additional resources to be allocated.

Proposed Allocation Scenarios

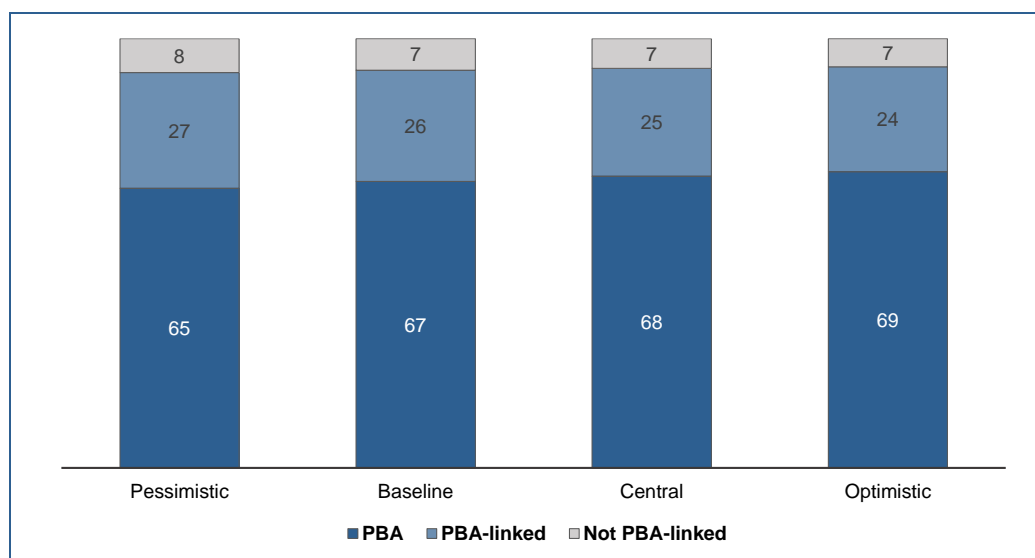
Table 5: ADF-14 Resource Allocation

	ADF-14 Financing Scenarios							
	Pessimistic (-5% increase in subscriptions)		Baseline (0% increase in subscriptions)		Central (+5% increase in subscriptions)		Optimistic (+10% increase in subscriptions)	
	UA million	(%)	UA million	(%)	UA million	(%)	UA million	(%)
ADF-14 Resources Available for Allocation	5,858	100	6,611	100	7,364	100	8,117	100
Transition Support Facility	614	10.5	614	9.3	614	8.3	614	7.6
<i>Pillar I: Supplemental</i>	534	9.1	534	8.1	534	7.3	534	6.6
<i>Pillar II: Arrear Clearance</i>	20	0.3	20	0.3	20	0.3	20	0.2
<i>Pillar III: Targeted</i>	60	1.0	60	0.9	60	0.8	60	0.7
Regional Operations envelope	1,230	21.0	1,388	21.0	1,546	21.0	1,704	21.0
Private Sector Facility	200	3.4	200	3.0	200	2.7	200	2.5
Performance-Based Allocation	3,814	65.1	4,408	66.7	5,003	67.9	5,598	69.0

4.4. Table 5 presents, in nominal and percentage terms, allocation scenarios showing how the ADF-14 resources would be allocated among the PBA system, RO envelope and the TSF. These allocation scenarios rely on the TSF Pillar I eligibility list presented in Section 3 (Table 4) and the four replenishment scenarios as included in the “ADF-14 Financing Framework” paper (pessimistic, baseline, central, and optimistic).

4.5. While the TSF envelope stood at 13% of resource available for allocation under ADF-13, depending on the ADF-14 replenishment scenario, the size of the TSF would vary from 7.6% (under the optimistic scenario) to 10.5% (under the pessimistic scenario) of allocable resources. Given the RO envelope is fixed at 21% of resources, and a fixed set-aside of UA 200 million is allocated to the PSF, the PBA envelope would consequently comprise between 65.1% (under the pessimistic scenario) and 69.0% (under the optimistic scenario) of ADF-14 resources.

Figure 3: Estimated Share of Allocations Linked to the PBA System under ADF-14 (Percentage)



Notes: PBA = Performance-Based Allocations

PBA-linked = TSF Pillar I + ROs (with cost-sharing)

Not PBA-linked = TSF Pillar II & III + ROs (exempted from cost-sharing) + PSF

4.6. Figure 3 demonstrates that, within the suggested scenarios, the percentage of ADF-14 resources to be allocated on the basis of performance would range between 92 and 93%, which is slightly higher than in ADF-12 and ADF-13 (Figure 1). With a higher replenishment, the ADF-14 allocation framework would reinforce performance as the bedrock principle of the Fund's country allocations.

5. Recommendations

5.1. Deputies are invited to provide guidance on the proposals detailed in Section 3 of this paper:

- (i) **Undertaking the CPIA exercise every two years starting from Q4, 2016.**
- (ii) **Keeping the current PBA formula unchanged under ADF-14.**
- (iii) **Increasing the unused reserve of the TSF Pillar I from 10 to 15%.**
- (iv) **For Pillar II of the TSF, allocate UA 20 million from ADF-14 replenishment and carrying over any unutilized resources from ADF-13 to ADF-14.**
- (v) **Maintain the RO envelope at 21% of ADF-14 resources and reduce the RO contribution leveraging ceiling to a maximum ratio of 1:1.5 for TSF countries, and 1:1 for other countries.**
- (vi) **An additional contribution of UA 200 million to the PSF.**

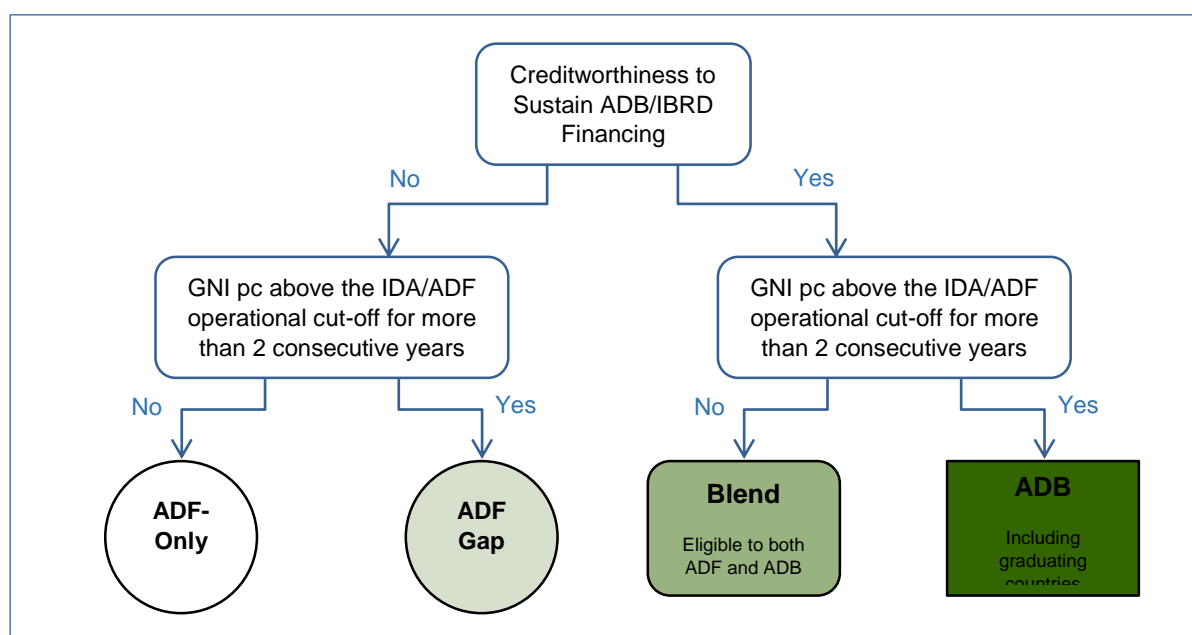
Annex I: Classification of Countries Eligible for ADF Resources

Table I-1: Country Classification under ADF-13 and projected ADF-14

Country		TSF	ADF-13			ADF-14 (projections)		
			2014	2015	2016	2017	2018	2019
1	Benin		■	■	■	■	■	■
2	Burkina Faso		■	■	■	■	■	■
3	Burundi	■	■	■	■	■	■	■
4	Cameroon		●	●	●	●	●	●
5	Cape Verde		▲	▲	▲	▲	▲	▲
6	Central African Rep.	■	■	■	■	■	■	■
7	Chad	■	■	■	■	■	■	■
8	Comoros	■	■	■	■	■	■	■
9	Cote d'Ivoire	■	■	■	□	□	□	□
10	Congo Democratic Rep.	■	■	■	■	■	■	■
11	Congo Rep.		▲	▲	▲	▲	▲	▲
12	Djibouti		□	□	□	□	□	□
13	Eritrea	■	■	■	■	■	■	■
14	Ethiopia		■	■	■	■	■	■
15	Gambia		■	■	■	■	■	■
16	Ghana		□	□	□	□	●	●
17	Guinea	■	■	■	■	■	■	■
18	Guinea-Bissau	■	■	■	■	■	■	■
19	Kenya		■	■	●	●	●	●
20	Lesotho		■	□	□	□	□	□
21	Liberia	■	■	■	■	■	■	■
22	Madagascar	■	■	■	■	■	■	■
23	Malawi		■	■	■	■	■	■
24	Mali	■	■	■	■	■	■	■
25	Mauritania		■	■	■	■	■	■
26	Mozambique		■	■	■	■	■	■
27	Niger		■	■	■	■	■	■
28	Nigeria		▲	▲	▲	▲	▲	▲
29	Rwanda		■	■	■	■	■	■
30	São Tomé et Príncipe		□	□	□	□	□	□
31	Senegal		■	■	■	●	●	●
32	Sierra Leone	■	■	■	■	■	■	■
33	Somalia	■	■	■	■	■	■	■
34	South Sudan	■	■	■	■	■	■	■
35	Sudan	■	■	■	■	■	■	□
36	Tanzania		■	■	■	■	■	■
37	Togo	■	■	■	■	■	■	■
38	Uganda		■	■	■	■	■	■
39	Zambia		●	●	●	●	●	▲
40	Zimbabwe	■	■	■	■	■	■	■

- Eligible for TSF
- ADF-only (category A)
- Gap (category A)
- Blend (category B)
- ▲ In transition to ADB (category C)
- ▲ ADB-only (category C)

Figure I-1: The Bank's Group Country Classification



ADF-only Countries: According to the Bank's Group Credit Policy classification, a country is considered ADF-only if its income level is below the GNI pc cut off for IDA/ADF eligibility (\$1,215 for fiscal year 2014/2015) for each year and if it is not deemed creditworthy for non-concessional financing.

Gap Countries: Since 2011, countries which GNI pc exceeds the GNI pc cut off by more than two years (or at least three consecutive years) but that are not deemed creditworthy are classified as gap countries. It is important to note that gap countries are ADF as they remain highly dependent on concessional financing. Currently, four ADF eligible countries achieved the gap status: Djibouti, Ghana, Lesotho and Sao Tomé & Príncipe.

Blend: A country which is creditworthy as defined by the Bank's Group and its income level is below the IDA/ADF GNI pc cut off each year.

Graduating Countries: They are countries in transition from ADF or Blend categories to ADB. The minimum length of the transition period is set to 2 years. Depending on the level of poverty and human development; the average economic growth; and the financial need, one graduating country can extend its transition period up to 5 years.

ADB: A country which GNI pc exceeds the operational cut off for more than two consecutive years (or at least three consecutive years), and complies with the Bank's creditworthiness criteria at the moment of the assessment. Depending on the country's development level and based on the Transition Framework for Countries Changing Credit Status (ADB/BD/WP/2011/20/Rev.2), the country will benefit from a transition period from 2 to 5 years.

GNI per capita: Gross National Income as computed using the Atlas method in current US dollars.

Total public debt as a percentage of GDP: Refers to the total public debt outstanding at year-end (as % of GDP).

Total debt servicing as a percentage of total exports: Includes interest and amortization paid by a country as a percentage of total exports of goods and services.

CPIA: Is the Country Policy and Institutional Assessment. The CPIA score is the aggregate indicator assessing the annual overall performance of a country in terms of economic management, structural policies, policies for social inclusion/equity, governance, and policies enabling infrastructure development and regional integration.

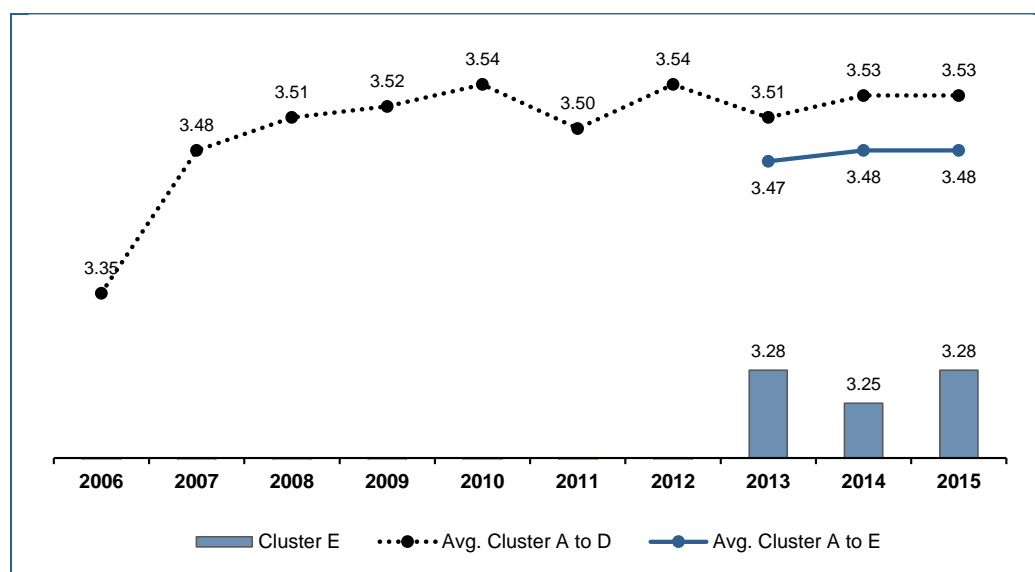
GNI pc operational cut-off: Is the per capita gross national income threshold we used as a first criterion to determine classification of countries.

GNI pc threshold for LMICs: Is the per capita gross national income threshold we used as a sub-criterion as part of the creditworthiness assessment of countries.

Annex II: Implementation and Key Outcomes of the ADF-13 PBA Adjustments

Addition of Cluster E

Figure II-1: CPIA Score Averages under ADF-13



In implementing Cluster E, up-stream consultations during the drafting of the questions and guidelines of the new cluster for the ADF-13 negotiations, ensured early internal buy-in by the Bank Group's country teams in charge of the annual CPIA evaluations. In addition, an online CPIA Platform was developed and has significantly contributed to an efficient operationalization of the new cluster (see Box II-1). Substantively the inclusion of Cluster E has not let do any distortions in the CPIA structure nor created score inflation. As highlighted in Figure II-1-the new CPIA average aggregate of Cluster A to E is strongly correlated with the old aggregate of Clusters A to D. In general, Cluster E contributed to greater rationalization of overall CPIA scores and also helped reduce its trend magnitude.

Box II-1: The Online CPIA Platform

Up to the 2011 exercise, the CPIA process was an inefficient, non-transparent and error-prone manual exercise: All exchanges between drafters, reviewers and coordinators during the production of the CPIA notes and scores used to be done entirely via email. Following a pilot phase in 2012, the Bank has since developed a CPIA Platform (<https://cpia.afdb.org/>), which is a secure online tool to implement, and monitor the annual country assessment process, report on results, share knowledge, and foster policy dialogue with RMCs.

Today, the Platform is the bedrock of the CPIA compilations and greatly assists country teams to efficiently produce their annual country evaluations in a secured, transparent, and timely manner. The platform is designed appropriately to ensure quality of evaluations involving several hundred peer reviewers both from, within, and outside the Bank. The tool has also not only strengthened the implementation of the annual assessments but is now also used as a knowledge-sharing tool providing robust data, reporting on results, and facilitating policy dialogue between the Bank and its RMCs.

Inclusion of the AIDI

Inclusion of the AIDI index in the computation of the PBA – starting from the first year of the ADF-13 cycle – has proceeded well. The index uses data collected under the Africa Infrastructure Knowledge Program (AIKP) and complemented with other international sources. To ensure its robustness over space and time, AIDI data is regularly updated and released yearly in the month of November since 2013 (see Box II-2).

Box II-2: Africa Infrastructure Development Index

The AIDI is based on four major components, which are: (i) Transport; (ii) Electricity; (iii) ICT; and (iv) Water and Sanitation. Its yearly releases reflects the updates made on 9 selected indicators that comprise the Index's components. These are mainly the following: Total paved roads (km per 10,000 inhabitants), Total paved roads (km per km² of exploitable land area), Net Generation of Electricity (KWh per capita), Total Phone Subscription (fixed line and mobiles, per 100 inhabitants), Number of Internet Users (per 100 inhabitants), Fixed (wired) Broadband Internet Subscribers (per 100 inhabitants), International Internet Bandwidth (Mbit/s), Improved Water Source (percentage of population with access), Improved Sanitation Facilities (percentage of population with access).

Performance Principle

Performance remain the bedrock of the PBA system. Under ADF-12, 69% of PBAs were allocated to the top performing countries (first and the second CPA quintiles). Recent PBA adjustments have not altered this performance principle given that 68% of resources are channelled to the same best performers under ADF-13. Moreover, the ADF-13 adjustments have meant stronger rewards to the highest performing countries by transferring resources from the second to the first quintile. As shows Figure II-2, this applies to resources distributed by quintiles of overall performance (CPA) as well as by quintiles of CPIA (average scores of cluster A, B, and C).

To be sure, the balance between performance and needs components underlying the PBA framework, still allows for adjustments to better address the particular demands of the neediest countries. Figure II-3 shows the shift in the allocation structure from ADF-12 to ADF-13, where the largest share of resources (around 29%) moved to countries belonging both to the first performance and the first needs quintile. The further a country moves away from this group due to a lower need and/or lower performance, the smaller the size of its PBA. This demonstrates the impact of introducing the AIDI in the PBA formula, which helped rebalance the distribution of resources in favour of countries experiencing higher deficits in infrastructure commodities.

Figure II-2: PBA by (a) Performance and (b) CPIA Quintiles in ADF-12 and ADF-13 (Percentage)

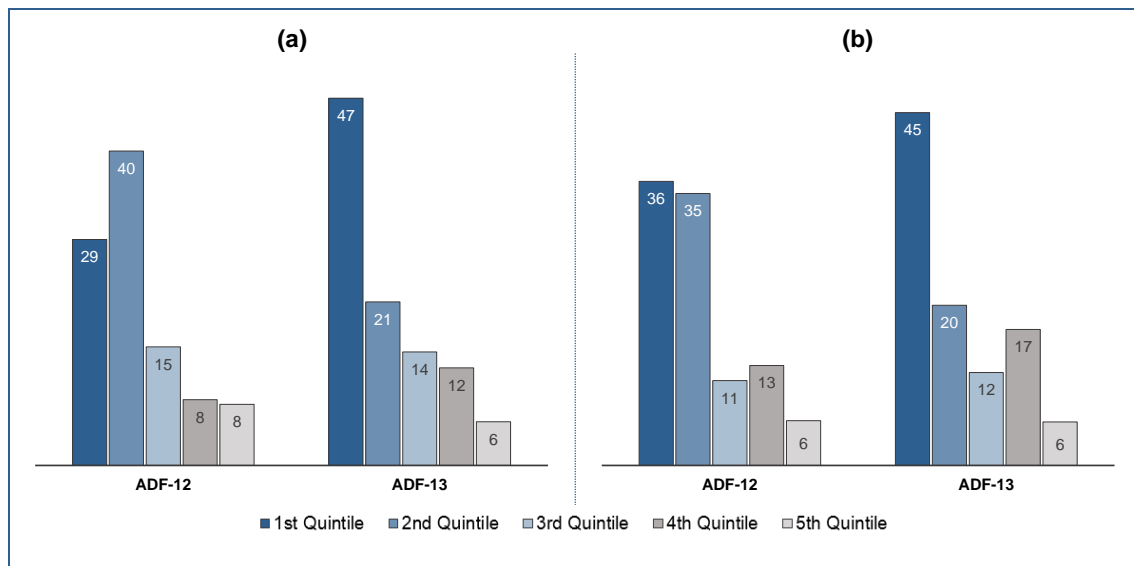
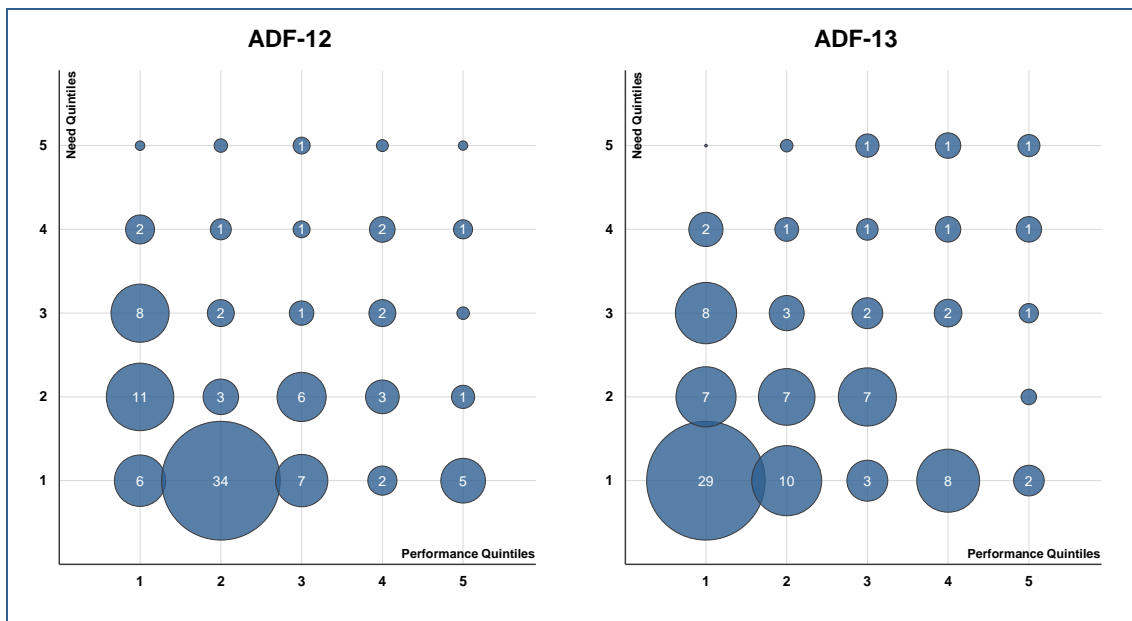


Figure II-3: PBA by Needs and Performance Quintiles in ADF-12 and ADF-13 (Percentage)



Annex III: ADF Guarantee Instruments

Progress on PRG and PCG Implementation

Institutional and Operational Arrangements: Detailed operational guidelines set out in a Strategic Framework and Operational Guidelines document, were adopted for the PRG in 2011 and for the PCG in 2013. These provide the framework with principles and modalities extending the instruments.

Marketing, Awareness Building and Demand Creation: The Bank has undertaken a range of measures to promote the use of these financial instruments. It has provided intensive awareness and focused training activities for Bank staff and has organized various outreach activities for both regional member countries (RMCs) and for private sector investors as well as lenders. Marketing, awareness and training events have been organized reaching a wide audience of both Bank staff and clients. Marketing and awareness initiatives are also being pursued in 2016 with relevant departments and also delivering a series of workshops in certain regional member countries. Staffs attached to field offices have also participated in building additional, front-line support.

Collaboration efforts: The Bank collaborates with other partners (the Multilateral Investment Guarantee Agency, the World Bank, the US Overseas Private Investment Corporation, and USAID) to ensure that PRG and PCG are offered in parallel with other guarantee and insurance products.

Government Consent: ADF guarantees require the consent of the host government in order for the Fund to extend the product to beneficiary projects, particularly since the country provides the requisite counter-indemnity. Accordingly, the Bank is seeking to sensitize authorities in RMCs about the benefits of guarantees and in particular to reassure them that they do not create any additional conditional liability for governments. This has been critical in ensuring their support for related projects.

Constitution of a Guarantee Taskforce: Following the approval of the ADF PRG Framework in 2011, the Bank's Guarantee Task Force was constituted to identify, prepare and support the implementation of ADF guarantee transactions. Given the multidisciplinary and specialist skills required to manage guarantee instruments, the Task Force includes focal points from organizational units responsible for energy, legal services, private sector operations, treasury, environment and social safeguards issues.

Internal capacities: Guarantee instruments are more complex than both sovereign and non-sovereign debt financing transactions. To increase the utilization of the guarantee instruments, it has been necessary to build internal capacity on this form of financing. The Bank currently has professional staff with requisite skills to support the guarantee operations, but scaling up the guarantee portfolio will require hiring new specialized staff as well as training and knowledge transfer for existing staff, through structured in-house courses to broaden the guarantee expertise.

Demand for PRGs

Since its approval in 2011, the PRG has been utilized to support three key private sector operations in the energy sector under PPP structures (Table III-1). PRG's operations success to date is encouraging and can be measured in terms of its (i) outcome, which is the number and volume of PRG operations supported; and (ii) output, which is the volume of guarantees over total project financing or over commercial debt mobilized. As a result of the 4 times leverage factor, the ADF PRGs approved to date have enabled UA 36.4 million of the ADF PBA to guarantee UA 145.6 million and helped catalyse over USD 2.7 billion of investments.

Demand for PCGs

The PCG's leveraging effect is designed to operate by consuming only 1/4 of the face value of the guarantee extended, which is then deducted from the country's PBA. This leveraging effect translates into an increase in the commitment capacity of the Fund by 75% of the face value of the guarantee extended. To date, the PCG has been utilized to support two transactions (Table III-2).

Enquiries have also been received to use the PCG for syndicated loans, in particular from financial institutions seeking to make loans to energy projects and other capital intensive expansion programs of commercially-run SOEs. Additionally, the Bank has been approached by counter party banks, requesting credit enhancement on their derivative transactions, or swaps, with ADF member countries, in order to hedge interest rate and currency risks related to sovereign international bond issues. There is also an emerging interest to use the instrument for non-conventional financing, including for leasing and mortgage-backed securities.

Table III-1: Projects supported by the PRG (May 2016)

Name	Country	Date of Approval	Main Characteristics
Lake Turkana Wind Project	Kenya	October 2013	The ADF is providing a PRG with a face value of UA 17.4 million to cover certain obligations of the Kenyan government and governmental entity in connection with the transaction.
Power Sector Privatization	Nigeria	December 2013	The PRG with a face value of UA 120 million is provided in a programmatic approach, to cover several independent power producers.
Geothermal Development Corporation (GDC) Menengai IPP Project	Kenya	October 2014	PRGs with a total face value of 8.24 million will be extended in support of three IPPs, which won a tender to generate power from the Menengai geothermal field. The program provides guarantees against non-payment under Power Purchase Agreements and Steam Supply Agreements of the Kenya Power Lighting Company.

Table III-2: Transactions supported by the PCG (May 2016)

Name	Country	Date of Approval	Main Characteristics
Economic Management Reform Support Program	Madagascar	March 2016	As a leveraged instrument, only USD 10 million will be deducted from the country's PBA to enable the country accessing USD 55 million loans.
Tanzania Mortgage Refinance Company (TRMC)	Tanzania	May 2016	With a total guarantee exposure of USD 4 million, the PCG will support TMRC to raise long-term funding from the Tanzanian local currency bond markets to local banks for mortgage finance operations.

Pipeline and Pre-Pipeline Projects

There is ongoing demand for the PRG and PCG, with private sector project developers in Ghana⁷, Kenya and Uganda, amongst others engaging the Bank on the possibility of using the guarantees to develop power projects.

While the demand for the PRG has been concentrated in the energy sector, the instrument was introduced during the initial design phases for a range of projects, to encourage its use in different sectors. In fact, the Bank in December 2015 was requested by the Government of Uganda (GoU) to participate in the development and funding of the Kampala-Jinja expressway (toll road) project, which is being structured as PPP. It is expected that the ADF PRG will be utilized to backstop the GoU's obligations under an availability payment structure with the concessionaire. The project is currently under preparation by the Bank. The feasibility of leveraging the financing instruments is also being considered across those non-infrastructure sectors requiring credit enhancement to mitigate government exposure.

⁷ In February 2015, a formal request was received from the Government of Ghana (GoG) for an ADF PRG for the Ghana 1000 Gas to Power Integrated Project, to back the payment obligations of the Electricity Company of Ghana for an exposure of up to \$120 million i.e. UA 85 million. A preparation mission has already taken place to assess the project and collect the necessary documents for a full appraisal of the project. In April 2015, the ADF received another formal request from the GoG for Quantum Power, a gas infrastructure entity, undertaking a liquefied natural gas (LNG) project, involving the installation, commissioning and operation of the infrastructure required to import, store, re-gasify LNG and deliver re-gasified LNG to Ghana National Petroleum Corporation (GNPC), a governmental entity, and the related off-takers. The ADF PRG with an expected face value of UA 53 million will back the payment obligations of the GNPC under a Facilities Use Agreement with Quantum Power. The project is currently under preparation.

Annex IV: Addressing Fragility in the PBA System

The prevailing ADF-13 PBA formula has two main components: need and performance. Needs are captured by: GNlpc; Population (Pop); and infrastructure gap as measured by the AIDI. Performance is captured through the Country Performance Assessment (CPA), which is mainly based on the cluster scores (A, B, C, D, and E) of the CPIA and the PPA. Building on the simulations' methodology presented in the "*Addressing Fragility in the Performance-Based Allocation System*" paper of the First ADF-14 replenishment meeting, this annex provides additional avenues to explicitly address fragility in the PBA by adding a fragility component in the formula. Instead of including a single fragility index, the new component consists of a combination of fragility indices. Thus, a country allocation *A* would rely on three building blocks as follows:

$$A = \text{Performance Component} \times \text{Needs Component} \times \text{Fragility Component} \quad (1)$$

$$\text{where } \text{Performance Component} = CPA^{4.125} \quad (2)$$

$$\text{Needs Component} = GNlpc^{-0.125} \times Pop^1 \times AIDI^{-0.25} \quad (3)$$

$$\text{Fragility Component} = (Index_1)^\alpha \times (Index_2)^\beta \times \dots \times (Index_n)^\gamma \quad (4)$$

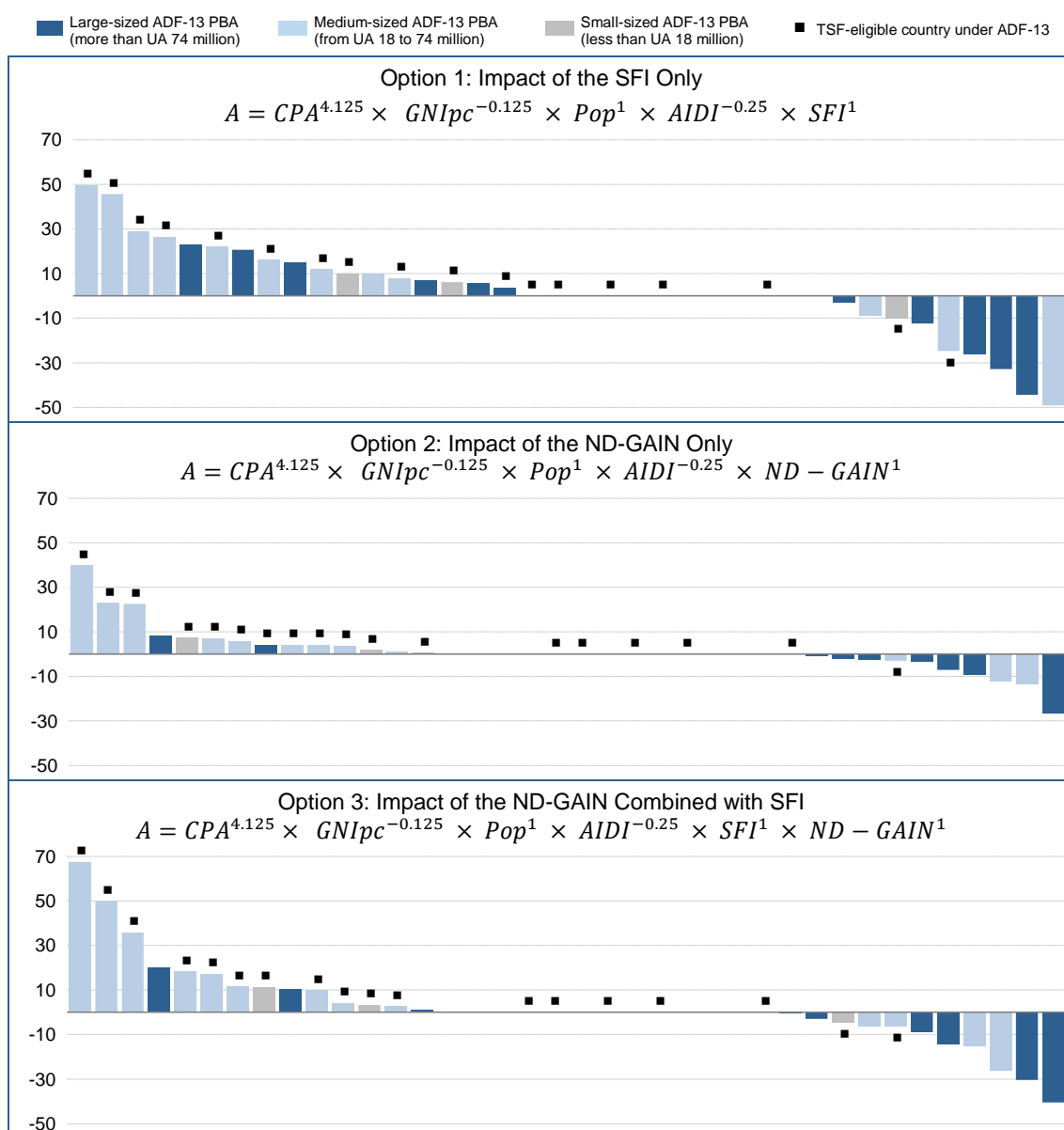
Based on the outcomes of the previous simulations and Deputies' feedback, the State Fragility Index (SFI)⁸ is retained in the current simulations, to which the ND-GAIN index⁹ is added, and potential combinations between the two indices are explored. While the baseline scenario uses the same input and PBA envelopes as ADF-13, the two indices were standardized between 0 and 100 and a 3-year moving average was used to avoid excessive volatility. For the SFI, a range of positive exponents were applied. However, since higher scores of the ND-GAIN translate situations of lower vulnerability, negative exponents were used for the latter. Therefore, three options were explored within the fragility component of Equation (4) as follows:

- Option 1** $\text{Fragility Component} = (SFI)^\alpha$
with $\alpha = \{+0.5; +1.0; +1.5\}$
- Option 2** $\text{Fragility Component} = (ND - GAIN)^\beta$
with $\beta = \{-0.5; -1.0; -1.5\}$
- Option 3** $\text{Fragility Component} = (SFI)^\alpha \times (ND - GAIN)^\beta$
with $\alpha = \{+0.5; +1.0; +1.5\}$ and $\beta = \{-0.5; -1.0; -1.5\}$

⁸ The SFI – produced annually by the Center for Systemic Peace – provides clear, sound, and accessible data for most ADF-eligible countries (except Sao Tomé & Príncipe). It aims at measuring the degree of long and mid-term fragility on the basis of a country's ability to deal with conflict; make and implement public policy; deliver essential services and its systemic resilience in maintaining system coherence, cohesion and quality of life; responding effectively to challenges and crises; and sustaining progressive development. The use of the SFI only in the fragility component of the PBA formula allows reaching relatively comprehensive impacts on resources redirected to TSF-eligible countries while preserving the performance principle and avoiding excessive distortions of the remaining country allocations.

⁹ The ND-GAIN index is produced annually by the University of Notre Dame with accessible data covering most ADF-eligible countries (except Somalia and South Sudan). The index summarizes a country's vulnerability to climate change and other global challenges in combination with its readiness to improve resilience. It is composed of a Vulnerability score and a Readiness score. On vulnerability, it considers 36 indicators structured through six life-supporting sectors – food, water, health, ecosystem service, human habitat and infrastructure. Readiness is measured through 9 indicators structured within three components – economic readiness, governance readiness, and social readiness.

Figure V-1: Individual PBA Variations (Percentage)



While detailed outcomes of explored simulations can be provided separately upon demand, for the sake of simplicity, in what follows, the three options are reported with exponent $\alpha = +1.0$ and $\beta = -1.0$. Figure V-1 shows that impacts of Option 1 and Option 2 on individual allocations – compared to the baseline scenario – are quite similar. In effect, the SFI and the ND-GAIN as well, would increase medium-sized allocations by transferring resources from large-sized ones, while smallest allocations would not be significantly affected. In addition, positive and negative variations in individual PBAs would be similar in absolute terms under these two options. As for countries in fragile situations, 5 TSF-eligible countries would see their allocations unchanged for the two options. While the ND-GAIN would contribute to channel more resources to 12 TSF-eligible countries, the SFI would do the same for 11 TSF-eligible countries. However, the impact magnitude of the SFI is higher with additional resources averaging UA +9.82 million per each TSF country as compared to the UA +4.89 million generated by the ND-GAIN (Table V-1). This is, in part, explained by the overall redistribution effect of the SFI which is around three times higher than the ND-GAIN (UA 212.45 million for the SFI compared to UA 73.76 million for the ND-GAIN).

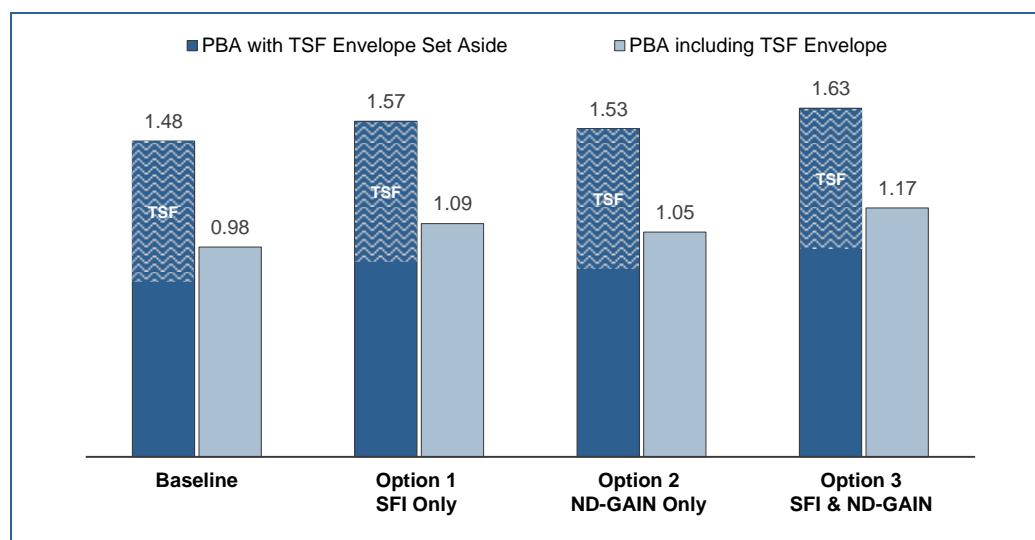
Option 3 combines both the SFI and the ND-GAIN in the fragility component of the PBA formula and, thus, seems to be cumulating the effects of the two previous options. In fact, while the structure of individual PBA variations remains closely similar (with increases in the medium sized allocations and decreases in the large-sized ones),

the overall magnitude of variations is almost equal to the sum of variations generated by Option 1 and Option 2. For instance, the average of positive variations is at +24.7% for Option 3, while the same indicator for Option 1 and Option 2 is at +18.3 and +7.4%, respectively. The same cumulative effect applies for the average of additional resources flowing to TSF-eligible countries, which is scaled up to UA +15.01 million with Option 3. However, while the first two options would secure more than 65% of PBA resources to the first two CPA quintiles of countries, Option 3 is below this threshold with a share of 63.3% (Table V-1).

Table V-1: Key Results of the Explored Simulations

		Baseline	Option 1 SFI Only	Option 2 ND-GAIN Only	Option 3 SFI & ND-GAIN
		ADF-13	$\alpha = 1.0$	$\beta = -1.0$	$\alpha = 1.0$ $\beta = -1.0$
Redistributed resources (UA Million)		NA	212.45	73.76	263.36
Share of PBAs in top 2 CPA quintiles (Percentage)		68.6	65.3	65.8	63.3
PBAs to TSF countries (UA Million)		816.39	908.16	872.91	968.95
Share of PBAs to TSF countries (Percentage)		27.4	30.6	29.4	32.8
Impact on TSF countries whose PBA increase	No.	NA	11	12	11
	UA MM	NA	+9.82	+4.89	+15.01
Impact on TSF countries whose PBA decrease	No.	NA	2	1	2
	UA MM	NA	-8.12	-2.14	-6.25

Figure V-2: Simulations of Resources Flowing to TSF-Eligible Countries (UA Billion)



In the case of the proposed options, we also considered for each, a second round of simulations where the expected ADF-13 TSF envelope (UA 661.80 million) is added to resources available for allocation under the PBA framework. As shown in Figure V-2, for the three options, this would not help to channel more resources to TSF-eligible countries. Within this assumption, the total PBAs flowing to TSF-eligible countries could be raised, from UA 0.98 billion under the baseline scenario, up to UA 1.17 billion under Option 3, which combines both impacts of the SFI and the ND-GAIN. Meanwhile, in none of the explored options would more resources be allocated to TSF-eligible countries than in the current configuration where the TSF is considered as a set aside envelope. For instance, with Option 2 and Option 3, TSF-eligible countries would likely to be losing UA 483 million and UA 466 million, respectively, of their ADF resources.

Annex V: RMCs Identified in the FY16 MDB Harmonized List of Fragile Situations

Country ^a	2014 World Bank CPIA	2014 AfDB CPIA	Harmonized Average	Political & Peace-building Missions ^b	Peace-keeping Missions ^c
ADF-Eligible Countries					
1 Burundi	3.27	3.38	3.32	■	
2 Central African Rep.	2.43	2.28	2.36	■	
3 Chad	2.69	3.24	2.97		
4 Comoros	2.72	2.47	2.59		
5 Congo Democratic Rep.	2.98	3.30	3.14		■
6 Cote d'Ivoire	3.25	3.50	3.37		■
7 Eritrea	1.99	2.14	2.07		
8 Gambia	3.14	3.21	3.17		
9 Guinea-Bissau	2.50	2.67	2.59	■	
10 Liberia	3.10	3.50	3.30		■
11 Madagascar	3.13	3.20	3.17		
12 Mali	3.37	3.65	3.51		■
13 Sierra Leone	3.27	3.37	3.32	■	
14 Somalia		1.11	1.11	■	
15 South Sudan	2.00	2.22	2.11		■
16 Sudan	2.43	2.56	2.49		■
17 Togo	2.99	3.20	3.10		
18 Zimbabwe	2.7	2.2	2.4		
ADB Countries					
19 Libya	-	-	-	■	

Source: MDB Harmonized list of fragile situations FY16

^a As compared to the FY15 harmonized list, Gambia has joined the FY16 list. Three countries, Guinea, Malawi and Niger, are not in the FY16 harmonized list. Pending publication of the FY17 updated list, these countries would merit a qualitative assessment.

^b Specifically defined as the presence of a UN and/or regional (e.g., AU, EU, OAS) peace-building and political mission in this country in the last three years [sources: UN DPKO, AU, EU websites].

^c Specifically defined as the presence of a UN and/or regional (e.g., AU, EU, OAS, NATO) peace-keeping operation in this country in the last three years, with the exclusion of border monitoring operations [sources: UN DPKO, AU, EC, websites].

Annex VI: Two-Stage Eligibility Criteria for TSF Pillar I

Stage 1 Eligibility Criteria	
Commitment to consolidate peace and security	<p>To demonstrate commitment to consolidating peace and security after crisis or conflict, the country should have:</p> <ul style="list-style-type: none"> • Signed comprehensive and internationally recognized peace agreement or a post-crisis or reconciliation agreement, and no ongoing hostilities of any significance or • On the basis of a broader assessment of the degree to which the authorities , have developed and followed through on post-conflict or crisis programs to address the roots of fragility and conflict, as the degree of international support they have garnered for these efforts. • A functioning governmental authority or transitional government broadly acceptable to stakeholders and the international community. <p>Evidence of government’s commitment in this regard may include, among others, progress towards and/or approval of new national constitution; and progress towards normalizations of relations with the international community (key regional bodies such as the AU and economic communities and/or international institutions).</p>
Unmet social and economic needs	<p>Post-crisis and transitional states are considered to face a uniquely challenging combination of circumstances demonstrated by:</p> <ul style="list-style-type: none"> • Continuing severe economic difficulties caused by conflict, as evidenced in contraction of real gross domestic product (GDP) per capita by 5% or more between 1995 and 2014. • Extremely low levels of human development as indicated by the country’s rank in the bottom quintile of the UNs’ Human Development Index (HDI). <p>The GDP and HDI criteria shall be complemented by a targeted assessment of the impact of recent crisis on economic and social conditions, as well as the spill- over effect of conflict at the sub-national and regional levels.</p>
Stage 2 Eligibility Criteria	
Improved macroeconomic conditions and sound debt policies	Assessment of a country’s program to improve its macroeconomic performance and debt management policy should be conducted in close collaboration with other partners and based on key performance benchmarks used to guide engagement and assess the country’s progress over the medium term.
Sound financial management practices	Assessment of a country’s commitment to pursue sound public financial management practices should be based on progress in reforming its public expenditure management system, addressing corruption seriously and reviving or strengthening its revenue mobilization institutions.
Transparent public accounts	Monitoring of the transparency of public accounts should assess the regularity of reports or publications on government revenues and expenditures, external debt obligations and new borrowings.

Annex VII: TSF Pillar I Resource Allocation under ADF-14

Country	PBA	Discount							Top-Up Multiplier		TSF Pillar I Allocation	
	"High 2" ADF-13 Basic Alloc.	Harmonized CPIA (AfDB/WB)	Applied Discount (%) ^a	GNIpc, PPP (Avg. 2012-14)	Applied Discount (%) ^b	Engagement Year	Applied Discount (%) ^c	Total Discount (%)	Applied top-up factor	Alloc. with top-up ^d	After Discount	Final Allocation
1 Burundi	43.52	3.32	10	750.00	20	2004	30	60	1.5	65.28	26.11	26.11
2 Central African Rep.	6.58	2.36	-	706.67	20	2006	30	50	1.5	9.87	4.94	10.00
3 Chad	50.03	2.97	-	2,000.00	30	2015	-	30	2.0	100.05	70.04	60.00
4 Comoros	0.75	2.59	-	1,406.67	30	2007	30	60	1.5	1.12	0.45	10.00
5 Congo Democratic Rep.	301.25	3.14	-	630.00	20	2004	30	50	1.5	451.88	225.94	60.00
6 Guinea-Bissau	3.02	2.59	-	1,370.00	30	2004	30	60	1.5	4.53	1.81	10.00
7 Liberia	22.77	3.30	-	693.33	20	2007	30	50	1.5	34.15	17.07	17.07
8 Madagascar	81.30	3.16	-	1,373.33	30	2014	-	30	2.0	162.60	113.82	60.00
9 Mali	95.72	3.51	10	1,453.33	30	2014	-	40	2.0	191.43	114.86	60.00
10 Sierra Leone	27.70	3.32	10	1,663.33	30	2004	30	70	1.5	41.55	12.46	12.46
11 Somalia	0.43	1.11	-	-	-	2014	-	-	2.0	0.86	0.86	10.00
12 South Sudan	13.39	2.11	-	1,796.67	30	2012	-	30	2.0	26.79	18.75	18.75
13 Sudan	62.53	2.49	-	3,816.67	30	2014	-	30	2.0	125.06	87.54	60.00
14 Togo	25.88	3.10	-	1,193.33	30	2008	30	60	1.5	38.82	15.53	15.53
15 Zimbabwe	17.15	2.43	-	1,603.33	30	2014	-	30	2.0	34.30	24.01	24.01
15% Unused Reserve (UA million)											80.11	
Total TSF Pillar I Envelope (UA million)											534.05	

^a A 10% discount is applied if a country has its latest AfDB/WB CPIA score greater than 3.3.

^b A 20% discount is applied if the GNI pc (purchasing power parity) of a country is greater than 500 USD. If it is greater than 1,000 USD, the applied discount is 30%.

^c A 30% discount is applied if the length of TSF re-engagement of a country (including engagement under the Post-Conflict Country Facility) is greater than 5 years.

^d A top-up multiplier factor of 1.5 is applied if a country is receiving TSF Pillar I resources for the third cycle. Otherwise, a factor of 2.0 is applied.