African Development Fund (ADF)
ADF-13 First Replenishment Meeting
Tunis, Tunisia, 21-22 February 2013

Chair's Summary

1. ADF Deputies and observers from international development institutions, bilateral agencies, AfDB Board members and AfDB Management met in Tunis, Tunisia on 21-22 February 2013 to discuss the thirteenth replenishment of the African Development Fund (ADF-13). They were joined in their discussions by the Governor from Côte d' Ivoire, and the Deputy Director from the Kenya Ministry of Finance, representing the Governor from Kenya. The President of Liberia, the Honourable Mrs Johnson-Sirleaf also addressed the meeting. The meeting was chaired by Mr. Richard Manning and this Chair's Summary is issued under his responsibility.

2. Opening the meeting, President Kaberuka called on donors to sustain the momentum of growth and poverty reduction in Africa through a Replenishment that would advance the transformation of Africa as envisioned by the Bank Group's draft Long Term Strategy. He underlined the special emphasis the Bank Group has placed on fragile states and gender equality going into ADF-13, and announced that he would be appointing a Special Envoy for Gender. He called for a constructive discussion on the ADF resource allocation system while ensuring responsiveness to the diverse and evolving needs of Africa's low-income countries. President Kaberuka highlighted the Bank's strong commitments and continued efforts to strengthen institutional effectiveness, efficiency and results.

3. President Sirleaf spoke both as President of Liberia and as chair of the Bank's newly established High-Level Panel on Fragile States. She commended the Bank for its responsiveness in addressing the needs and special circumstances of her country, where she asserted that its support had 'made a critical difference', and of other fragile states, while arguing for even greater attention to regional dimensions of conflict, better coordination between donors and stronger leadership of the Bank, making a case for specific action in the Mano River Union, and for further adapting mechanisms of financing. She mentioned in particular seven challenges: donor coordination, addressing the roots of fragility, regional dimensions of fragility, regional programming, adapting financing modalities, building up local capacities, and increasing responsiveness and accountability.

ADF-13 Strategic direction and operational priorities

4. Drawing on President Sirleaf's introductory remarks and on specific examples where the Bank had facilitated and contributed to strategic advances, particularly at regional level, Management underlined the unique role of the Bank as a trusted partner to the continent and the ADF's achievement of development results. Noting the significance of this, Participants commented in particular on the following points:

- <u>Strategic direction</u>: strong support was expressed for alignment with the Bank Group's draft Long Term Strategy (LTS) including its overarching objectives of support for inclusive growth and transition to green growth. Deputies requested more clarity on the operationalization of these objectives and their elaboration, including specific examples, of how the comparative advantage of the Bank has made a difference. Deputies urged swift approval of the LTS before their second meeting and the finalization of the Private Sector Development Policy and Strategy.
- <u>Operational priorities and ADF-13 indicative pipeline</u>: strong support was also expressed towards the proposed priorities: Infrastructure, Regional Integration, Governance, Private Sector Development, and Skills & Technology. Deputies endorsed continued focus on this strategic selectivity – however, they observed that the ADF-13 indicative pipeline is heavily skewed towards infrastructure, and to transport within that figure, and urged that the sectoral breakdown align better with the proposed operational priorities, particularly a greater balance among the infrastructure sub-sectors, including energy (not least sustainable energy) and water and sanitation. Some Deputies also underlined the importance of infrastructure projects financed by the Bank including complementary measures that address maintenance, capacity development and infrastructure governance issues. Management noted that softer sectors such as food security, agriculture, education and health also benefit through infrastructure spending. Deputies requested for further analysis of the pipeline for the second meeting, including regarding the level of readiness.

- Special Areas of focus: Strong support was expressed for the special areas of focus: Fragile states, Gender, and Agriculture and Food Security. Welcoming the Bank's efforts to accelerate progress to further mainstream *Gender* into operations, Deputies urged quick completion of the ongoing work on the gender strategic framework and action plan, in order to feed into discussions before the third ADF-13 meeting. With regards to *Agriculture and Food Security,* Deputies supported the Bank's approach of engagement in this sector primarily through rural infrastructure and cooperating with specialized institutions such as IFAD.

Institutional effectiveness and results

5. Participants recognized important reforms that have been undertaken in recent years, improvements particularly striking to those who had been Deputies in earlier Replenishments. They however urged the Bank to make further progress in the areas of:

- Institutional effectiveness, efficiency and value for money: several Deputies noted that with the difficult budgetary situation in many donor countries and increasing domestic pressures, the Bank needed to demonstrate its effectiveness and efficiency more strongly than ever. They supported the current efforts to improve staff management, and were pleased to learn of the significant decline in vacancy rates (currently at 6.6%). They encouraged Management to continue improving staff capacity especially in field offices and notably in fragile states. Management agreed to produce a short note setting out the nature and timetable of the various strands of reform in corporate efficiency and effectiveness for the next meeting of the Replenishment, including an institutional reform/initiative matrix for the AfDF-13 period. Some Deputies also stressed that external audit should be reinforced, in line with international best practices. With regard to the return of the Bank to Abidjan, Deputies asked Management to ensure that the operational functionality and effectiveness of the AfDF would not be negatively affected during the relocation phase. They invited Management to monitor the process carefully and to take corrective measures whenever necessary.

- Results measurement and impact evaluations: Deputies underlined the importance of the Bank showing clearly results achieved under previous ADF replenishments as well as expected results from ADF-13 reflecting the different financial scenarios. Management indicated its intention to produce a new results measurement framework for the next meeting including both indicators and draft indicative targets. Some Deputies underlined that this should be done in close coordination with other MDB's. Several Deputies spoke of the importance that they attach to the work of the independent evaluation department and specifically to impact evaluation. They requested that the Director of the Evaluation Department be given the opportunity to address the ADF Deputies at the second meeting.

Fragile states

6. In line with President Sirleaf's speech, Participants welcomed AfDB's enhanced support since 2008 and the need for sustained and deeper engagement so as not to lose the gains made. They stressed the importance of the Fragile States Facility (FSF) and encouraged additional improvements in management and delivery of assistance to fragile states. Management provided an update on actions taken in recent months, including the relocation of the Fragile States Unit to the office of the First Vice President and Chief Operating Officer, and the devolving of FSF Pillar III operational activity to the various country teams.

- Operational effectiveness: There was strong support for Management's proposal to (i) ensure fuller attention to regional dimensions of conflict and fragility; and (ii) strengthen the systematic application of 'fragility lens' and political economy analysis in ADF country strategy papers, project design and implementation. Deputies recognized that speed of response was often essential, but that associated risks must be assessed and tackled. They supported Management's intention to examine the rules, procedures and risk management of the Bank Group, as well as strengthening of country presence, with a view to increasing the flexibility and expeditious response to fragile states. They encouraged stronger donor coordination on the ground. They further urged that enhanced engagement should be accompanied by concrete actions based on lessons of development effectiveness for improving outcomes in order to help overcome the myriad challenges associated with fragility and conflict.

- There was broad agreement on the need to review the definition of fragility and methodologies for assessing fragility as proposed by Management, while at the same time ensuring that this work does not lead to significant delays in making decisions. This process should take place in close consultation and cooperation with other relevant organizations.

- Fragile States Facility: Deputies expressed strong support for the continuation of FSF and its three pillars. As regards *Pillar I*, agreement was expressed with Management's proposal to lengthen the period of support (in combination with clear exit strategies considering specific contexts) and to discuss in more detail options for eligibility criteria and resource allocation during the second meeting, including reviewing whether the Bank has sufficient flexibility to respond to opportunities to support countries demonstrating a renewed commitment to reform, and to engaging with countries in arrears. It was also agreed that the demands on *Pillar II*, and any necessary action, should be discussed during the second meeting. Deputies underscored the importance of *Pillar III* for capacity building and technical assistance and urged Management to continue improving the implementation of activities supported by this pillar and to explore new ways to better leverage financial and human resources.

- Management confirmed that initial findings and recommendations from the Bank's High Level Panel on Fragile States would be provided to Deputies for the third meeting and any initial indications of thinking for the second meeting. The Report of the Panel would also inform a revision of the Bank's strategy for fragile states to go to the Board in 2013 for implementation in 2014. The Panel's work will focus on the strategic and operational implications (to the Bank Group) of the approach set out in the 'New Deal' agreed at Busan.

Performance-Based Allocation (PBA)

7. Participants welcomed Management's efforts to improve the PBA system, acknowledged that the evolution of ADF's clients was a strong rationale for revising it, and recalled previous agreements that performance must remain central to ADF's resource allocation. They emphasized that any changes to the system be as simple, transparent and comprehensible as possible, and built on sound and accessible data, and evidence of the links between proposed indicators and poverty reduction and growth. Some deputies recommended that reform should result in a reduction of the complexity of the formula. They urged consultations with other MDBs during PBA revision, and that the Bank's system should remain coherent with that of other MDBs (in particular IDA's), while not necessarily identical to them.

- Deputies agreed that there should be an increase in the minimum allocation (option 2), certainly to UA 10M (a level similar to IDA's). For a higher increase, Management should put a specific proposal backed by suitable evidence to the second meeting.

- Several Deputies expressed support for the alignment of the PBA system with the Bank's mandate as set out in the draft LTS (Option 1): further work was needed for the second meeting on the analysis, including on the case for a proposed infrastructure index.

- Mixed views were expressed on the population and GNI exponents (Options 3 and 4): Deputies agreed to consider these further in the light of an outcome on option 1. More broadly, some Deputies asked Management to have an integrated approach to assess the impact of combined options.

- Deputies referred to the FSF as the main instrument to address the specific needs of fragile states. Some deputies considered that recognition of the special needs of fragile states (options 5 and 6) could be addressed partly within the context of the Fragile States Facility and partly in the PBA while others felt that they should be addressed solely within the FSF; in particular, preventive approaches to address structural vulnerability were mentioned.

- Management agreed to present a better targeted set of proposals for the next meeting drawing on these conclusions.

Financial capacity and ADF-13 financing framework

8. Responding to the series of proposals presented to them in two financial papers, Deputies provided the following guidance:

- ADF-13 Financing framework: They agreed that the exchange rate reference period should be 1 February to 31 July 2013; that the 10 year encashment schedule should remain in place (with provision for voluntary acceleration as at present); and that accelerated encashment should be fully hedged. It was also agreed that the technical gap would be discussed closer to the final replenishment meeting.

- Long-term ADF capacity: Deputies favored hardening ADF's standard lending terms on the lines of Management's proposal to reduce maturities from 50 to 40 years, with 10 years of grace period.
  - With regards to the *differentiation of lending terms to ADF countries*, most supported Management's proposal to divide ADF recipients into two categories. Deputies emphasized that the Debt Sustainability Framework must be fully respected. Several, but not all Deputies expressed a preference (in some cases a strong preference) for any division among ADF-only borrowers to be based on GNI per head rather than on the African Human and Infrastructure Development Index as proposed by Management.
  - Deputies wished to see strong alignment with IDA, though not necessarily identical loan terms. It was noted that IDA's own position was under review and might become clearer in late March. Deputies agreed to revert to the issue of loan terms at their next meeting.
  - Deputies agreed on introducing an *accelerated repayment clause* prospectively and a *voluntary repayment* framework. However they stressed that it was important not to inhibit graduation, and indeed to achieve an engagement with the prospectively graduating country to discuss the particular situation and if necessary to provide adequate incentives for it.

- Deputies discussed in detail the assumptions that underlay Management's calculations of the Advanced Commitment Capacity (ACC). They requested further clarifications and reflections on: (i) the impact of the new loan cancellation policy and market interest rate fluctuations, stressing that the concepts and financial assumptions on these issues should reflect economic reality; (ii) administrative cost sharing arrangements, questioning the large share of ADF and impact of the cost of the return to Abidjan; (iii) the liquidity policy of the Bank (in comparison with IDA); and (iv) net income transfers from the Bank to the ADF. One Deputy requested further assessment of the impact of the assumed donor contributions on the level of the ACC in the scenarios. Management pointed out that the present cost-sharing arrangements, agreed in 2010 and periodically reviewed by the Board, were based on a careful analysis of administrative costs of the Bank Group, and currently reflect an equitable methodology for sharing cost among the Bank Group institutions. Decisions regarding ADB transfer to ADF are made on the basis of the Bank's financial sustainability as spelled out in the Income Model, but that it was envisaged, as in 2003, to compensate ADF for a part of the costs related to the return to Abidjan. Deputies fully recognized that it is essential to ensure that the Bank remains financially sound (and maintains its AAA rating). Management will provide a technical note on the ACC calculation for the next meeting.
- Deputies welcomed Management's proposed options on innovative financial products. Deputies stressed that in assessing options the following should be looked at as well as the potential multiplier effect: (i) likely demand for the product; (ii) administrative costs for each option; (iii) debt sustainability consequences where relevant; and (iv) concern that too many or too large set asides could undermine the PBA approach. Deputies gave initial feedback on the specific options in the paper based on these considerations. Some Deputies noted that links between these innovative financial products and discussions relating the Fragile States Facility could merit further consideration. Management agreed to present fully elaborated proposals for the next meeting. This would include advice from Legal counsel on relevant options.

Next Meeting

9. It was confirmed that the next meeting would be held in Tunis on 13-14 June 2013.

Richard Manning, ADF-13 Coordinator

March 2013