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MEMORANDUM

TO : THE BOARDS OF DIRECTORS

FROM : Modibo I. TOURE
Secretary General

SUBJECT : TOWARDS A MEDIUM-TERM BANK GROUP STRATEGY*

Please find attached hereto, the above-mentioned document.

Attach:

cc: The President

***Questions on this document should be referred to:**

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SCCD:C.H.

AFRICAN DEVELOPMENT
BANK GROUP

TOWARDS A MEDIUM-TERM STRATEGY

2 FEBRUARY 2008

Executive Summary

This paper is intended to provide the basis for an initial discussion on the African Development Bank Group's (the Bank or Bank Group) Medium-Term Strategy (MTS) rather than a first draft of the final product. It rests on policy and resource decisions already agreed by the Board, and takes account of the conclusions of the eleventh replenishment of the African Development Fund (ADF) and the commitments made. It is consistent with the thrust of the High Level Panel Report on the long-term direction of travel for the Bank; however it does not make any judgment on the specific proposals made by the Panel. These will be discussed at a later stage in the light of recommendations to be made by the President to shareholders.

The paper considers the current positioning of the Bank within a changing international aid architecture, and against the primary needs of its African clients. Its starting position is that the Bank must remain relevant to all its Regional Member Countries (RMCs). It suggests that the Bank should be judged by results, the contribution it makes to development and the reduction of poverty, in particular by promoting growth and economic integration.

The paper proposes greater selectivity with operational focus on: infrastructure; building capable states (by tackling fragility and promoting governance); private sector operations; higher education, technology and vocational training. The paper makes clear that through these areas the Bank will contribute directly to broader human development objectives, agriculture and climate change.

The paper argues that the Bank must complement operational selectivity by focusing on cross-cutting improvements in the quality and effectiveness of its products and services and their delivery; by better leveraging its core assets; and increasing focus on results and results measurement. Within these three areas are a variety of more specific actions to be undertaken. It assumes further improvements in the way the Bank functions, and in its internal integration and coordination. It outlines how the Bank will strengthen the dialogue in country, and improve its internal business and HR processes. It will build the Bank's capacity to deliver, including by strengthening its knowledge and expertise so that it becomes a first call for advice to its RMCs. It will continue to decentralize and will draw on an analysis to be prepared during the MTS period to refine its approach. It will better leverage its financial strength, putting the Bank's balance sheet to work in a manner that is consistent with safeguarding financial integrity and its triple-A credit rating.

Some tentative financial scenarios are provided, extrapolating from the current position in the three component parts: African Development Bank sovereign lending; private sector; and, ADF. These indicate potential orders of magnitude, recognizing that the first two are essentially demand driven and therefore will depend on the attractiveness of the products and services provided. It recognizes that delivering on the MTS program will require more human and financial resources, particularly to drive better portfolio management and results measurement, knowledge activities, decentralization, and upgrading staff skills. The scenarios indicate that these increases would be affordable.

The MTS will be elaborated in the light of guidance from the Boards. It would be helpful therefore to focus discussion at this stage on: the shape of the final product; those areas for further analysis and discussion; and the degree of specificity required, recognizing that the Medium Term Strategy will be underpinned by annual and rolling multi-year budget and operational plans.

Acronyms and Abbreviations

ADB	African Development Bank
ADF	African Development Fund
AU	African Union
CSP	Country Strategy Paper
DAC	Development Assistance Committee (OECD)
EC	European Commission
ESW	Economic and sector work
FDI	Foreign direct investment
GDP	Gross domestic product
HR	Human Resources
ICA	Infrastructure Consortium for Africa
IFAD	International Fund for Agricultural Development
KPIs	Key Performance Indicators
M & E	Monitoring and evaluation
MDGs	Millennium Development Goals
MICs	Middle-income countries
MLTSF	NEPAD Medium- to Long-Term Strategic Framework
MTS	Medium-Term Strategy
NEPAD	New Partnership for Africa’s Development
NGOs	Non-governmental organizations
OECD	Organization for Economic Co-operation and Development
PCR	Project completion report
PPPs	Public-private partnerships
RECs	Regional economic communities
RMCs	Regional member countries
RSDIP	Regional Spatial Development Program
SMEs	Small and medium-sized enterprises
STAP	NEPAD Short-term action plan
UA	Unit of account
UNECA	United Nations Economic Commission for Africa
US$	United States dollar

TOWARDS A MEDIUM-TERM STRATEGY

1. Purpose and Approach

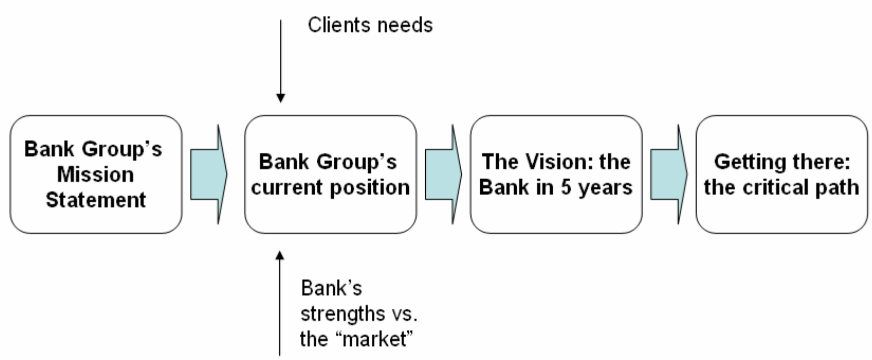
Purpose

- This document has been prepared as the basis for an informal discussion with the Boards intended to highlight the key medium-term directions for the African Development Bank Group (the Bank or Bank Group). It is work in progress and, in the light of guidance from the Boards, will be followed by a fuller draft of the Medium-Term Strategy (MTS).

- It outlines a proposed strategy based on an analysis of client needs, the Bank's internal strengths, and the evolution of the aid landscape. It also proposes specific ways to operationalize this strategy.

Approach

- This outline is organized as follows:



2. Bank Group's Mission Statement

- The Bank Group's mission statement will be set out in the MTS. It must underline the importance of the Bank being, and remaining, relevant to all its Regional Member Countries (RMCs).

- As a starting point this document uses a mission statement that is consistent with both Article 1 of the Bank's charter and that suggested by the High Level Panel: "poverty reduction and development through growth and economic integration." In other words to help Africa rid itself of deep poverty, and provide its people with opportunities to prosper and live lives of dignity and promise. To achieve this, the Bank will help Africa to diversify, to become competitive, integrated, globally connected, and increasingly self-financing.

3. Bank Group’s Current Positioning

African Development Performance

- By many important measures, Africa’s development prospects have improved substantially, with recent growth performance the best in decades. Faster growth has been driven by macroeconomic reforms, including stronger public finances, and a consequent improvement in the investment climate. A favorable global economy, with high demand for African primary commodities, has also been a key driver.

- Yet poverty remains pervasive, human development indicators remain among the lowest in the world, and far too many people have far too few opportunities to build healthier and more prosperous lives. Thus the overall picture in Africa remains mixed.

Progress	Room for Improvement
▪ Growth ▪ Improving political context ▪ Improved financial market access for some MICs ▪ Better investment climate ▪ Keen donor interest ▪ More capable development partners	▪ Poverty levels ▪ Income equality and inclusive development ▪ Limited regional and continental integration ▪ Diminishing global trade share ▪ Low levels of investment and savings

- Africa faces many challenges including marginalization in global trade and investment flows; small, fragmented economies characterized by low economic productivity due in part to poor infrastructure; weak government institutions; a relatively high number of fragile and post-conflict states; persistent disease; and climate change. At the same time, if these primary challenges can be overcome globalization presents Africa with unprecedented opportunities to grow and modernize. In this context, the needs of the Bank’s clients’ are changing fast.

What our Sovereign Clients want

- Against this background of generally strong growth across Africa recently, levels of economic and social development at the country level, as measured by per capita GDP, are diverging, not converging. As a result, country clients needs are very different:

  – **Middle-income countries (MICs)** have made progress but have to be able to compete in a global market place, increasingly without protection from trade preferences. To do so they want to enhance economic competitiveness, increase productivity notably by improving infrastructure, their knowledge base and human capital. At they same time they want to continue to fight pockets of exclusion and poverty. They want access to services and products better tailored to their needs.

  – **Low-income countries** are becoming increasingly diverse; some are making good progress and aspiring to MIC status, while others are advancing more slowly. Some are benefiting from high commodity prices and will want to use revenues wisely to upgrade their infrastructure, diversify their economies, and avoid the “resource curse”. All need to invest significantly to improve the competitiveness and diversification of their economies to better withstand external shocks. All also need significant investments to build institutional capacity and deal with disease and climate change.

  – **Post-conflict and fragile states** need special attention and dedicated resources. They want to make progress on stabilization and basic macroeconomic reforms, paving the way for debt relief and reengagement with the international donor community. They need significant and sustained assistance to rebuild core institutions and rehabilitate vital services and basic infrastructure.

What our Non-sovereign Clients want

- The Bank also serves private sector and non-sovereign clients, who have identified three broad needs:

  – Advice – providing expertise, in particular when it comes to packaging and syndication.

  – Finance – to fund specific transactions. Loans must be competitive, with the lowest possible rates, longest possible maturities, and minimum delays. Demand for equity and quasi-equity investments is also growing.

  – Risk mitigation – Investors are looking for reassurance that their interests are adequately protected from political interference and that governments respect their contractual obligations.

Financing Context: Development finance trends

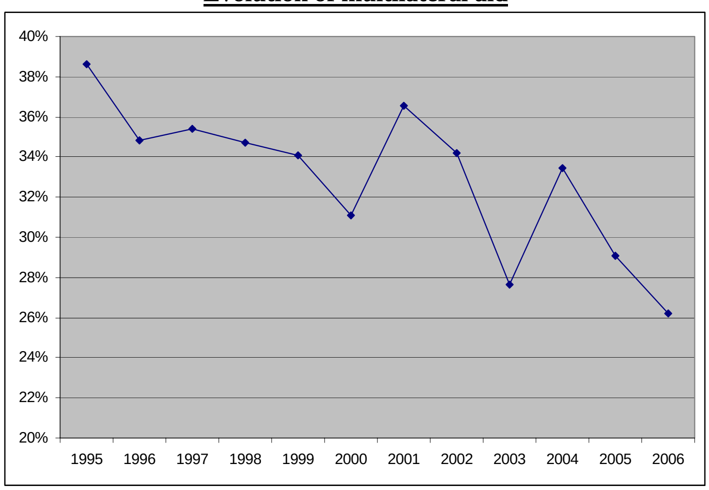
- The international community is giving Africa more concerted attention: traditional donors have promised a major increase in aid, new donors are emerging and private investors, though still focused primarily on natural resources, are increasingly considering opportunities in Africa. Capital markets are showing greater appetite for African debt.

- Growth in aid to Africa is coming mostly from **bilateral** sources, but much of that increase is in the form of emergency or humanitarian aid, or in debt relief. There has been little real growth in the resources made available in country for investment in capacity building, basic infrastructure or services. Multilateral aid has decreased as a percentage of overall aid over the last 10 years, from more than one third of total aid in the mid-1990s to about one quarter currently.

- Recent years have seen a **marked increase in the number of donors** – public bilateral, multilateral and private. The increase in bilateral donors has been driven by the emergence of **non-traditional donors** from the Middle East and developing countries such as China, India and Brazil engaging increasingly with Africa in "South-South" cooperation. Large amounts of financing available from alternate sources have been put at the disposal of resource-rich countries aiming in particular at developing their resource exploitation and trade. This financing is often provided with fewer conditions.

- **New multilateral donors** have also appeared, predominantly highly focused vertical funds targeting specific issues such as health and environment.

<u>Evolution of multilateral aid</u>



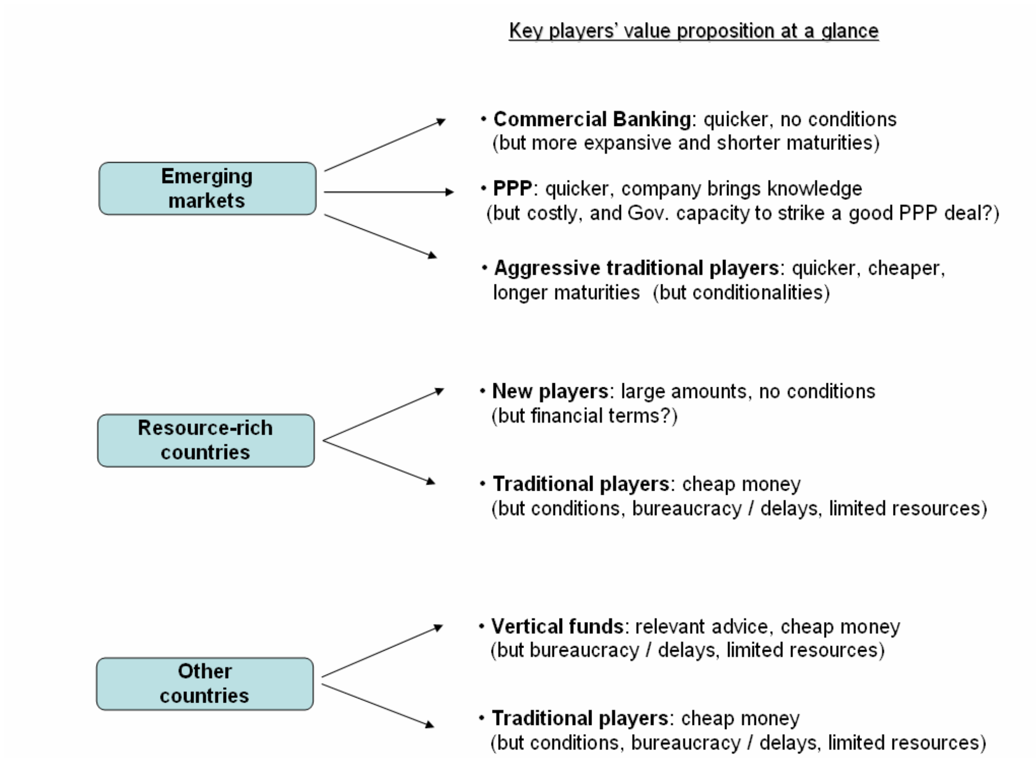
Source: DAC/OECD

- **Private foundations** have also gained in influence and importance while a plethora of NGOs remain active across the full range of sectors.

- The last two decades have seen a significant shift in the developed and developing countries alike towards **more mobilization of the private sector in particular for provision and financing of infrastructure**. Africa compares weakly to other developing regions, though reflects the same phenomenon. The limited scale of these types of investment in the continent reflects the often small profit margins on offer when set against long-term political risk and regulatory instability concerns. Mitigation instruments developed by bodies such as MIGA have helped, but have not brought about wholesale change in the levels of private investment. It is encouraging that in 2005 foreign direct investment (FDI) flows to Africa surged to an historic level of US$31 billion, up from US$17 billion in 2004. It remains to be seen whether this trend is confirmed, and distribution remains extremely uneven across countries. However, the greater presence and level of interest of the FDI community in Africa is a major and important opportunity.

- There has been a massive increase globally in foreign investment, but very little of it has gone to Africa outside of the resource rich economies, and very specific sectors. **Emerging countries have turned more and more to commercial banks to finance their growth**, ready to borrow at a higher rate in exchange for no conditionality and quick processing times. But current turbulent market conditions and the wider global experience to date underline the volatility of these flows.

- In response, **some "traditional" donors have pursued a more aggressive strategy** in emerging markets, by cutting rates or improving delivery speed.



- At the same time, development finance has become more **fragmented**, characterized by a higher number of independent operations of relatively small size. In many cases, aid is being delivered through less flexible instruments such as technical assistance, emergency relief or in tied forms that give countries little say in its use.

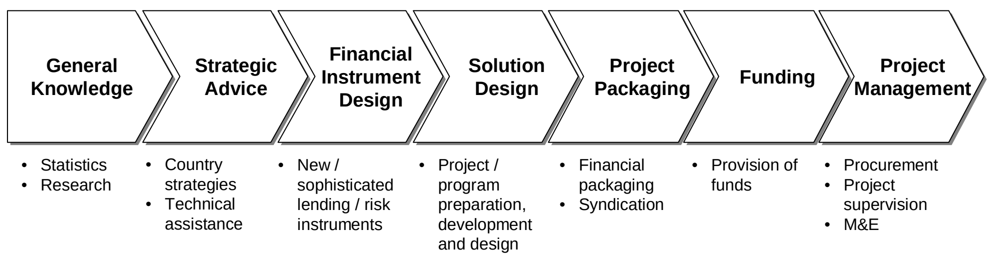
- These trends have implications for beneficiaries and donors. More aid channels and increasingly fragmented instruments have put pressure on recipients to effectively manage aid. This task has proven particularly difficult for poor countries with weak institutional capacity and has generally increased transaction costs for beneficiaries and donors. To counteract these trends, donors are under pressure to be increasingly selective in their interventions and to improve their own coordination, partnership and harmonization. At the same time, to respond to increasing client differentiation, donors must increasingly develop tailor-made solutions (i.e., remaining relevant to MICs, enhancing support to fragile and post-conflict states). There is urgency for all multilaterals to deliver more effectively, and to demonstrate convincing results.

The Bank Group's positioning

Areas for improvement…

- The Bank is currently present all across the development banking value chain and upstream in knowledge generation and promotion. As a result, it may be stretched too thin at a time when many players are becoming more specialized and may not currently have adequate resources to be an effective full-service provider.

Simplified value chain



- The Bank has a mixed record in impact and results. It has been too bureaucratic, inflexible and remote in past. Comparing MDB project life cycles shows that the Bank is making progress but remains slower than the World Bank and other regional banks. The execution of reforms to address these shortcomings is major and urgent work in progress.

- The Bank Group is **small relative to the scale and scope of the development challenge in Africa**. It is the seventh largest provider of aid to Africa and the African Development Fund (ADF) has consistently accounted for only about 3-4% of total aid to Africa. This pattern holds true across most sectors, particularly in health and education, where bilaterals dominate (DAC bilaterals account for roughly 70% of all aid to Africa for health and education) and the Bank is a marginal financier.

…And strengths to build on

- **Small size can also be seen as an asset**, making it easier for the Bank Group to be fast, more flexible and proactive vis-à-vis clients, and more selective. It has the advantage of having integrated non-sovereign and private sector lending, in principle providing a greater ability to tailor engagement to country needs.

- **Position as Africa's Bank:** it is the only multilateral focused exclusively on the Continent; its ownership structure provides for "equal voice" of the RMCs and promotes perception as the "RMCs' bank"; its distinct African character (i.e., ownership structure, African president and predominantly African staff) confers legitimacy and an ability to play the "honest broker" role. As a major Pan-African organization, the Bank is well positioned to build effective, credible partnerships with other African institutions.

- The Bank is better recognized for its relatively **strong performance in certain areas**. It has therefore been entrusted with leadership in key continental initiatives: implementing AU/NEPAD programs in infrastructure, regional integration, and economic governance; as host for the Infrastructure Consortium for Africa, African Water Facility, and African Fertilizer Facility. The

Bank can increasingly use the “space” and “platform” these initiatives provide to demonstrate excellence and results at both country and multi-country/regional levels.

- **Growth in private sector development activity –** There has been a step change in the level of direct private sector financing in 2007. The strong pipeline of projects and increasing demands for Bank Group participation highlights significant opportunities for growth and for public-private synergies.

- **Organized for improved country focus and greater sector depth –** The 2006 restructuring has created stronger country and regional departments to drive country focus while sector departments have been merged to provide depth. New departments were created to provide focus and capacity for emerging priorities (i.e., governance, regional integration).

- **Strengthened managerial and staff capacity** – In 2006-07, the Bank undertook a major recruitment campaign attracting a significant number of new managers and professionals, primarily in operations and direct operations support to significantly expand capacity to deliver programs. A revamped and expanded program for young professionals was re-launched in 2007.

- As a result of past reforms, the African Development Bank (ADB) has a **strong balance sheet and conservative risk exposure**. Reviews are underway to examine whether this strength could be better leveraged to provide greater support to MICs and the private sector, consistent above all with maintaining the Bank’s triple A rating.

Challenges…

- **Positioning in an increasingly crowded field:** The Bank’s added value could be called into question in many of its present operations. As previously mentioned, it is present as a small player across a wide range of development activities. The Bank is neither the biggest operator, nor the most specialized. It has not yet developed a strong name for itself in research/knowledge. Africa is attracting new commercial and public financiers, including specialized dedicated funds and foundations. This positioning as a generalist, but without the scale of human and financial resources of other generalists, may not be tenable.

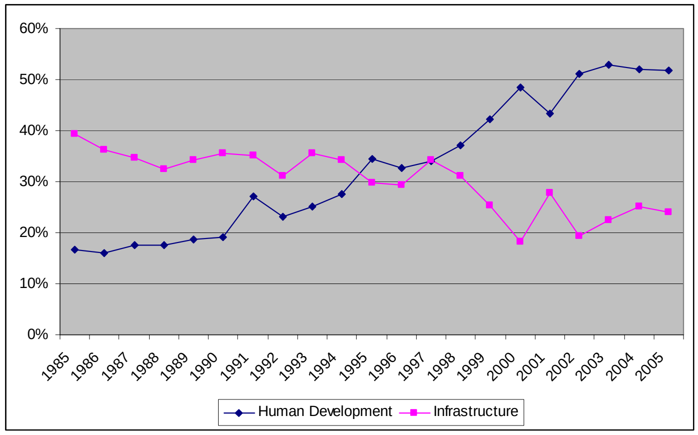
- **Deeping reform:** The Bank’s ongoing reforms have generated momentum but remain a work in progress. The Bank will need to deepen the momentum and fully implement reforms to achieve improved results and outcomes and position itself to play a bigger role in the future.

- **Adding value for MICs:** Many MICs have improved their access to the global capital markets at competitive rates, and their demand for loans from IFIs has fallen. Many are also adopting more active debt management strategies and prepaying old, more expensive loans. Nonetheless, MICs are an important constituent and would like to benefit from improved Bank support to address remaining challenges. Interest and fees from sovereign loans to MICs are a key component of the Bank’s income.

…And Opportunities to seize

- **Enhanced focus/growth in infrastructure lending –** The Bank can fill key gaps in the international aid architecture. As shown below, financing for infrastructure has declined significantly, particularly from bilateral donors. Financing for regional projects also remains low. The Bank has positioned itself well to play a greater role in infrastructure and regional operations.

Official development assistance for Africa



Source: DAC/OECD

- The Bank Group can also build on its **integrated structure** as a source of advantage: it is well placed to build synergies across public/private sectors and foster Public-Private Partnerships (PPPs). There are also vital and underdeveloped synergies between the Bank's core focus and critical other areas such as the agriculture and social sectors.

- **ADF-11 replenishment:** The strong ADF-11 replenishment will allow the Bank to expand its lending, including for regional projects that support integration and enhanced support to fragile states. Strong delivery on ADF-11 commitments is needed to position the Bank effectively for further increases under ADF-12.

4. The Bank Group in 5 Years

Core Objective

- The Bank will be recognized globally and sought after within Africa as a preferred partner demonstrating that it provides high-impact, well-focused development assistance and solutions. Results will be evident. It will have moved towards its longer term vision of being a premier development institution for Africa.

Business model

- The Bank will focus on poverty reduction, primarily by supporting the drivers of improved and more equitable growth, opportunity and economic integration.

- Its operations will be focused on: infrastructure, building capable states and improving governance, private sector operations, higher education and technology and vocational training.

- Through these operations it will contribute materially to improvements in the MDGs relating to health, education and gender.

- The Bank will be an effective and respected voice for Africa internationally and within Africa on development issues.

- The Bank will provide high quality services across its RMCs, and to both public and private sector clients.

- The Bank will demonstrably improve its effectiveness, focusing particularly where demand is strongest, its strengths are clear, and its impact will be greatest.

Implications

- **Medium-term objective:** Fully realizing its vision is a longer term proposition. During the MTS period, the Bank Group will build further on established foundations of reform, results and selectivity, emphasis on execution, delivery, and focus, and institutional momentum to take a significant step towards achieving this vision. The current reforms take account of lessons learned during the implementation of the first MTS and have been described in detail in *"Enhancing the Effectiveness of the Bank"* (ADB/BD/WP/2006/18/Rev.1). The MTS builds on these reforms and extends them over the next five years.

- **Operational focus**: Greater selectivity and focus at the sectoral level is required to: leverage the Banks' limited resources more effectively; produce demonstrably superior results; and earn a position of acknowledged leadership at the country level and within the donor partnership. A more selective operational focus has been set out in the Bank's annual operational program, in individual Country Strategy Papers, and in the operational framework for the ADF-11 Replenishment. The Bank's selective operational focus will be along the following lines:

  - **Infrastructure** - An increasing proportion of the Bank's new commitments and outstanding portfolio will be in basic infrastructure investments, especially transport, power, water and sanitation, and communications. The Bank will actively seek to ensure that these investments benefit both rural and urban populations by improving growth, productivity, employment and access to market opportunities and essential services, particularly those required for accelerated progress toward the MDGs. The Bank will show visible leadership in the continental initiatives (NEPAD, ICA). Infrastructure is defined in its broadest sense with clear linkages to other sectors, particularly agriculture where the Bank will contribute through irrigation, rural roads, marketing and storage facilities, etc. Linkages to and impact upon key cross-cutting issues such as gender and environment will be more systematically developed and assessed

  - **Building Capable States -** the Bank will enhance its engagement in fragile states. It will assist fragile states to transit out of fragility, help prevent slippage in countries at risk, and assist countries in post-crisis and post-conflict transition move forward towards more stable political and economic development.

  - **Governance** – The Bank is uniquely positioned and firmly committed to deliver deeper operational engagement to strengthen governance in several key areas linked directly to its other operational priorities.The Bank will focus on strengthening transparency and accountability in the management of public resources, at the country, sector and regional levels, with a special attention to fragile states and natural resources management. As an African institution, the Bank is uniquely positioned to address these challenges and make a clear contribution. The choice and mix of instruments will be tailored to country circumstances, combining budget support, institutional strengthening projects, non-lending operations and analytical and advisory work.

  - **Private Sector Operations –** The Bank's recent update of its Private Sector Strategy sets out specific commitments for its work in this priority area going forward. Transactions will be further scaled up in the context of: greater linkage to country strategies; developing synergies with other Bank departments (e.g., working with agriculture to develop agribusiness and fisheries); clearer articulation of the "development case" and expected results; and, greater diversity with respect to sectors and partners. Operational focus will be on infrastructure, industry and services, financial intermediation and microfinance / SMEs.

  - **Higher education, technology and vocational training –** The Bank will invest in upgrading and rehabilitating existing facilities including national and regional centers of excellence to provide quality tertiary level training to improve the conditions for scientific and technological innovations. It will develop partnerships with the private sector to design and implement projects to sustain economic and social growth in the RMCs. The Bank will support technical and vocational education and training operations to build skills to address chronic high unemployment.

- **The Bank's contribution to agriculture -** Agricultural development and productivity, and food security, remain critical for Africa. The Bank will make a major contribution through its core areas of operational focus, for instance through provision of rural infrastructure, water and water management, through private sector interventions, and by working in partnership with others. The joint Bank Group/IFAD evaluation of aid to agriculture will report in 2008, and Bank policies and programs will be reviewed to take account of its findings.

- **The Bank's contribution to human development outcomes -** Sustained progress on the health MDGs will be impossible without adequate investment in health systems, including human resources, physical infrastructure, access to clean water and sanitation, proper financial management and accountability. The Bank intends to remain directly engaged in the social sectors, managing more effectively its large portfolio so as to produce better results, but making new commitments on a substantially more targeted and selective basis. The Bank would expect new operational commitments in the social sectors to remain broadly at current levels in nominal terms. To contribute more selectively, the Bank will:

  – Increasingly create and better exploit opportunities to link human development objectives with core operations in infrastructure, such as water and sanitation and power infrastructure that contributes to health and education, and roads to improve rural access to markets and social infrastructure.

  – More systematically target and more effectively monitor social benefits and impacts as part of core project design, supervision and reporting.

  – Develop more innovative and effective partnerships with highly focused and capable service providers including by leveraging its increasingly effective field presence and core investment activity, and through cooperative activities.

- **The Bank Group and Climate change -** The Bank will invest to develop its internal capacity to play a more meaningful role in addressing the climate change challenge in Africa. It will mainstream an integrated approach to climate change and development. Internal skills improvements will be essential as will better integration of climate-related perspectives and issues into the operational cycle. The Bank will focus specifically on:

  – Clean energy investments, adaptation and climate proofing Bank investments;

  – Better management of Africa's lakes, forests and river basins;

  – Promoting carbon offsets where appropriate, including in private sector operations;

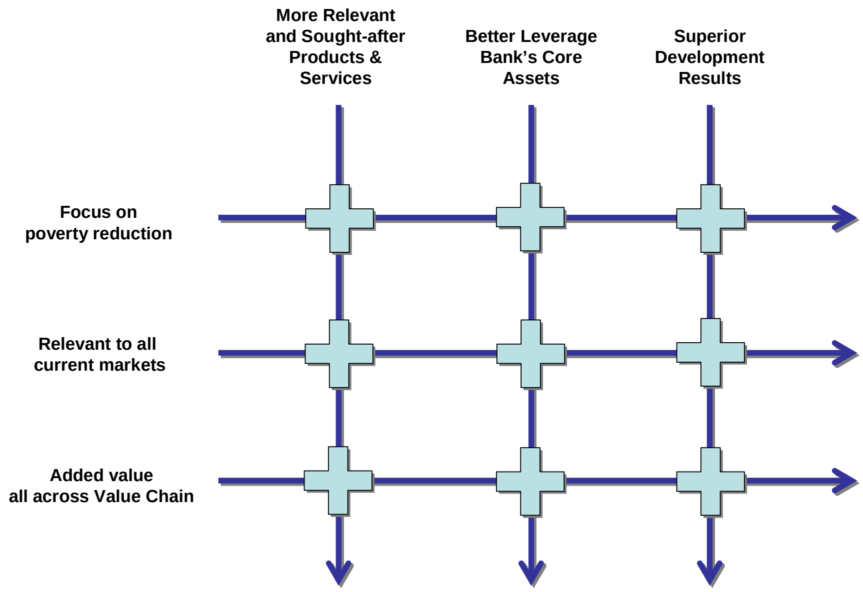
  – Ensuring deep and effective collaboration with the wider community of actors engaged in the climate change effort, drawing actively from the global knowledge pool so that RMCs can access high-quality advice and analysis.

- **To complement greater operational focus,** the Bank will undertake priority actions over the next 5 years to achieve 3 key objectives:

  – Provide more relevant and sought-after **services more selectively.**

  – Build upon and better leverage the **Bank's core assets.**

  – Produce and better demonstrate superior **development results.**



- These priority action areas capture the core of the Bank's strategic and operational focus through 2012. They:

  – reflect the current context and emerging challenges and opportunities for both Africa and the Bank;

  – flow from and build upon already agreed policies and strategic directions;

  – are operationally relevant across the full range of the Bank's Regional Member Countries; and,

  – are deliverable, monitorable, and engage the entire organization.

- The sections below set out for each Priority Action Area the Bank's broad commitments, together with specific measures, initiatives, deliveries or requirements needed for their achievement. The priority action areas are inextricably linked, with clear achievement in each necessary to accomplish the others, and with some specific actions and commitments necessarily common to several objectives.

More relevant, sought-after products and services, provided more selectively

- Provision of **more relevant and sought-after products and services** must be rooted in the following:

  – Greater selectivity at the sector level according to the areas of operational focus described above;

  – A stronger and more operationally selective country focus;

  – Deeper, more effective support for Fragile States and regional integration;

  – A more client-responsive engagement in MICs;

  – Improved products and improved delivery;

  – Effective partnerships in support of harmonized and selective engagement.

- **Stronger and more operationally selective country focus** captured in a new generation country-owned strategies, focused more effectively on the drivers of growth and development:

- – Increasingly produced jointly with key partners, and reflecting more active engagement at the country level;
- – Clear results focus with monitorable benchmarks linked meaningfully to projected operational activities;
- – Operational focus set out with clarity and specificity, limited to at most 3 sectors;
- – Key cross-cutting issues systematically addressed including Private sector development and synergies; Agriculture, Natural Resources Management, Social and Human Development; Gender, Environment and Climate Change; and knowledge Activities.

▪ **Deeper and more effective support of Fragile States:** The emergence of numerous RMCs from periods of conflict and decline creates both unique opportunities and a compelling case for renewed and deeper Bank engagement. The Bank's new Fragile States Facility sets out a comprehensive operational and financial framework through which to provide more effective support for these countries, and for other fragile states. Its key elements are:

- – Supplemental ADF funding (beyond normal allocations) for priority investments in selected post-conflict countries;
- – An improved mechanism for arrears clearance for eligible countries;
- – Targeted capacity-building support for a wider range of fragile states;
- – A clear performance assessment mechanism.

▪ **Deeper regional integration** within Africa is imperative to build markets and new opportunities for growth, job creation and improved living standards; to create more robust, competitive and diversified economies; and, to attract and reward new sources of investment finance. The Bank's member countries believe it is uniquely positioned to make a major contribution to these priority objectives. The Bank's new Strategic and Operational Framework for Regional Operations provides the basis for significantly expanded Bank support for operations to deepen cross-border economic, commercial and policy linkages. Its key elements are:

- – An expanded pool of specifically earmarked ADF resources;
- – Clear guidelines to ensure strong project selection and sponsorship;
- – A priority focus on infrastructure to build trade and competitiveness;
- – Selective support for regional public goods;
- – Partnership with regional entities and, where possible, the private sector;
- – Support for investments linking ADF and ADB countries.

▪ The Bank will also contribute to the development of regional integration plans and implementation. Planning and development activities will include: update of the NEPAD STAP, finalization of MLTSF, finalization and launch of Regional Spatial Development Program (RSDIP), and REC capacity building.

▪ **More client-responsive engagement in the MICs:** The Bank's operating environment in its middle income members has become substantially more challenging. Major investment, development and regional integration needs still exist, but access to finance on attractive terms from both established and new sources has grown significantly. National level capacity is stronger and national priorities more sharply defined, but there is large unmet demand for more tailored support and analytical and advisory work.

▪ The Bank must respond more effectively to these realities and offer a more relevant and competitive array of products and services. A new strategy is being prepared to better meet the challenges, whose principal elements are:

- – More competitive lending products more systematically bundled with high-value knowledge and advisory services;

- Expanded but well-targeted non-sovereign operations, principally through private sector investments;
- More effective linkages between sovereign and non-sovereign operations;
- More effective leverage of unexploited strength in the Bank's balance sheet;
- Expanded operations to promote regional integration.

▪ **Improved Products and Improved Delivery:** The Bank must further improve the quality and relevance of its current products, both lending and non-lending, develop new means to meet emerging and differentiated demands from its member countries and partners, and improve product and service delivery across the full spectrum. Important initiatives and efforts are already underway; these will be implemented on a priority basis, as well as complemented in the short to medium-term by new and additional steps.

▪ The President will put to shareholders his recommendations on how the Bank should respond to the recommendations of the **High Level Panel**. This document therefore makes no assumptions but simply notes that, subject to shareholder agreement, the Bank could explore over the medium term the viability and relevance of **new products / initiatives to** enable it to better respond to and meet the diverse needs of its RMCs.

▪ **Key Strategic and Operational Documents:** The Bank will make comprehensive improvements in both the content and presentation in most key documents in order to improve clarity and focus, and their linkage to the Bank's strategic objectives and operational commitments. This includes, among others: Country Strategy papers, Country Portfolio Reviews, Project Appraisal Reports, and the Annual Portfolio Performance Report.

▪ **Knowledge services** are increasingly identified by all of the Bank's RMCs as a necessary and still under-served complement to the Bank's lending activities. The Bank's new structure and staffing alignment better positions it to deliver on these higher expectations, and it is committed to moving forward over the MTS period. In particular, it will:

- Ensure that knowledge generation is more operationally useful and relevant.
- Substantially increase and improve the extraction of knowledge from the Bank's work and that of others.
- More effectively disseminate knowledge through internal and external networks and in RMCs and enhance utilization of key products (African Economic Conference, seminars, and policy workshops).
- At the diagnostic / analytical level Bank will seek to make high quality contributions on a relative basis, working in partnership with others to ensure a holistic understanding of development challenges.
- Become a first port of call for knowledge on economic and social developments in Africa; i.e. high quality research and analysis of African Economic Development (African Economic Outlook, African Development Report, African Development Review, African Competitiveness Report);
- Establish selective Knowledge Partnerships with world class universities, research centers, and sister institutions.
- Provide advisory services and advocacy (i.e. a stronger voice for Africa on development issues), operationally relevant economic and sector work and research, and dissemination of the Continent's success stories.
- At the sector level, focus on areas where services can enhance the **impact** of lending (e.g., Infrastructure, Governance, etc.) It will contribute to better quality at entry and results measurement.

▪ **Streamlined project procedures**, including a restructured procurement and financial management unit, and greater delegation of authority, including to field offices, will speed project implementation and lead to significantly reduced project cycle times and non-financial transaction costs. Disbursement processes will be further streamlined and decentralized.

- The Bank must further enhance its delivery of products and services through **more effective decentralization.** Progress to date will be evaluated in 2008 and the results will materially inform further development of the program.

- The Bank will work more effectively in **partnership** with others with clear agreements to deliver maximum combined impact. This includes a comprehensive review of existing memorandums of understanding with external partners, and exploration of selected "priority partnerships". These could include:

  – Other pan-African organizations such as the AU and UNECA

  – Non-African organizations such as the EC, the World Bank and emerging donors

  – African and international research institutions: to leverage limited internal capacity

  – Intensified partnerships with specialized institutions such as IFAD and Global Fund will be explored, including with respect to using the Bank's field presence to leverage their specialized assets.

- **Increase harmonization**, including greater reliance on country systems, and other Paris Declaration measures including more joint operations (co-financing), joint missions, joint analytical work, and a reduction in the number of project implementation units.

Build and Better Leverage the Bank's Core Assets

- Over the MTS period the Bank will actively explore ways to build and to leverage more effectively its core assets – human, financial, and positional.

- **Develop Human Resources:** To deliver on its strategic objectives the Bank must ensure that it is fully staffed with, manages, invests in, and retains the best available talent. Staff recruitment and staffing needs will be clearly linked to program deliverables and strategic focus.

  – The strategic priority over the next five years will be to **improve the allocation of staff and skills in line with institutional strategic priorities.** A comprehensive assessment will consider the present match between staffing skills and allocations and institutional priorities. Larger, higher impact projects will leverage staff capacity and underpin selectivity. It is expected that the proportion of staff focused on front-line operational delivery will increase. Similarly, the proportion of staff in the field is expected to increase.

  – **Enhanced recruitment techniques** that leverage best practices in technology, assessment centre methodologies, and strengthened induction and orientation practices; most positions will be advertised externally.

  – **Assessment to identify staff competencies** in a more systematic way in order to determine the staff's capacity to help the Bank face the challenges in light of the strategic priorities.

  – **Strengthened performance management and productivity assessment tools**, accompanied by managerial training, to ensure that the Bank's workforce remains agile, productive, and fully qualified. Full roll-out of the new performance evaluation and management system provides a solid basis to drive higher performance and to introduce greater rewards to encourage top performance. Performance metrics will increasingly target improved and more rigorous portfolio management where relevant.

  – **Revised compensation framework**, including bonuses and non-cash incentive programs for strong performers

  – Implementing a **learning and development strategy**, including larger/more systematic staff training program, including management training. Bank staff must employ state of the art tools to conduct economic analysis for high quality project development and implementation; more systematic training investments will be made for Field Office/local staff.

- Leverage **financial strength:**

  – Maintain the Bank's triple-A credit rating through sound, professional risk management, including strengthened treasury risk management. Implement more proactive, early warning systems to facilitate risk management decisions.

  – Review the Bank's current credit guidelines and analytical framework. In common with other MDBs this will include a review of the **capital adequacy** framework and sovereign and non-sovereign exposure limits.

  – Work with outside experts to review the potential of the ADB balance sheet.

  – Promote more co-financing and joint operations to mobilize finance to complement Bank funds.

  – Develop synergies across Bank Group public and private sector windows.

- Better leverage the Bank's **enhanced field presence**. Improvements will be made through closer relationships and greater responsiveness to Field Offices, including through:

  – Provision of **appropriate facilities** (a comprehensive study of the comparative advantages of leasing vs. buying will be carried out in the various locations to inform the Bank's approach and decision);

  – Improved systematic **communication tools** that enable headquarters to understand and respond to Field Office needs in a timely manner; and

  – **Accelerating the recruitment process** to staff Field Offices and developing and maintaining effective decentralized human resources management practices and methodologies. The goal will be to provide appropriate capacity with the right skills mix in the field.

  – Creating a Bank **telecommunications infrastructure** that will ensure full, reliable, and robust communications with member countries, field offices, development partners, and markets, including by enhancing the videoconferencing facilities, providing continuous training to field office staff. A key objective will be ensuring seamless integration of field office staff in country teams and across complexes.

  – Reviewing **Information Technology and Information Services** to ensure that these serve fully the changing needs of the Bank (for instance in delivering the results agenda, in managing performance, and underpinning outreach and knowledge services), and that we make full use of system capability.

  – Creating a framework that better facilitates **mission travel** and coordination with Field Offices through the implementation of a more user-friendly and flexible travel policy and better staff connectivity while on mission.

  – Continuously improving the capacity of the staff to communicate in the **business languages** of the Bank's member countries through enhanced training programs and the increasing use of language technology to support translation and interpretation.

  - **Deliver corporate services** more efficiently including through more outsourcing of support activities and developing longer-term partnerships with competitive suppliers.

  - Leverage **technology** to enable RMCs to access their loan and project information easily and completely, using the Client Connection facility. Will enhance RMC debt management capacity.

Produce and Better Demonstrate Superior Development Results

- Focus on **Results** and measurement of Results

  – Regular results monitoring and reporting to implement the commitments made under ADF-11.

- Reduction of the PCR backlog, significant improvements in PCR quality, and a more systematic focus on learning from past/ongoing operations.
- To reinforce the results framework going forward, explicit financing for baseline studies (where needed) and results measurement work will be included in all project and CSP logframes
- Development of standardized output indicators by sector to facilitate aggregation of Bank outputs. Extension of SAP to allow regular entry and monitoring of outputs

▪ **Focus on Quality** – The Bank Group will continue its Quality at Entry survey on a biennial basis (or annually if resources are available). The Bank will also extend quality enhancement to knowledge activities and, importantly, its support to implementation (supervision).

▪ Full implementation of new **Business Processes,** including a more fully functioning peer review and quality assurance process. The new Operations Committee, including a functioning secretariat, will be the driver of quality at entry and portfolio monitoring Bank-wide.

▪ More active and effective **portfolio management** will be possible in part through a major improvement in quality of project data, recruitment of country program officers in Tunis and in field offices. Revised project supervision report template, Back-to-Office Reports, and country portfolio reviews, focusing on specific issues and setting out actionable timeline for follow-up steps. Reduction of the ratio of cancellable projects will be accomplished in line with KPI targets.

▪ **Integrated Strategic Planning, Programming, Budgeting and Performance Monitoring** promises multiple benefits:

- Better implementation of administrative and capital budgets with more timely and analytical financial reporting
- More systematic benchmarking of the Bank's performance
- Greater decentralization of programming and budgeting with trained coordinators in each complex
- Instituting multi-year rolling Indicative Operational Program and Indicative Non-Operational Program to be presented to the Boards at mid-year together with the Mid-Year Performance Review
- Flexibility and greater empowerment/accountability of managers
- Allocation of resources aligned with strategy and linked to performance
- Enables improved reporting to the Deputies and Board as a basis for different relationship.

▪ **Corporate Deliverables - KPIs**:

- Centrality of portfolio management for sector and regional directors' KPIs, leading to greater accountability for results at every level.
- Systematic monitoring and reporting on KPIs, structured in cascading manner – institutional, complex, department and division levels. Integration of portfolio management and performance indicators into KPIs and unit/manager level performance criteria.
- Reviewing management information needs, how far they are currently being met, and what improvements are needed.

▪ **Improve institutional governance** through better communication between Management, staff and the Board, better alignment of the Board work program with Bank priorities, and more systematic follow up of Board recommendations and decisions.

5. Getting There: the Critical Path

- The full MTS will lay out a strategic Action Plan with timelines, targets and resource requirements for delivery. It will provide a medium-term framework which will guide priorities, the allocation of resources, and the annual and rolling multi-year budget and work programs; it is not intended to substitute for the latter.

Projection of Bank Group lending operations to 2012

- The lending projections for the period 2008 to 2012 seek to frame the expected level of resources required by the Bank Group if the strategic objectives described in this document are to be delivered.

- We have defined 4 basic scenarios as follows.

  - **Scenario I: low growth in ADB (+5% / year), relatively aggressive growth in private sector according to plan (~+20% / year), 50% ADF replenishment in 2010**

    - This is a conservative scenario, which integrates constraints to private sector growth (in particular, staffing and existing exposure limit).
    - In this scenario, in 2012 the Bank Group will still be preponderantly focused on its ADF window (53% of its new business) and its public lending (73% for ADB and ADF together, vs. 27% for private sector).

  - **Scenario II: 100% increase in replenishment level at ADF-12**

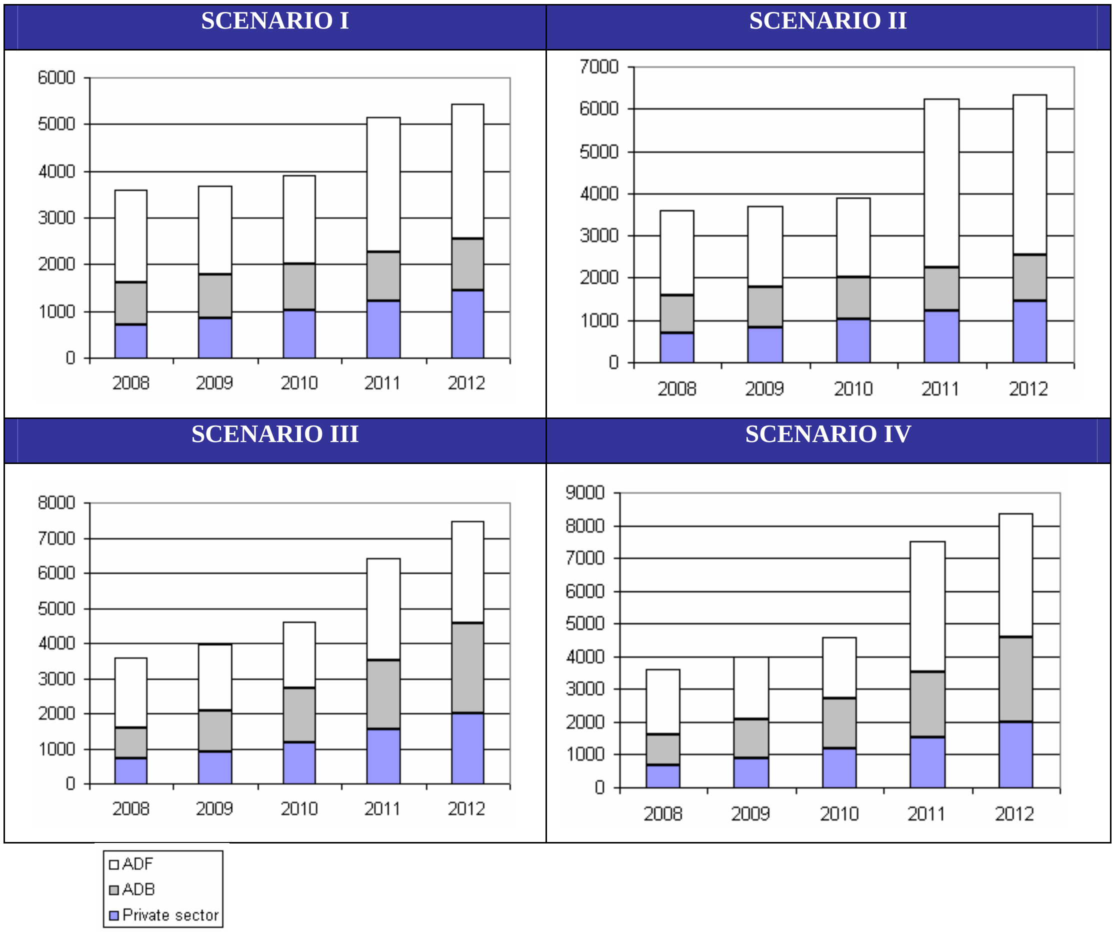
    - This scenario supposes that Donors will keep Africa as a priority, and will reward the Bank Group's performance over 2007-2009. Other hypotheses remain the same as in scenario I.
    - In this scenario, in 2012 the Bank Group will still be strongly focused on its ADF window (60% of its new business) and its public lending (77% for ADB and ADF together, vs. 23% for private sector).

  - **Scenario III: aggressive growth (+30% / year) in the ADB / Middle Income Countries and private sector**

    - This scenario supposes that constraints to this growth (staffing, exposure) are removed, and that the Bank Group substantially rethinks its products and client service to become a stronger player in a tough, competitive environment. Such growth would rely especially on a strong research and statistics complex, able to generate break-through insights and give the Bank an edge in a difficult market.
    - In this scenario, in 2012 the Bank would look very different to what it is now. MICs would be key clients. The ADB window would represent 34% of the value of operations; the private sector window would be sizeable (27%); ADF would still play an important role, although not as prominent as in the past (39%).

  - **Scenario IV: combination of scenarios II and III – an aggressive ADB and private sector, coupled with a strong ADF replenishment**

    - In this scenario, in 2012 the Bank Group will be about equally balanced between its ADF and MIC clients, with 45% of its business done by the Fund, and a solid private sector window (24%).



Impact on exposure limits

- An increase in the exposure limit for non-sovereign operations would be necessary especially to sustain the more aggressive scenarios. These projections suggest that the existing limit of 15% is likely to become a global constraint especially with the more aggressive growth scenarios for non-sovereign lending. Higher non-sovereign exposure limits would need to be considered in the next few years to allow for more ambitious growth scenarios.

- More generally, in order to see how the Bank Group can best leverage its financial situation for the benefit of its clients, there will be a need to safeguard the Bank's financial integrity while ensuring an optimal use of its capital. To this end, the Bank will further investigate what is its best capital level in light of its medium-term strategy. The assumptions linked to the way the risk capital is defined and used, such as the computation of the "maximum sustainable portfolio" for the Bank, would need further evaluation.

Impact on resource allocation

- The MTS will have resource implications and require the Bank to increase and reallocate staff and financial resources in priority areas, including:

  – Priority operational departments (e.g., private sector, governance), particularly as lending is forecast to increase. More intensive work in fragile states and on regional projects will also require resources. An analysis of current skills and gaps will guide decisions on staffing levels.

  – Providing the capacity to respond to new challenges, such as those arising from the climate change, clean energy and adaptation agenda.

- Significantly improving portfolio management, harmonization and results measurement.

- Scaling up its capacity to deliver knowledge services – research, economic and sector work, policy and technical advice. This will require resources in the Office of the Chief Economist but also operational departments.

- Delivering on the Bank's HR strategy will require significant investments in training.

- More effective decentralization to underpin improvements in the Bank's effectiveness and relevance.

▪ Given the extent of the challenge faced in Africa and the role set out for the next five years, a higher level of resources, financial and human, will be required over the period. A medium-term financing framework will be developed detailing the required increase in administrative resources. A preliminary estimate of the resources required to deliver the proposed program indicates that, using the 2007 budget as a base, the administrative budget of the Bank might need to increase by up to 20 percent by 2012.

▪ The lending scenarios detailed above point to a likely increase in the Bank's net income. A more detailed analysis of future net income will be prepared for the final MTS. However, preliminary analysis suggests that the Bank could comfortably accommodate the proposed increase in administrative expenses while maintaining its financial integrity.

Implementation plan

▪ The final MTS paper will lay out an implementation plan with more specific timelines, targets and resource implications for HR, general administration and capital budgets.