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ADF-13 Resource Allocation Framework

Discussion Paper

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Executive Summary

This paper presents the framework for the allocation of the resources of 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.

The ADF-12 resource allocation framework has worked well. However, several challenges were encountered, mainly with respect to the system's flexibility and its alignment with the African Development Bank Group's (AfDB or Bank Group) mandate. Management therefore believes there is room for improvement, to ensure that the allocation system better serves the ADF's institutional characteristics, client base, operating context, strategic focus and comparative advantage. Proposed changes to the system aim at:

- Better aligning the PBA system with the ADF's operational priorities flowing forth from the Bank Group's Strategy for 2013-2022;
- Ensuring meaningful engagement with all ADF countries through PBA allocations;
- Enhancing the ADF's responsiveness to fragile states through the Fragile States Facility;
- Achieving greater equity in allocating resources for Regional Operations;
- Leveraging and catalyzing private sector resources through new, innovative financial instruments.

For the PBA, Management recommends to increase the minimum allocation to UA 15 million per cycle in ADF-13, in order to ensure meaningful engagement with all ADF countries through the PBA allocation. Furthermore, for future replenishments, Management proposes to discuss at each replenishment consultation the opportunity of adjusting the minimum allocation. Secondly, to improve the alignment between the PBA system and the ADF's operational priorities based on the Bank Group Strategy for 2013-2022, Management recommends to add a new Cluster E on infrastructure development and regional integration to the Country Policy and Institutional Assessment (CPIA) questionnaire and to include the African Infrastructure Development Index (AIDI) in the PBA formula as an additional measure of needs. Management recommends a coefficient of 0.06 for the CPIA Cluster E, and an AIDI exponent of -0.25. Simulations confirm that these two measures would result in larger allocations for countries that have significant infrastructure deficits, while maintaining the principle of rewarding good performance through a more comprehensive assessment.

Following its proposal in the "Proposed Adjustments to the Bank Group Framework for Engagement in Fragile States" paper to revise the eligibility criteria of Fragile States Facility (FSF) Pillar I, Management estimates that the volume of ADF-13 resources required for the FSF (Pillars I, II and III) will range from UA 831.4 million to UA 901.7 million depending on the top-up factor and phase-out discounts applied in the Pillar I allocations.

Concerning regional operations (RO), Management proposes to maintain the current 20 percent set aside for the RO envelope. Management recommends to allow FSF Pillar I allocations to leverage RO envelope funding and to offer a differentiated multiplier of 2 times for the countries eligible for FSF Pillar I, versus 1.5 times for other ADF recipients. For countries with small PBA allocations, Management proposes to require a regular contribution to project costs of up to 10% of their PBA for each regional project undertaken. Finally, Deputies' views are sought on the use of the RO incentive mechanism to promote policy reforms, including through program-based operations.

Two innovative financial instruments are proposed in the "ADF-13 Innovative Financing Instruments" paper. The ADF Partial Credit Guarantee will be financed through countries' PBA allocations. The Private Sector Facility is a guarantee instrument that will extend credit enhancement to the AfDB to support the development of privately funded transformational projects in ADF countries. Management envisages to allocate UA 165 million from ADF-13 resources for this purpose.

This paper presents the share of the PBA envelope and the set asides under the three replenishment scenarios set out in the "ADF-13 Financing Framework and Capacity" paper. Due to the strong linkages between FSF Pillar I allocations and country PBA allocations and due to RO cost-sharing, the percentage of resources allocated directly or indirectly on the basis of the PBA will remain approx. 90 percent, as it was in ADF-11 and ADF-12. Therefore, performance remains the fundamental principle of the resource allocation framework. Deputies are invited to provide their views on these issues.

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Abbreviations

ADF	African Development Fund
ADF-8	Eighth General Replenishment of the African Development Fund
ADF-9	Ninth General Replenishment of the African Development Fund
ADF-10	Tenth General Replenishment of the 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	African Infrastructure Development Index
AIKP	African Infrastructure Knowledge Program
CDB	Caribbean Development Bank
CPA	Country Performance Assessment
CPIA	Country Policy and Institutional Assessment
DSF	Debt Sustainability Framework
FSF	Fragile States Facility
GNI	Gross National Income
GR	Governance Rating
IADB	Inter-American Development Bank
ICT	Information and Communication Technologies
IDA	International Development Association
IFAD	International Fund for Agricultural Development
IOP	Indicative Operational Program
MDRI	Multilateral Debt Relief Initiative
MFI	Multilateral Financial Institution
MTR	Mid-Term Review
NEPAD	New Partnership for Africa's Development
PBA	Performance-Based Allocation
PIDA	Program for Infrastructure Development in Africa
PPA	Portfolio Performance Assessment
PSF	Private Sector Facility
RMC	Regional Member Country
RO	Regional Operation
RPG	Regional Public Good
SSA	Sub-Saharan Africa
UA	Unit of Account
USD	United States Dollar

ADF-13 RESOURCE ALLOCATION FRAMEWORK

1. Introduction

- 1.1. Following the first meeting discussing the Thirteenth General Replenishment of the African Development Fund (ADF-13), this paper proposes a comprehensive framework for allocating ADF-13 resources to countries eligible for funding from the African Development Fund (ADF or Fund) (both ADF-only countries and blend countries) through the Performance-Based Allocation (PBA) system, the Regional Operations (RO) envelope and the Fragile States Facility (FSF). It draws upon and is complementary to the papers on “Proposed Adjustments to the Bank Group Framework for Engagement in Fragile States”, “ADF-13 Financing Framework and Capacity” and “ADF-13 Innovative Financing Instruments”.
- 1.2. Resource allocation systems are a recurrent topic during replenishment discussions, both at the African Development Bank (AfDB or the Bank) and other Multilateral Financial Institutions (MFIs). The main challenge is to design a system that allocates resources across recipient countries in a manner that equitably rewards their performance, while responding to their diverse needs; is simple, transparent and comprehensible to both donors and recipients; is built on sound and accessible data and solid analysis; and supports the operational priorities of the institution. Coming to agreement on such a system inevitably involves trade-offs and compromise.
- 1.3. At the first ADF-13 replenishment meeting, where discussions focused on the PBA system, participants welcomed Management’s efforts to improve the system, acknowledged that the evolution of the 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 urged consultations with other MFIs during PBA revision, and that the Bank’s system should remain coherent with that of other MFIs (in particular the International Development Association’s (IDA)), while not necessarily identical to them. (See Box 1 on MFI consultations and coordination process)
- 1.4. Building on these discussions, this paper sets out Management’s proposals concerning the allocation of ADF-13 resources. These include improvements to the PBA system, modifications to the financing of ROs, and the financial consequences of the recommendations for the FSF elaborated in the “Proposed Adjustments to the Bank Group Framework for Engagement in Fragile States” paper and for the new instruments discussed in the “ADF-13 Innovative Financing Instruments” paper.
- 1.5. Section 2 of the paper reviews the implementation of the ADF-12 resource allocation framework and sets out some of the challenges encountered. Sections 3, 4, 5 and 6 set out Management’s proposals to respond to these challenges, concerning the PBA system, the FSF, the RO envelope and new financing instruments, respectively. Section 7 subsequently presents the resource allocation scenarios incorporating the proposals. Section 8 discusses some issues related to the use of ADF-13 resources, and Section 9 concludes.

Box 1: Multilateral Financial Institutions coordination process and seminars on the Performance Based Allocation system

In the late 1990s, the relationship suggested by the Dollar-Collier model between needs, good governance and development provided both a rationale for development assistance and an assurance that such assistance could be effective. Against this background, the African Development Bank (AfDB) and sister institutions like the World Bank, the Asian Development Bank, the Inter-American Development Bank, the International Fund for Agricultural Development, the Global Environment Facility and the Caribbean Development Bank moved to establish PBA systems for allocating donors’ contributions and internally generated resources.

In this context, the Multilateral Financial Institutions (MFIs) launched a coordination process on their respective resource allocation systems. In addition to informal exchanges between resource allocation experts, a technical working group on PBA systems meets annually to discuss the latest developments, share experiences and good practices, explore options for improvement of PBA systems and promote harmonization and alignment. Issues discussed in recent years have included the use of post conflict performance indicators, the Country Policy and Institutional Assessment (CPIA) questionnaire,

Box 1: Multilateral Financial Institutions coordination process and seminars on the Performance Based Allocation system

measuring portfolio performance, use of CPIA assessments in country dialogue, sources of data for PBA inputs, graduation and transition, and managing volatility in ratings. AfDB Management and staff have used the opportunity of the technical working group meetings to present and discuss its ongoing work on improving the PBA system. The proposals Management makes in this paper have been extensively discussed at the most recent meeting of the group.

Each MFI hosts a meeting in turn. The AfDB last hosted the meeting in 2011. In between meetings, informal bilateral discussions and teleconferences with multiple participants take place.

In addition to actively participating in the MFI technical working group, the AfDB has undertaken targeted missions and organized a number of seminars on the PBA system to expand its knowledge and hear a range of views from stakeholders including client representatives, academics, experts, civil society representatives and leading opinion formers. Two of such seminars are:

- A High-Level Seminar on “Aid Allocation Systems in a Changing Africa” organized in Mauritius in February 2012; and
- A seminar with the AfDB Board of Directors organized in December 2012.

These missions and events have yielded valuable insights that Bank staff have employed in exploring options to improve the ADF allocation system.

2. Implementation of the ADF-12 Resource Allocation Framework

2.1. The current ADF resource allocation framework has three main components:

- (i) national allocations for all eligible countries are determined through the PBA system;
- (ii) supplementary resources are allocated to a defined group of fragile states through the FSF, which has three pillars: Pillar I provides supplemental financing to 12 fragile states meeting the eligibility criteria; Pillar II provides resources for arrears clearance; and Pillar III provides funding for technical assistance and capacity building activities in the full range of 17 fragile states;
- (iii) the RO envelope provides funding for regional operations, additional to participating countries' contributions from their PBA allocations.

2.2. Under the Bank Group Credit Policy¹, eligibility for the ADF is determined by countries' Gross National Income (GNI) per capita and creditworthiness². In ADF-12, 41 countries were eligible for ADF resources, of which 38 ADF-only, one blend country, and two countries transitioning to AfDB-only status³. (see Annex I)

Overall Resources

2.3. Total expected resources under ADF-12 amount to Units of Account (UA) 6.263 billion. As highlighted in Table 1, internally generated resources and payments received on donors' subscriptions⁴ available for commitment to projects and programs stood at UA 5.208 billion on 31 March 2013. On that same date, UA 3.503 billion or 67 percent of the resources available for commitment had been committed. The balance available for commitment stood at UA 1.704 billion. With a strong pipeline of projects in place for approval during the rest of the year, Management expects nearly all PBA and RO resources, as well as those of FSF Pillars I and III, to have been committed by the end of the ADF-12 cycle (Figure 1). Management's consideration as at end April 2013 is that the resources for arrears clearance (FSF Pillar II) might remain unused in the period to December 2013, and therefore proposes that these

¹ Resolution B/BD/94/07/Rev1 adopted on 16 May 1995; ADB/BD/WP/95/79 dated 8 May 1995; *Bank Group Credit Policy*, ADB/BD/WP/98/40, 9 March 1998.

² The operational cut-off (threshold) for International Development Association (IDA)/ADF eligibility for FY2013 is gross national income per capita of US\$ 1,195.

³ As of 1 January 2013, Angola has completed its two-year transition period to AfDB-only and is no longer eligible for the ADF.

⁴ See Annex II: Status of ADF Subscriptions and Payments.

resources be carried over into ADF-13 within the same Pillar, in line with the discussions with the Deputies at the ADF-12 Mid-Term Review (MTR).

Table 1: ADF-12 Resources and Uses at 31 March 2013

(UA million)

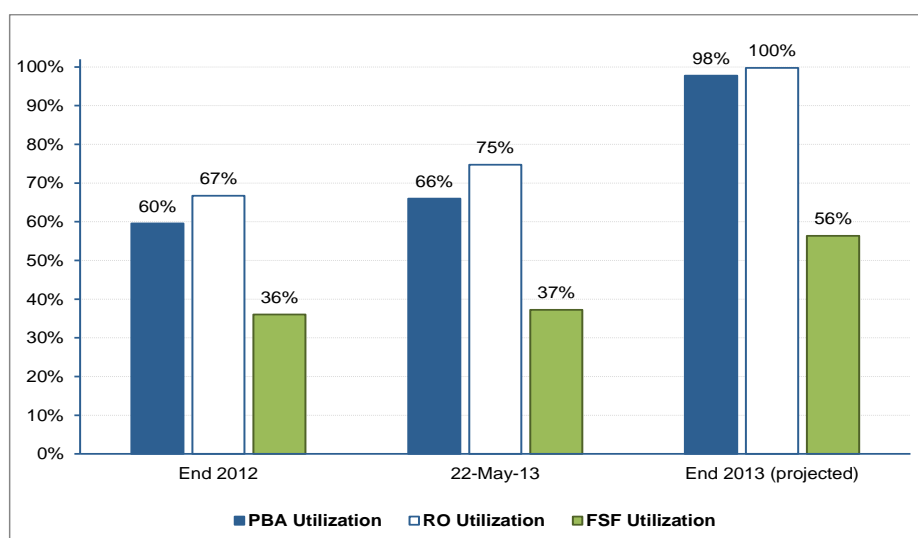
	Expected ADF-12 Resources ⁵	Available Resources (Commitment Capacity) ⁶	Committed Resources ⁷	Balance
Performance-Based Allocation resources	3,892.68	3,154.60	2,422.42	732.18
Regional Operations envelope	1,164.17	1,164.17	776.94	387.23
Fragile States Facility	764.04	829.91	302.46	527.45
<i>of which Pillar I: supplemental</i>	<i>404.94</i>	<i>404.94</i>	<i>261.05</i>	<i>143.89</i>
<i>of which Pillar II: arrears clearance</i>	<i>359.10</i>	<i>362.29</i>	<i>0.00</i>	<i>362.29</i>
<i>of which Pillar III: targeted</i>	<i>0.00</i>	<i>62.68</i>	<i>41.41</i>	<i>21.27</i>
Project Preparation Facility	-	16.60	1.65	14.95
Contingencies	442.35	42.42	0.00	42.42
TOTAL	6,263.24	5,207.70	3,503.47	1,704.23

Source: Unless otherwise indicated, all data presented in tables and figures are generated internally by the African Development Bank.

- 2.4. Since its creation in ADF-8, the size of the RO envelope has been determined as a percentage of total allocable ADF resources⁸, steadily increasing to 20 percent for ADF-12. When it was established in ADF-11, the FSF's size was first set at 7.5 percent of allocable resources. For ADF-12, the FSF was set at a fixed amount instead to fully cover Pillar I and II needs identified at the time of the replenishment discussions, namely UA 764 million or around 13 percent of allocable resources.

Figure 1: Projected Use of ADF-12 Resources as at 22 May 2013

(Percent)



⁵ African Development Fund. 22 January 2013. *2013 Country Allocations Under ADF-12*. ADF/BD/IF/2013/04.

⁶ African Development Fund. 19 April 2013. *Statement of Commitment Capacity as at 31 March 2013*. ADF/BD/IF/2013/60. Available resources for Fragile States Facility (FSF) Pillar II include the carry-over of UA 3.19 million from ADF-11. Available resources for FSF Pillar III include UA 60 million AfDB net income transfer and UA 1.5 million from income earned on FSF resources.

⁷ This amount includes surcharges on grants as derived from the Statement of Commitment Capacity.

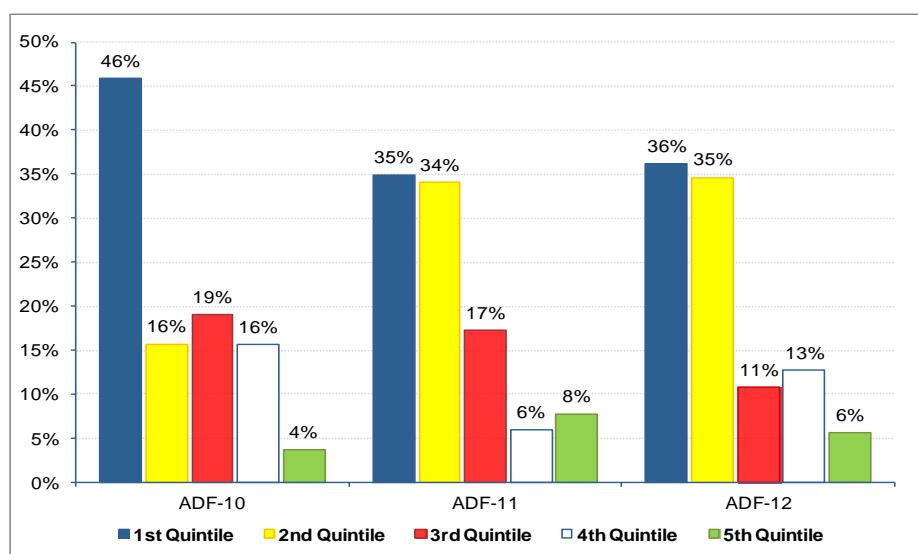
⁸ Allocable resources are the total resources mobilized for a certain replenishment, plus carry-overs from previous replenishments, minus contingencies. See African Development Fund, 22 January 2013, *2013 Country Allocations Under ADF-12*, ADF/BD/IF/2013/04, Table 1.

The Performance-Based Allocation System

- 2.5. The allocation of ADF resources to ADF-eligible Regional Member Countries (RMCs) is a six-step process that takes place annually. First, resources for the RO envelope and the FSF are set aside. Second, all countries are granted a minimum allocation, currently set at UA 1.67 million per year or UA 5 million per cycle. Third, resources are allocated to eligible countries based on annual assessments of country performance and needs using the PBA formula. Fourth, country-specific financing terms (loans, grants, or a loan/grant combination) are determined using the Debt Sustainability Framework (DSF) classification. Fifth, debt relief to eligible RMCs under the Multilateral Debt Relief Initiative is deducted from beneficiary countries' allocations, and resources provided by donors to compensate ADF for the Multilateral Debt Relief Initiative debt cancellations are then re-allocated to all ADF-only RMCs on the basis of the PBA. Finally, all allocations that fall under the minimum of UA 5 million for the ADF cycle are topped up to reach that level.
- 2.6. Country performance remains the bedrock principle of the allocation system, with three indicators of performance included in the PBA formula: the Country Policy and Institutional Assessment (CPIA), the Governance Rating and the Portfolio Performance Assessment (PPA), which together make up the Country Performance Assessment (CPA). As illustrated in Figure 2, strong performers have received the majority share of successive ADF replenishments. The share of ADF resources allocated to the two best performing quintiles increased from 61.5 percent under ADF-10 to 70.8 percent under ADF-12, while less than 20 percent has been allocated to the two lowest-performing quintiles. These trends are also reflected over the three years of the ADF-12 cycle (2011, 2012 and 2013) and in the per capita allocations (see Annex III). This demonstrates that the allocation mechanism is effective at directing more resources to stronger performers.

Figure 2: PBA Allocation by CPIA Performance Quintile, ADF-10 to ADF-12

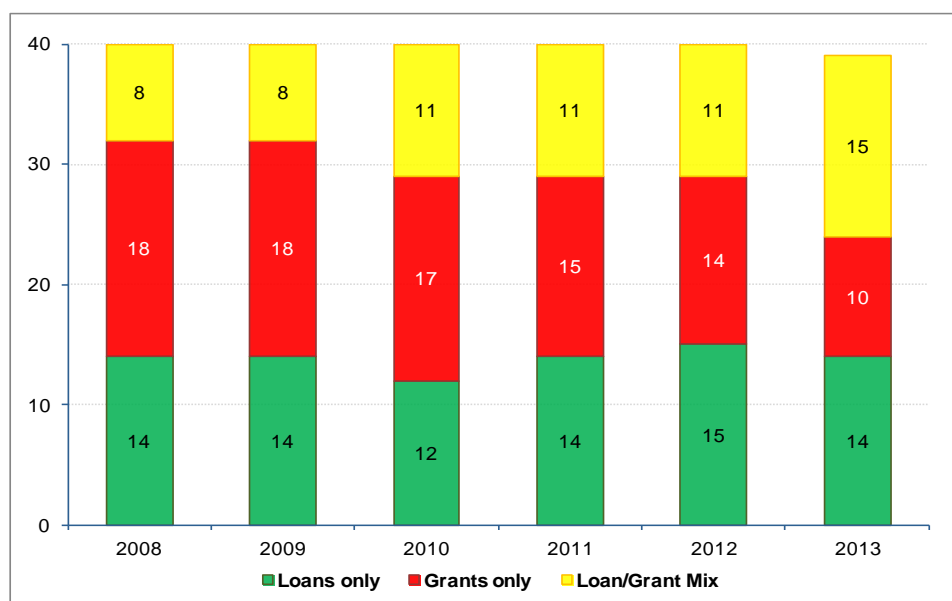
(Percent)



- 2.7. At the same time, the PBA system takes into account countries' needs, as indicated by GNI per capita and population (see Annex III). Countries' financing terms are also adjusted to their level of debt sustainability as assessed against the DSF, with countries analyzed as having a high risk of debt distress qualifying for 100 percent grants, countries at low risk qualifying for 100 percent loans, and countries at moderate risk qualifying for a 50/50 loan/grant combination (Figure 3).

Figure 3: DSF Classification for PBA allocations, 2008-2013

(Number of countries)



Challenges encountered

- 2.8. The current PBA system has been useful for determining national country allocations for more than ten years. However, it has encountered a number of challenges and limitations, as set out and discussed at the ADF-12 MTR and the first ADF-13 replenishment meeting.
- 2.9. **Rapidly changing context of African countries.** The ADF recipient countries have witnessed substantial changes in their economic and institutional circumstances. Commendable progress has been achieved in macroeconomic stability and economic growth while at the same time results in social transformation and poverty reduction have been insufficient. Also, RMCs are requesting a different type of assistance from their development partners: in order to boost growth and make it sustainable, they require increased efforts to promote infrastructure, regional integration and private sector development. The Bank's commitment to respond to these challenges implies that its policy dialogue with RMCs, notably on the basis of the CPIA, should also reflect such a shift and reward those countries that perform well in these areas.
- 2.10. **Imperfect alignment between the allocation tool and Bank Group's core priorities.** The Bank itself also implemented critical reforms to both improve its performance in delivering assistance to its clients and be recognized as a knowledge institution and prime development partner on the continent. The Bank Group's recently adopted Strategy for 2013-2022 elaborates its response to the pressing challenges of the African continent during the next decade. The operational priorities set out therein determine the focus of ADF-13. As elaborated at the first replenishment meeting, some of these focus areas, including infrastructure development and regional integration, are not well captured in the allocation system, notably the CPIA questionnaire. The alignment between the ADF core priorities and the PBA system can thus be strengthened.
- 2.11. **Changes in aid landscape.** Against the backdrop of substantial changes in the development assistance landscape, with the emergence of new players and changing roles for traditional actors, the question has arisen how the ADF can continue to engage meaningfully with its recipients through the PBA allocation. Inflation and cost increases over the past ten years have reduced the purchasing power of the minimum allocation, which has remained fixed at UA 5 million per cycle. At the same time there is an increased focus on achieving and measuring results in fragile states. The limitations of the PBA system in responding to issues of fragility are well known and form one of the reasons for the Bank's engagement with the fragile states through the FSF.

- 2.12. **Balance between performance and needs.** The well-documented challenge of trying to achieve two different objectives (addressing countries' needs and rewarding their policy and institutional performance) with one single instrument (development assistance volume) has continued to be felt. The discussion on the optimal balance between these two elements in the PBA formula has also continued throughout the ADF-12 period. At the same time, the PBA principle of allocating more resources to better performing countries continues to be strongly supported by most donor countries, as reiterated at the first ADF-13 replenishment meeting, and Management's commitment to this principle remains undiminished.
- 2.13. Management's recommendations to address the challenges are set out in section 3 below.

Fragile States Facility and Regional Operations envelope

- 2.14. **Fragile States Facility.** The FSF was established in 2008 primarily to provide additional resources and operational flexibility to fragile states that have important resource needs that cannot be addressed adequately only through the PBA system, as they start from a very low base of performance. Under ADF-12, the FSF has continued to play a critical enabling role by channeling dedicated financial resources and providing greater operational flexibility for fragile states through three pillars: (i) topping up regular country allocations with a multiple of the average of the two highest country PBAs under ADF-11 (Pillar I); (ii) standing ready to trigger operational reengagement in countries with protracted arrears meeting specific eligibility criteria (Pillar II); and (iii) providing targeted support for institutional development through capacity building and technical assistance (Pillar III).
- 2.15. As summarized in Table 1, the amount of resources allocated to the FSF under ADF-12 was UA 764 million, of which UA 405 million was applied to Pillar I (see Table 2) and UA 359 million to Pillar II. Regarding Pillar III, the unused balance of resources from ADF-11 was rolled over and supplemented with income earned on FSF resources.

Table 2: Fragile States' Pillar I and Total Allocations under ADF-12

(UA million)

Country	Pillar I allocation ¹	Three-year PBA Allocation plus Pillar I Allocation
Burundi	57.23	93.27
Central African Republic	26.43	43.16
Comoros	10.00	15.38
Congo DRC	60.00	249.26
Côte d'Ivoire	60.00	124.42
Guinea Bissau	12.51	19.76
Liberia	52.43	91.66
Sierra Leone	28.71	55.00
South Sudan	17.03 ²	33.90
Sudan	22.97 ²	77.16
Togo	41.51	63.42
Zimbabwe	16.12	33.69
Total	404.94	900.09

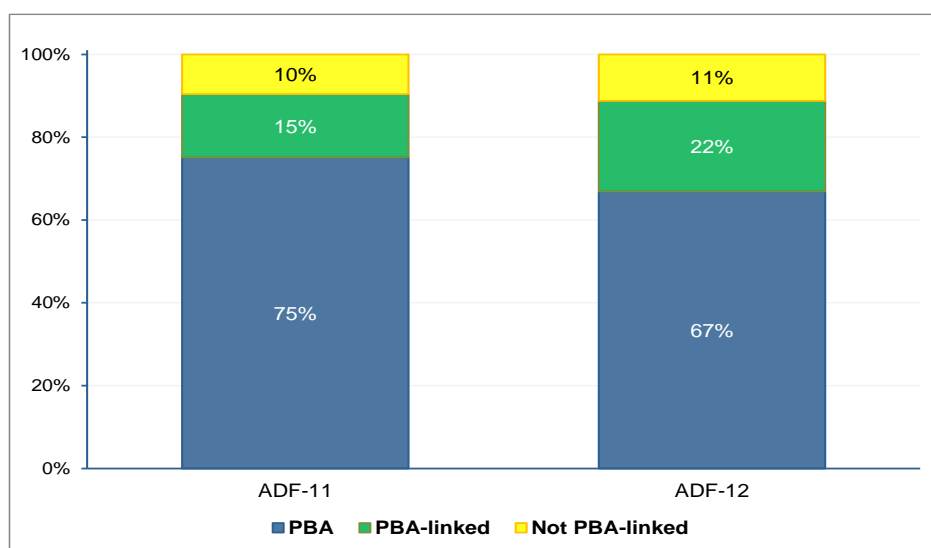
Notes: [1]: A floor of UA 10 million and a ceiling of UA 60 million apply to Pillar I allocations; [2] Following the apportionment of resources between South Sudan and Sudan.

- 2.16. **Regional Operations envelope.** Resource allocation for ADF-funded ROs has been guided by the Regional Operations Framework⁹ endorsed in 2008. It introduced the cost-sharing principles (and related exceptions) whereby participating countries contribute at least one third of a project's cost through their national Performance Based Allocations to leverage up to two thirds from a dedicated set-aside, the RO envelope.

⁹ Strategic and Operational Framework for Regional Operations (ROs) – ADF/BD/WP/2008/16

- 2.17. During ADF-12, 20 percent of resources were set aside for the RO envelope. To strengthen the link between ROs and performance and enhance national ownership of such operations, a rigorous annual Prioritization and Selection process was introduced¹⁰, whereby all ROs requesting funding are evaluated against an agreed scorecard before the Operations Committee selects the most compelling and meriting projects.
- 2.18. The cost-sharing mechanism was maintained, as were the possible exceptions to this mechanism for countries with a small PBA allocation¹¹ and for Regional Public Goods. A cap was however introduced on the total amount that could be allocated under the Regional Public Good exemption regime (15 percent of the RO envelope).
- 2.19. Even though the FSF and the RO envelope are set-asides from the PBA, country cost-sharing of ROs and the top-up factor in the FSF Pillar I allocations have enabled a strong link to country PBA allocations and thus to performance. As a result, approximately 90 percent of ADF resources have been directly or indirectly allocated on the basis of performance (Figure 4).

Figure 4: Share of Allocations linked to the Performance-Based Allocation System
(Percent)



Notes: PBA=Performance-Based Allocations; PBA-linked = FSF Pillar I + regional operations with cost-sharing; Not PBA linked = FSF Pillars II and III + regional operations exempted from cost-sharing (regional public goods + small allocation countries whose contribution is capped)

Challenges encountered

- 2.20. **FSF.** An important feature of the resource allocation methodology applied to FSF Pillar I under ADF-11 and ADF-12 is its transparency and the link to performance with the application of the “2x top-up factor” principle. The upfront nature of the three-year allocations offers recipients predictability, and eligible countries have accessed a significant amount of additional resources from the FSF compared to what they would have received from the PBA alone. While this straightforward approach has been very useful in ensuring predictability and transparency, it has also implied some rigidity since the FSF was not able to respond to emerging needs mid-cycle or to support countries demonstrating renewed commitment to reform.
- 2.21. **RO envelope.** As set out at the ADF-12 MTR, demand for funding of ROs far outstripped the supply of resources. Pressure to participate in funding of quality projects will further increase following the endorsement by African Heads of State and Government, in January 2012, of the Program for Infrastructure Development in Africa (PIDA). Its Priority Action Plan outlines 51

¹⁰ Regional Operations Selection and Prioritization Framework - ADF/BD/WP/2011/01

¹¹ Countries with a three-year indicative PBA allocation of UA 20 million or less contribute the standard share of project costs up to a maximum of 10 percent of their allocation; the ROs envelope covers the remaining costs.

critical infrastructure programs and projects contributing to the continent realizing its full growth potential. This infrastructure blueprint amounts to capital investments of USD 7.5 billion per year up to 2020, with strong calls on the ADF to play a significant role.

- 2.22. The cost-sharing arrangement introduced in ADF-11 has provided a strong incentive for ADF countries to participate in operations promoting regional economic integration. In light of growing expectations, maintaining this incentive for a sufficient number of good projects has, however, proven to be a challenge. In addition, the perceived disproportionate benefit that countries with a small PBA allocation (whose contributions to ROs are capped) derive from the RO envelope¹² was identified as a challenge in maintaining equitable access for all potential beneficiaries.
- 2.23. The approach to the new Regional Integration Strategy, presented at CODE on 2 April 2013, identified the need for providing mechanisms for the stabilization of fragile regions. However, due to the limited size of their PBA allocations, fragile countries find the trade-offs between national operations and participating in regional operations particularly poignant.
- 2.24. The independent evaluation of the Bank's multinational operations¹³ also identified a clear need for innovative use of existing instruments to tackle the soft aspects of regional integration initiatives and to ensure they yield their full benefits, particularly in terms of infrastructure services.
- 2.25. Management's recommendations to address these challenges are set out in section 4 for the FSF and section 5 for the RO envelope.

3. Proposals to improve the PBA system

- 3.1. The first ADF-13 replenishment meeting discussed the challenges that the PBA system has faced during the more than 10 years of its existence, recalled in Section 2, and possible options to address those challenges and make the system more robust. Management put forward three objectives for a reform of the system: (i) to align the allocation methodology with the Fund's strategic and regional focus; (ii) to ensure a meaningful engagement with recipient countries through country allocations; and (iii) to strengthen the PBA framework for fragile states.¹⁴
- 3.2. Deputies acknowledged that there is a strong rationale for adjusting the PBA system. At the same time, they recalled that performance must remain central to the ADF resource allocation and emphasized that any changes to the system be as simple, transparent and comprehensible as possible. Deputies also advised on the need to build on sound and accessible data, as well as evidence of the links between proposed indicators and poverty reduction and growth.
- 3.3. At the first replenishment meeting, Management proposed six options to fine tune the PBA system. Several Deputies expressed support for the first option, concerning the alignment of the PBA system with the Bank Group's mandate as set out in the draft of its Strategy for 2013-2022 (which has since been approved). Management proposes to pursue this alignment in a balanced way, i.e. through both the performance component and the needs component of the PBA formula. Therefore, this section analyses in detail Management's recommendation to add a cluster of questions (Cluster E) to the current CPIA questionnaire to capture countries' performance on the ADF strategic priorities of infrastructure and regional integration, and to introduce the Africa Infrastructure Development Index (AIDI) in the PBA formula as an additional measure of needs.
- 3.4. Options 2, 3 and 4 concerned ways to ensure meaningful engagement with recipient countries through the PBA allocation. On the minimum allocation (option 2), Deputies agreed to top it up and align it with IDA's minimum allocation, while remaining open to going further if Management provides the required justification. At the first IDA-17 replenishment meeting in March, IDA Deputies agreed to increase the IDA minimum allocation to SDR (=UA) 12 million per cycle. This section provides arguments for an increase beyond that amount.

¹² For example, in one RO approved during ADF-12, a small allocation country achieved a multiplier effect of 85 to 1 with its contribution.

¹³ *Fostering Regional Integration in Africa: an evaluation of the Bank Group's Multinational Operations, 2000-2010* – ADF/BD/WP/2012/70

¹⁴ African Development Bank, *Options for a More Robust ADF Performance-Based Allocation System*, February 2013.

- 3.5. Options 3 and 4 were to lower the exponent on population in the PBA formula to favor less populous countries and better reward performance; and to increase the weight of GNI per capita to account for countries' access to other concessional and non-concessional sources of funding. These options received mixed views from Deputies, who agreed to consider them further in the light of an integrated approach to assess the impact of combined options. After having conducted simulations, Management has come to the conclusion that the expected results are not achieved and that, when combined with other options, changes in these exponents result in a stronger concentration of reallocated resources to a limited number of countries. Management has therefore decided not to pursue these options further at this time.
- 3.6. As regard to the options 5 and 6, "use of a partially differentiated CPIA questionnaire for fragile states" and "incorporation of an index of fragility in the PBA formula", Deputies referred to the FSF as the main instrument to address the specific needs of fragile states. Hence, Management is no longer considering options specifically aimed at fragile states in the PBA framework, and proposes only to strengthen the Bank's assessment of sources of fragility and vulnerability in ADF countries. This recommendation is elaborated in the paper "Proposed Adjustments to the Bank Group Framework for Engagement in Fragile States".
- 3.7. Performance remains the bedrock of the system. To ensure that the principle of rewarding strong performance is preserved, Management undertook simulations to assess the impact of each scenario of proposed adjustment and ensure that no substantial distortion takes place (see Annex VIII). Simplicity and transparency are also key guiding principles that the proposals comply with.
- 3.8. At the same time, in recent revisions of MFIs' PBA systems, a notable shift towards a stronger poverty orientation can be observed, including through reducing the weight of the performance factor in the PBA formula (IDA), giving a greater weight to the "Social inclusion and Equity policies" cluster of the CPIA (Inter-American Development Bank) and adding a poverty variable to the formula (Caribbean Development Bank¹⁵). As recommended by the Deputies, Management's proposed adjustment of the ADF PBA system avoids misalignment with the PBA system of IDA and other development partners¹⁶. The introduction of an additional cluster of questions to the main CPIA questionnaire follows the example of IFAD, which also has such a cluster of additional questions (see Annex IV, which also sets out the different weights that institutions attach to the various elements in their PBA formulas). Alignment with IDA's CPIA questionnaire is preserved, since the proposed new cluster does not modify the main CPIA Clusters A through D nor their sub-criteria.¹⁷ Introducing an additional element of needs in the formula is in line with the observed stronger poverty orientation of PBA systems in general and with tailoring to the institutional mandate in particular.
- 3.9. In sum, Management recommends a single package of proposals: increasing the minimum allocation and adding a Cluster E to the CPIA questionnaire while introducing the AIDI in the PBA formula. This approach narrows down the number of issues to be discussed while contributing to a better understanding of the changes to be introduced to the PBA system and clarifying the implications in terms of reallocation of PBA resources that will result.

Management's proposals to fine tune the PBA system

Increase the Minimum Allocation

- 3.10. Increasing the minimum allocation seeks to provide to small population countries a larger basis for leveraging the catalytic role of ADF funding. While Deputies agreed during the first ADF-13 replenishment meeting to top up the current minimum allocation of UA 5 million per cycle and align it with the IDA minimum (recently established at UA 12 million for IDA-17), Management submits for Deputies' consideration the following arguments for an increase of the minimum allocation up to UA 15 million per cycle.

¹⁵ This poverty variable comes in addition to the vulnerability index already included as a needs component in the CDB's PBA formula - see Annex IV

¹⁶ Management's proposals have been extensively discussed with other MFIs at the most recent meeting of the technical working group (see Box 1), where they received a positive reception and constructive feedback.

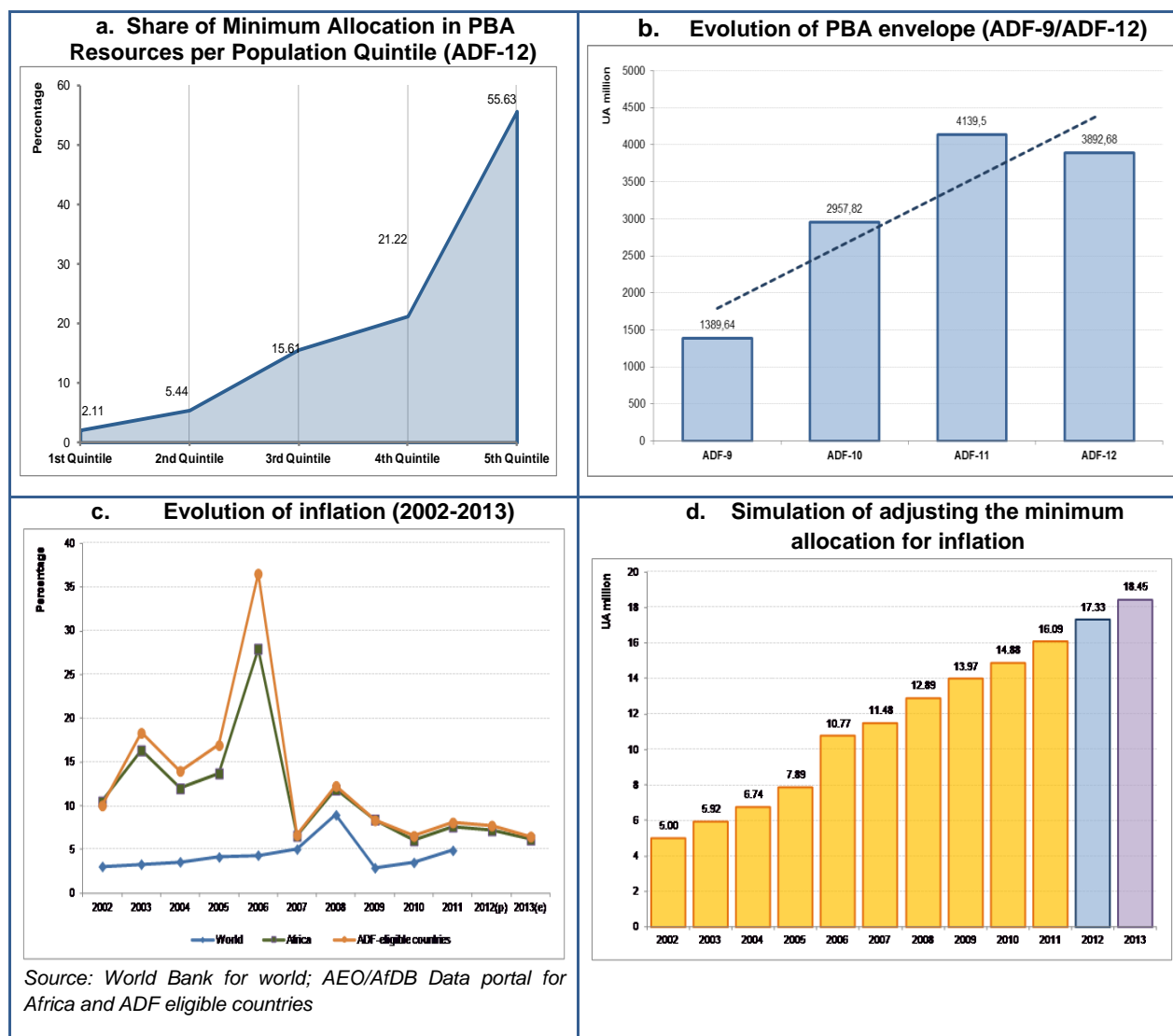
¹⁷ As is currently the case, it is also IDA's CPIA which will continue to be used for the policy-dependent debt thresholds used in the Debt Sustainability Framework. The addition of a cluster of questions to the ADB's CPIA will have no effect on the country DSF classifications.

- 3.11. **High dependence of small population countries on the minimum allocation.** As set out in the paper “Options for a More Robust ADF Performance-Based Allocation System”, countries with small allocations depend more on the ADF to finance their development than do countries with large allocations, because they receive the least Official Development Assistance from other sources. In addition, the minimum allocation makes up an important part of the resources these countries receive from the ADF. During the ADF-12 cycle, the sum of the minimum allocations for all ADF-eligible countries (UA 205 million) represented 5.4 percent of the total PBA envelope. At the same time, for the eight least populous ADF countries (fifth population quintile in Figure 5a), the minimum allocation represented 55.6 percent of their PBA resources. This highlights the dependence of small population countries on the ADF and particularly on the minimum allocation, and underlines their constraints to financing investment projects requiring large amounts of resources. Their opportunities to benefit from the economies of scale that may result from increased resources are currently severely limited.
- 3.12. **Unchanged minimum allocation over the last ten years.** The minimum allocation of UA 5 million has remained unchanged since at least 2002, i.e. ADF-9. Meanwhile, the size of the PBA envelope has been multiplied by 2.8 since then, growing from UA 1,389.64 million in ADF-9 to UA 3,892.68 million in ADF-12 (Figure 5b). While the amount of PBA resources allocated to the eight countries with the largest population (first population quintile) has been multiplied by 2.9 (from UA 710.12 million in ADF-9 to UA 2,078.34 million in ADF-12), the allocation for the eight least populous countries (fifth quintile) has been multiplied by 1.6 (from UA 65.92 million in ADF-9 to UA 102.60 million in ADF-12). This reflects an imbalance between the capacities of large and small population countries to acquire additional PBA resources as well as the inability of the current minimum allocation to overcome this imbalance.
- 3.13. **Eroding effect of inflation.** Inflation is an important indicator to measure the erosion of purchasing power over time, particularly as African countries have higher inflation rates than other regions of the world (figure 5c). Domestic production in Africa makes extensive use of physical inputs and skilled labor that are imported, hence subject to increased costs related to transport, customs and wages. For example, high transport costs add 75% to the price of African goods.¹⁸ Lack of infrastructure also contributes to inflated production costs. In general, providing infrastructure services is twice as expensive in Africa. For instance, power tariffs range between USD 0.02-0.46 per kilowatt-hour in Sub-Saharan Africa (SSA) compared to USD 0.05-0.10 in other developing regions, and road freight tariffs (in USD per ton-kilometer) are 3.5 to 4 times higher in SSA. As highlighted by the 2011 Infrastructure Consortium for Africa report, cost overruns during implementation are one of the top five risks for infrastructure projects in African countries.¹⁹
- 3.14. During the last 10 years (2002-2011), inflation in ADF-eligible countries has averaged 13.8 percent per year compared to 4.4 percent for the world, 5.7 percent for world developing countries and 12.1 percent for the African continent (Figure 5c). Given the eroding effect of inflation on purchasing power, Management believes that there is a case to increase the ADF minimum allocation to mitigate this effect. For illustrative purposes: using the average inflation rates of ADF-eligible countries for the 2002-2011 period and projections for 2012 and 2013, simulations show that if the UA 5 million minimum allocation had been adjusted for inflation each year since 2002, it would have risen to reach UA 18.45 million by 2013 (Figure 5d).

¹⁸ African Development Bank Group. *At the Center of Africa's Transformation: Strategy for 2013-2022*.

¹⁹ 2011 Infrastructure Consortium for Africa Annual Report: Financial Commitments and Disbursements for Infrastructure in Africa in 2011.

Figure 5: Arguments to increase the minimum allocation up to UA 15 million



3.15. **Redistribution effect vs. performance.** Simulations using the 2012 PBA allocations show that topping-up the minimum allocation to UA 15 million would result in redistribution of UA 55.73 million of PBA resources to 24 out of the (then) 41 ADF-eligible countries, most of which are countries with a small population, and 16 out of 17 fragile states. The 16 least populous countries (fourth and fifth population quintiles) would see their share of total PBA-resources increase from 8.2 percent to 11.8 percent. It should be noted that this redistribution would not undermine the performance principle, as the best performing countries (i.e. first and second performance quintiles) would still receive two-thirds of the PBA resources (Table 3).

Table 3: Impact of increasing the minimum allocation to UA 15 million*(Simulations on 2012 PBA allocations)*

# Higher Allocation			# Lower Allocation			Reallocated resources (UA Million)	Average increase (UA Million)	Average decrease (UA Million)
FS	NFS	Total	FS	NFS	Total			
16	8	24	1	16	17	55.73	2.32	3.51

Resources per Population Quintile (%)		
Quintile	UA 5 million (Baseline)	UA 15 million
1 st Quintile	55.08	51.95
2 nd Quintile	21.17	20.58
3 rd Quintile	15.55	15.71
4 th Quintile	6.07	7.45
5 th Quintile	2.14	4.31

Resources per CPA Quintile (%)		
Quintile	UA 5 million (Baseline)	UA 15 million
1 st Quintile	25.11	23.94
2 nd Quintile	45.29	43.05
3 rd Quintile	14.05	14.93
4 th Quintile	7.08	8.26
5 th Quintile	8.47	9.82

Add a cluster of questions to the CPIA questionnaire capturing the main ADF strategic priorities and introduce the African Infrastructure Development Index in the PBA formula

Adding a CPIA cluster E

- 3.16. The current CPIA questionnaire captures directly or indirectly many of the ADF strategic priorities, as guided by the Bank Group's Strategy for 2013-2022. However, while in some cases this link is straightforward (e.g. private sector development, governance and gender), other thematic areas are not captured in a satisfactory manner. Moreover, given the rationale and scope of the ADF strategic priorities, the current CPIA does not fully assess governments' policy and institutional performance in each of those thematic areas, whereas they are important for ensuring an efficient and effective use of resources (see Annex V).
- 3.17. To achieve a more comprehensive assessment of countries' policy and institutional performance and a better alignment between the allocation methodology and the final use of ADF resources, Management recommends for Deputies' consideration an additional CPIA Cluster E (CPIA_E). Such a cluster will assess countries' performance on identified ADF strategic priorities that are insufficiently addressed within the current CPIA. This approach follows the example of IFAD, which also has an additional cluster of questions, and has the advantage of preserving the alignment of Clusters A through D with the IDA CPIA, while enabling to fill the gap in the current Bank's CPIA as regards its Strategy for 2013-2022. The additional questions will enrich the Bank's assessment of countries' policy and institutional performance, broadening and deepening its knowledge, and enabling it to improve the quality of its policy dialogue with regional member countries, including in those areas in which the Bank has a comparative advantage and that constitute the bulk of its operations. Finally the Cluster E will offer an additional opportunity to reward country performance.
- 3.18. In order to ensure simplicity and a smooth improvement of the CPIA questionnaire, Management intends to proceed through a gradual approach and to include in the new cluster only some of the Strategy for 2013-2022 strategic priorities/focus areas. As the Strategy will be implemented over the next decade, additional dimensions or themes could be incorporated incrementally, based on ongoing experience, development effectiveness reviews and the evaluation of the Strategy, and upon approval by Deputies during future ADF replenishments.
- 3.19. The proposed two areas to be covered by the new CPIA_E are: (i) infrastructure development and (ii) regional integration (see table 4 for details). The inclusion of infrastructure in the new cluster is a logical corollary of the weight of this sector in the Bank's operations, i.e. 48.9 percent of Bank Group total loan and grant approvals in 2012 and 54.6 percent of ADF loans and grants approved for the same year. The Indicative Operational Program (IOP) for the next ADF cycle confirms the Bank's engagement to promote infrastructure development in Africa, with 75 percent of the ADF-13 IOP foreseen to support infrastructure development. Assessing infrastructure policy and institutional frameworks will also contribute to strengthening dialogue

with RMCs on infrastructure development challenges and its critical role for other sectors and areas, including private sector development, regional integration, agriculture and food security, and inclusive growth.

- 3.20. As regards regional integration, the Bank Group not only has a clear mandate to promote it, but it is also actively participating in several regional initiatives, including in the framework of the NEPAD and the PIDA. Moreover, the ADF has dedicated significant resources for multinational operations, more than UA 2.4 billion under ADF-11 and ADF-12 thus far. Looking ahead, the ADF-13 IOP includes UA 4.0 billion for 101 regional operations (52.6 percent of the total ADF-13 IOP of UA 7.6 billion). More comprehensively reflecting countries' policy and institutional performance on regional integration in the CPIA questionnaire is therefore a natural step.

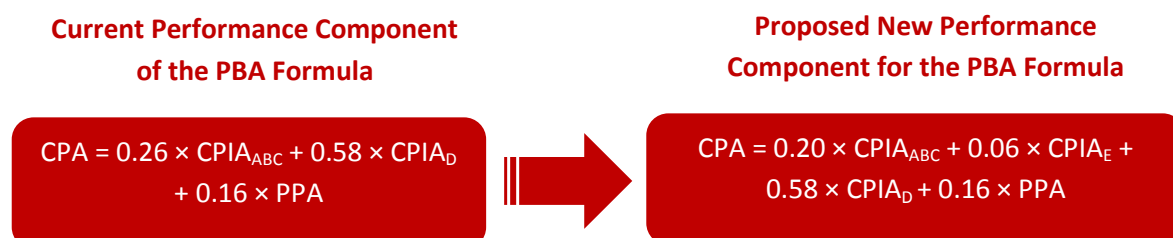
Table 4: Proposed CPIA Cluster E - ADF Priorities: Infrastructure Development and Regional Integration

Criterion	Sub-criterion	Description
I. Infrastructure Development	a. Sector strategy/policy	This sub-criterion covers the extent to which: (i) the country's Poverty Reduction Strategy Paper or any other national development plan takes into account infrastructure development; (ii) the infrastructure sector strategy is effectively implemented (use of planning tools such as master plans/multiyear action plans) and the necessary resources are allocated in the national budget; and (iii) the extent to which infrastructure development plans/strategies are aligned to other sector strategies/plans, including agriculture, food security, regional integration and trade, and private sector development.
	b. Legal and regulatory frameworks for infrastructure	This sub-criterion assesses the extent to which there is: (i) clear and transparent legislation and regulatory frameworks for infrastructure; (ii) comprehensive laws and regulations that take into account all of the infrastructure sub-sectors and the country's infrastructure needs; and (iii) local human and institutional capacity for designing and implementing that legislation/regulations.
	c. Public resource management and accountability in the infrastructure sector	This sub-criterion assesses the extent to which the government can be held accountable for the use of funds for infrastructure projects/programs (notably during the procurement process) and the results of its actions to develop infrastructure. It also assesses the extent to which the government respects environmental safeguards and consults the population and different stakeholders in designing and implementing infrastructure projects/programs.
II. Regional Integration	d. Movement of persons and labor and right of establishment	This sub-criterion refers to the level of implementation, by countries, of protocols regarding free movement of persons and labor within Regional Economic Communities. This includes, among others, the adoption of common passports, the easing of visa requirements and the extent to which the country facilitates issuance of a resident card. The efficiency of national immigration offices at border posts/airports with the required human and institutional capacities should also be assessed.
	e. Regional financial integration	This sub-criterion assesses the extent to which countries promote legal and regulatory frameworks that help capital move easily within a given REC. This supposes that the region has already adopted certain financial and investment protocols, or has even established an economic and monetary union.

- 3.21. The criterion for infrastructure development proposes three sub-criteria to assess governments' performance: (i) Sector strategy/policy, (ii) Legal and regulatory frameworks for infrastructure, and (iii) Public resource management and accountability in the infrastructure sector. The proposed criterion on regional integration complements the criterion on trade policy that already exists in the main CPIA by enlarging its scope and adding two new dimensions related to "Free Movement of Persons/Labor" and "Regional Financial Integration".

- 3.22. The $CPIA_E$ will be incorporated in the PBA formula through the performance component, the CPA. A coefficient of 0.06 is proposed for the new cluster, i.e. the weight of $CPIA_{ABC}$ would be reduced to 0.20. No changes are proposed to the weights of governance or the PPA. Figure 6 reflects what the performance component of the PBA formula would look like if $CPIA_E$ is adopted.

Figure 6: Incorporating Cluster E in the Performance Component of the PBA Formula

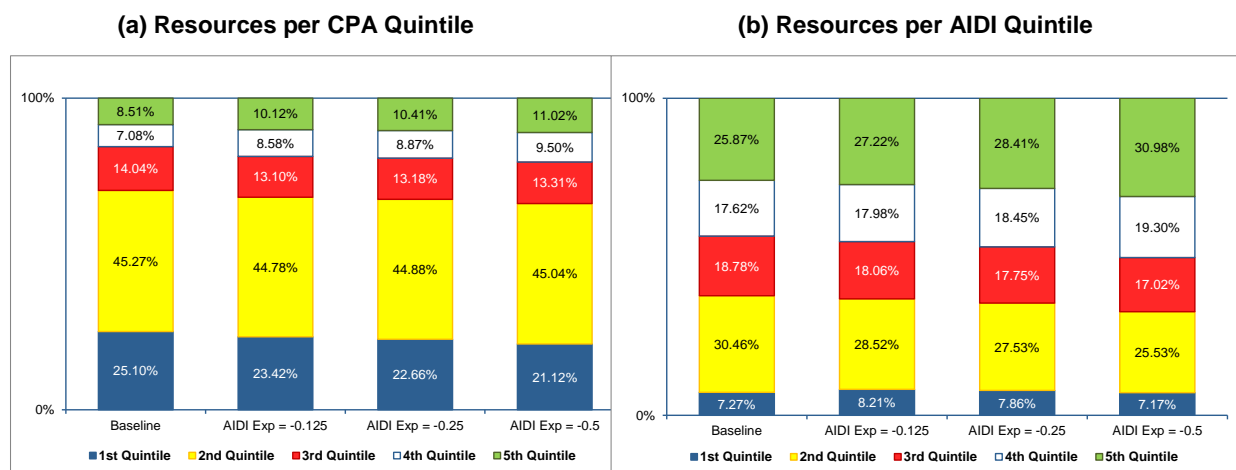


Including the AIDI in the PBA formula

- 3.23. Desiring to better align the PBA allocation methodology with the Bank Group Strategy for 2013-2022 in a balanced way, i.e. through both the performance and the needs components of the PBA formula, Management proposed the inclusion of the AIDI in the formula as a needs component in addition to the incorporation of CPIA cluster E as a performance component. The AIDI measures countries' level of infrastructure development based on four dimensions: transport, electricity, information and communication technology, and water and sanitation (see Annex VI for detailed information). The AIDI was proposed to be assigned a negative exponent such that countries with a lower level of infrastructure development would receive a larger allocation.
- 3.24. Following Deputies' feedback on this proposal at the first replenishment meeting, Management is submitting further analysis and simulations, assuming a minimum allocation of UA 15 million. The simulations also incorporate the proposed CPIA Cluster E in the performance component of the PBA formula, as illustrated in Figure 6. Indicative scores for the $CPIA_E$ were provided by the Bank's country economists.
- 3.25. In order to limit volatility and preserve data reliability, Management proposes to use a three-year moving average for country AIDI scores when computing the allocations (as it is the case for the GNI per capita element in the formula), i.e. for the 2014 PBA allocations (first year of the ADF-13 cycle), the AIDI average score for 2009-2011 would be used.
- 3.26. Figure 7 below shows the distribution of resources per (a) CPA performance quintile and (b) AIDI quintile for scenarios corresponding to an AIDI exponent of -0.125, -0.25 and -0.5. For these exponents, we note that there is no substantial distortion in the allocation trend across the performance quintiles when compared to the baseline scenario²⁰: the 16 top performing countries (first and second CPA quintiles) receive between 64 and 68 percent of PBA resources, compared to 70 percent in the baseline scenario (Figure 7a). At the same time, the countries that are poorer in terms of infrastructure are allocated more resources: between 45 and 50 percent of the resources are allocated to the 16 countries belonging to the fourth and fifth AIDI quintiles, as compared to 43 percent in the baseline scenario (Figure 7b). As many fragile states are among the countries with the poorest infrastructure, they benefit from the redistribution effect of the AIDI: regardless of the scenario, 16 out of the current 17 fragile states gain in allocation.

²⁰ The baseline scenario is the actual 2012 PBA allocations

Figure 7: Distribution of Resources per Quintile of CPA Performance and AIDI



- 3.27. As Deputies may recall, in the scenarios presented at the first replenishment meeting, incorporating the AIDI in the PBA formula resulted in a concentration effect, with three countries receiving 65 percent of the reallocated resources. In order to reduce this distortion, Management re-examined and revised the specific indicators included in the AIDI to make it more broad-based and cognizant of populations' access to infrastructure in addition to physical existence of infrastructure. New indicators were identified and incorporated into each of the four components (transport, electricity, ICT, and water & sanitation), thereby improving consistency between the components and making them more balanced. All the indicators selected have sound and reliable data sources for which data are available for the past 10 years. In addition, sensitivity analysis was undertaken to ensure the robustness of the individual indicators and the index as a whole. This revision of the AIDI has had the desired effect, in that the concentration in the reallocation of resources is reduced. Including the new Cluster E as a performance component also contributes to dampening the concentration effect.
- 3.28. The exponent on the AIDI in the formula is an important determinant of the level and distribution of country allocations. The aim is to allocate more resources to countries with greater infrastructure needs while continuing to reward good policy, institutional and portfolio performance and avoiding large fluctuations in country allocations. Having already established that the performance principle is respected under each of the scenarios under consideration, in order to determine the optimal exponent, Management undertook simulations and regressions with three exponents (-0.125, -0.25 and -0.5) and analyzed the results against the following criteria: (i) the volume of resources that is reallocated, (ii) the number of countries that see their allocation increase/decrease, (iii) the average impact on the 10 smallest and 10 largest allocations, (iv) the largest individual increase/decrease, and (v) the cumulative 5 largest increases/decreases (to measure concentration effect). (See Annex VII²¹) On the basis of this analysis, Management considers that the scenario with an AIDI exponent of -0.25 (AIDI^{-0.25}) yields the most balanced outcome in terms of the chosen criteria and therefore recommends this exponent.

Recommendations to Deputies

- 3.29. As set out above, Management firstly recommends to increase the minimum allocation to UA 15 million per cycle in ADF-13, in order to ensure meaningful engagement with all ADF countries through the PBA allocation. Furthermore, for future replenishments, Management proposes to discuss at each replenishment consultation the opportunity of adjusting the minimum allocation.
- 3.30. Secondly, to improve the alignment between the PBA system and the ADF's operational priorities based on the Bank Group Strategy for 2013-2022, Management recommends to add a new Cluster E on infrastructure development and regional integration to the CPIA questionnaire

²¹ Simulations assume that the GNI per capita and population exponents remain unchanged, a minimum allocation of UA 15 million and the coefficient of the new cluster E at 0.06.

and to include the AIDI in the PBA formula as an additional measure of need. Simulations confirm that these two measures result in higher allocations for countries that have significant infrastructure deficits, while maintaining the principle of rewarding good performance. Management recommends a coefficient of 0.06 for the CPIA Cluster E, and an AIDI exponent of -0.25.

3.31. The new PBA formula resulting from these recommendations would be:

$$A_i = (CPA_i)^4 \times \left(\frac{GNI}{P}\right)_i^{-0.125} \times P_i^1 \times AIDI_i^{-0.25}$$

$$CPA_i = 0.20 \text{ CPIA}_{(ABC)_i} + 0.58 \text{ CPIA}_{D_i} + 0.06 \text{ CPIA}_{E_i} + 0.16 \text{ PPA}_i$$

Where:

A_i	is the allocation for country i
$AIDI_i$	is the Africa Infrastructure Development Index score for country i
CPA_i	is the country performance assessment for country i
$CPIA_{(ABC)_i}$	is the rating for clusters A, B and C of the Country Policy and Institutional Assessment for country i
$CPIA_{D_i}$	is the rating of CPIA cluster D (Governance) for country i
$CPIA_{E_i}$	is the rating of the new cluster E for country i
$(GNI/P)_i$	is the gross national income per capita for country i
PPA_i	is the portfolio performance assessment for country i
P_i	is the population for country i

3.32. The main impacts on country allocations resulting from the increase of the minimum allocation to UA 15 million, adding a new cluster E in the CPIA questionnaire with a coefficient of 0.06 and incorporating the AIDI in the PBA formula with an exponent of -0.25 are summarized in Table 5 (more details are presented in Annex VIII). This package of measure results in:

- the two top performing quintiles continuing to receive more than two-thirds of PBA resources (67.54 percent).
- more PBA resources being allocated to countries with a low level of infrastructure: the 16 countries in the fourth and fifth AIDI quintiles receive 46.87 percent of resources, compared to 43.49 percent in 2012.
- more resources being allocated to countries with a small population: the fourth and fifth population quintiles receive 11.86 percent of resources, compared to 8.24 percent in 2012.

3.33. Fragile states are well represented among the 25 countries who see their allocation increase due to the adjustments.

Table 5: Impact of the Proposals on the Allocation of PBA Resources

(Simulations on 2012 PBA allocations)

# Higher Allocation			# Lower Allocation			Reallocated resources (UA Million)	Average increase (UA Million)	Average decrease (UA Million)
FS	NFS	Total	FS	NFS	Total			
16	9	25	1	15	16	75.05	3.00	-4.95

Resources per CPA Quintile (%)		
Quintile	Baseline	Scenario
1 st Quintile	25.10	22.66
2 nd Quintile	45.27	44.88
3 rd Quintile	14.04	13.18
4 th Quintile	7.08	8.86
5 th Quintile	8.51	10.41

Resources per AIDI Quintile (%)		
Quintile	Baseline	Scenario
1 st Quintile	7.27	7.86
2 nd Quintile	30.46	27.52
3 rd Quintile	18.78	17.75
4 th Quintile	17.62	18.46
5 th Quintile	25.87	28.41

Resources per GNI pc Quintile (%)		
Quintile	Baseline	Scenario
1 st Quintile	18.21	17.57
2 nd Quintile	17.76	16.68
3 rd Quintile	23.86	23.60
4 th Quintile	15.98	16.06
5 th Quintile	24.19	26.09

Resources per Population Quintile (%)		
Quintile	Baseline	Scenario
1 st Quintile	55.06	51.64
2 nd Quintile	21.16	21.13
3 rd Quintile	15.54	15.37
4 th Quintile	6.10	7.59
5 th Quintile	2.14	4.27

4. Proposals concerning the Fragile States Facility

- 4.1. At the first ADF-13 replenishment meeting, Deputies expressed a preference for addressing the challenges surrounding allocation of resources to fragile states through the FSF rather than the PBA system. The “Proposed Adjustments to the Bank Group’s Framework for Engagement in Fragile States” paper discusses various proposals for enhancing the flexibility, the responsiveness and the level of support to be provided through the three pillars of the FSF under ADF-13. This section focuses on the financial consequences of the recommendations made in the Fragile States paper, without repeating the arguments underlying these recommendations.

FSF Pillar I

- 4.2. The main objective of the revisions concerning FSF Pillar I is to strengthen the flexibility and responsiveness of the current approach, while maintaining sufficient predictability and incentives for improved performance. The key areas of proposed adjustment include revising the eligibility criteria; modifying the phase-out discount rates and top-up multiplier for third cycle recipients; and enhancing readiness to respond to emerging needs by keeping a portion of Pillar I resources unallocated, equivalent to 10 percent of the country-allocated resources.
- 4.3. Based on different assumptions regarding these elements, two scenarios are simulated to provide the range of the resource envelope that would be needed to support the potentially eligible countries in ADF-13. **Scenario 1** applies the revised eligibility criteria (yielding 15 eligible countries) while the 2x top-up factor and phase-out discounts agreed under ADF-12 are maintained. **Scenario 2** applies the revised eligibility criteria (15 countries) and introduces a modified top-up factor (reduced to 1.5x for third cycle recipients while maintaining the 2x top-up for second cycle recipients and pre-arrears clearance and newly engaging countries) and additional 10 percent phase-out discounts on the allocation for third cycle recipients and on the allocation for countries whose GNI per capita is greater than USD 1,000 (on a Purchasing Power Parity basis). Under these scenarios the estimated size of Pillar I for ADF-13 would range from **UA 607.6 million** to **UA 677.9 million**.

FSF Pillar II

- 4.4. Arrears clearance funds were targeted for Somalia, Sudan and Zimbabwe under ADF-12 but have not been used so far. All three countries are on the right track in terms of the technical requirements for arrears clearance support from the Bank Group and the commitment by respective governments to normalize relations with the international community. Management's expectation is that, if the current momentum is sustained and/or accelerated, all three could qualify for arrears clearance during the ADF-13 period.²²
- 4.5. The total amount of arrears of Somalia, Sudan and Zimbabwe to the Bank Group is projected to stand at UA 718 million at the end of ADF-13 period (see Fragile States paper, paragraph 3.26, Proposal 6; Table 2). Of this amount, the arrears to the AfDB (which can be cleared with ADF resources) come to UA 542 million. Deputies would recall that during the ADF-12 Mid Term Review it was agreed that FSF Pillar II resources would be rolled over into ADF-13 in the event that none of the eligible countries qualify for arrears clearance support during the remainder of the ADF-12 period. These resources amount to UA 362.3 million (ref. Table 1), leaving a gap of UA 179.8 million. Management therefore proposes to allocate **UA 179.8 million** to Pillar II from the ADF-13 replenishment in order to be able to clear the full amount of arrears of Somalia, Sudan and Zimbabwe to the AfDB as these countries qualify.
- 4.6. The three countries' ADF arrears are projected to amount to UA 173.7 million. As countries become eligible for arrears clearance, Management will make maximum efforts to mobilize resources from both internal and external sources for the purpose of clearing these arrears.

FSF Pillar III

- 4.7. During ADF 12, Pillar III resources were allocated to 19 countries and 3 regional institutions to carry out capacity building projects and access technical assistance for institutional development. Following the independent evaluation of the Bank's engagement in fragile states, actions are being undertaken to strengthen the design and delivery of FSF Pillar III operations with the view to enhance their quality, impact and contribution to state building (see Annex IX "Reforming Targeted Support (Pillar III) operations" of the Fragile States paper).
- 4.8. Plans are underway to modify the current Pillar III Operational Guidelines following the adoption of the new fragile states strategy, in order to align the Pillar III eligibility criteria and resource allocation approach with that new strategy. Management proposes that the resource envelope for Pillar III during ADF-13 be set at the average of the resources available under ADF-11 (UA 25.39 million) and ADF-12 (UA 62.68 million) i.e. **UA 44 million**.

Total FSF resource allocation under ADF-13

- 4.9. With the scenarios presented above, Management estimates that the volume of ADF-13 resources required for the FSF will range from UA 831.4 million to UA 901.7 million (Table 6). This amount represents an increase of 8.8 or 18 percent, respectively, compared to ADF-12.

Table 6: Estimated allocation of ADF-13 resources to the FSF under two scenarios for Pillar I

(UA million)

	Scenario 1	Scenario 2 (modified top-up factor and discounts)
Pillar I		
country-allocated	616.3	552.4
unallocated (10%)	61.6	55.2
Pillar II (3 countries)		
AfDB Arrears (gap)	179.8	179.8
Pillar III (all eligible FS)		
fixed amount	44.0	44.0
Total FSF envelope	901.7	831.4

²² Discussed in more detail in the Fragile States paper (Annex VIII)

- 4.10. The ADF-12 Report determined that the decision on the disposition of FSF resources unused at the end of the ADF-12 cycle will be made by Deputies in the context of the ADF-13 discussions. Management proposes to maintain the arrangements agreed in 2010 for the unused ADF-11 resources, namely that (i) the balance of unused FSF Pillars I, II and III resource at end-2013 will be carried over to ADF-13 within the same pillar, and (ii) unused resources in the PBA and RO envelopes will be carried over to ADF-13 and folded into the allocable pool of ADF-13 PBA resources.

5. Proposals concerning the Regional Operations Envelope

- 5.1. The infrastructure needs on the African continent remain enormous. Many national and regional programs and initiatives attempt to address these needs, including the New Partnership for Africa's Development, the Program for Infrastructure Development in Africa, the EU-Africa Partnership for African Infrastructure, the World Bank Infrastructure Strategy, and the Africa Infrastructure Finance Facility currently being developed by the AfDB. In this context, the ADF is called upon to play its part - and it will continue to support infrastructure and regional integration, two priority areas of the recently adopted Strategy for 2013-2022 - through all the instruments at its disposal, including country PBA allocations, the FSF and the RO envelope.
- 5.2. The new Bank Group Regional Integration Strategy, expected to be adopted before the end of the year, will operationalize the Strategy for 2013-2022 as concerns regional integration and will articulate the vision for ADF-13. In complement, a revised Regional Operations framework will likewise be proposed for Board approval before the end of 2013.
- 5.3. The cost-sharing framework whereby the RO envelope multiplies the participating countries' contributions from their PBA allocations has provided financial incentives to unlock critical bottlenecks to regional integration. Within the flexibilities of the RO framework, during ADF-12 Management lowered the standard multiplier from 2x to 1.5x. After the adoption of the Program for Infrastructure Development in Africa, this allowed the ADF to support a greater number of transformational infrastructure projects with a regional dimension.
- 5.4. In the preparation of the new Regional Integration Strategy, two pertinent issues are currently emerging: providing mechanisms for the stabilization of fragile regions and the need to tackle soft aspects of regional integration.

Use of FSF resources for regional operations

- 5.5. The new Regional Integration Strategy will aim to accelerate inclusive growth and the transition to green growth through enhanced movement of people, goods and services. To achieve this goal, regional institutions will need to be strengthened, as will regional infrastructure, the latter supporting connectivity and value chain production. Additional efforts will be directed towards building larger and more competitive markets, notably through investments aimed at stabilizing fragile regions of the continent by integrating them more closely with their neighbors.
- 5.6. Furthermore, recent examples have shown that conflict prevention costs far less than post-conflict reconstruction, not only in financial but also in human and social terms. It is easier to respond to fragility at a regional level when (a) neighboring countries have a mutually beneficial stake in each other's economies and are less likely to undermine each other's stability and (b) regions can prevent conflicts from spilling over borders by jointly addressing the social, environmental and economic stresses that affect their populations.
- 5.7. Under the current RO framework, fragile states face the constraint that they cannot use their FSF Pillar I allocations to leverage funding from the RO envelope, as FSF resources are currently not eligible for the incentive mechanism. Furthermore, countries in or exiting from situations of fragility understandably focus on national priorities. Drawing lessons from past and ongoing dialogue with authorities, more incentives are needed to trigger the interest of policy makers in regional solutions with benefits in the longer term, rather than short-term national investments.

- 5.8. To answer these two challenges, Management proposes the following:
- to allow FSF Pillar I allocations to leverage RO envelope funding;
 - to provide additional incentive for fragile countries by offering a differentiated multiplier – 2 times for the countries eligible to FSF Pillar I, versus 1.5 times for other ADF recipients. Concretely this would mean that as of ADF-13, for every UA that a Pillar I-eligible country contributes to an RO from either its PBA or its FSF Pillar I allocation, the RO envelope would contribute up to 2 UA.
- 5.9. These policy changes resonate with the discussions in the paper on engagement in Fragile States. They would be implemented through the revised and comprehensive Regional Operations framework to be proposed for Board approval before the end of 2013.

Leveraging the RO envelope for policy reforms

- 5.10. Implementing the “soft” policy aspects of regional infrastructure services has been a challenge. Some regional capacity building programs have been developed under the regional public goods exemption regime. However, countries require additional incentives to take responsibility and mobilize national funds for such purposes. This was highlighted by the independent evaluation of the Bank’s multinational operations as well as the review of the Regional Integration Strategy (2009-2012)²³. Though past interventions have been successful at improving physical interconnectivity, insufficient progress has been recorded in driving policy reforms related to regional integration: customs, harmonization, standardization, border facilitation, as well as the implementation of protocols and cooperation agreements which ease the movement of goods and services.
- 5.11. One way to address this challenge could be through innovative use of the existing RO incentive framework by implementing program-based operations that combine the hard and soft aspects of regional integration. Such operations could significantly contribute to fully delivering infrastructure services with greater development impact. For example, if a cross-border road is funded, separate national reform programs including trade policy measures could be designed in the concerned countries, leveraging additional funding from the RO envelope, under the same conditions currently applied to investment projects. By providing the right incentives, countries could be encouraged to translate regional agreements into national laws.
- 5.12. Before undertaking further work, Deputies’ views are sought on the use of the RO incentive mechanism to promote policy reforms, including through program-based operations.

Exceptions to cost-sharing for countries with small allocations

- 5.13. As highlighted above, the demand for funding for ROs has far outstripped the supply of resources in ADF-12. Going forward, this demand is expected to continue to grow as the Bank’s clients expect it to play a prominent role in facilitating integration initiatives and implementing the Program for Infrastructure Development in Africa. Management applied a balanced multiplier to extend the overall share of ADF going towards regional integration (par. 5.1), hence providing better accompaniment to countries implementing PIDA priorities, while maintaining the relative size of the RO set-aside.
- 5.14. One operational challenge that was difficult to address was the perceived disproportionate benefit that countries with a small PBA allocation derive from the RO envelope. The cumulative contributions to ROs by countries with a PBA below UA 20 million are capped to 10 percent of their PBA²⁴, while potentially offering them an unlimited leverage of RO resources. For example, in one RO approved during ADF-12, a small allocation country achieved a multiplier effect of 85 to 1 with its contribution of less than UA 1 million.
- 5.15. In light of a potentially unlimited incentive that also surpasses a country’s absorptive capacity, full commitment to and ownership of regional projects also needs to be ensured. To improve the perception of equity and promote a stronger appropriation of regional projects by countries with

²³ Bank Group Regional Integration Strategy, 2009 - 2012 – ADF/BD/WP/2009/22

²⁴ i.e. they contribute at least 1/3 (now 40 percent) of project costs until such contributions reach 10 percent of their PBA allocation, after which all costs are covered by the RO envelope

small allocations, Management proposes to require a contribution of at least 40 percent of project costs up to 10 percent of their PBA for each regional project undertaken. This would curtail the tendency to concentrate several regional projects within the same ADF cycle to benefit from the unlimited leverage offered once the 10 percent has been reached. An illustration is the case of Central African Republic which initially programmed 4 regional operations for ADF-12, significantly beyond the country's absorptive capacity.

- 5.16. This policy change would also be implemented through the revised Regional Operations framework to be proposed for Board approval before the end of 2013.

6. Proposals concerning new financing instruments

- 6.1. During the first replenishment meeting six possible new instruments were presented for Deputies' guidance, and initial feedback was provided on the specific options. Deputies generally favored new instruments designed to leverage ADF resources and catalyze more private sector financing in ADF countries. While the potential multiplier effect of the options was underlined, some Deputies expressed concern that too many or too large set asides could undermine the PBA approach.
- 6.2. The "Innovative Financial Instruments" paper presents the further work done by Management following the first replenishment meeting and recommends the introduction of two new instruments in ADF-13. This section concentrates on the financial consequences of this recommendation, without repeating the underlying arguments.

Partial Credit Guarantee

- 6.3. The first instrument proposed by Management, the ADF Partial Credit Guarantee, will be financed through countries' PBA allocations. As is the case for the existing Partial Risk Guarantee, 25 percent of the face value of each guarantee will be deducted from the country's PBA allocation. The introduction of this instrument therefore has no consequences for the allocation of resources between the PBA envelope, FSF and RO envelope in ADF-13.

Private Sector Facility

- 6.4. The second instrument proposed by Management, the Private Sector Facility (PSF), is a guarantee instrument that will extend credit enhancement to the AfDB to support the development of privately funded transformational projects in ADF countries. With this credit enhancement, the AfDB will be able to undertake more private sector operations in ADF countries than is currently possible. An in-depth description of the PSF is provided in the "Innovative Financial Instruments" paper.
- 6.5. To implement the PSF, a seed contribution is required. Since the Facility is not country-specific but available for operations in all ADF countries, Management envisages to allocate UA 165 million from ADF-13 resources for this purpose. The PSF is estimated to have a leverage of 4x, in other words 1 UA of PSF resources can leverage 4 UA of private sector financing from the AfDB²⁵. It is thus expected that the seed contribution would leverage UA 660 million of AfDB private sector operations. Given that the average share of the AfDB in a private sector operation is 20 percent of the total investment, the UA 660 million of AfDB private sector financing is expected to generate UA 3.3 billion of additional private sector investments on the ground.

²⁵ Assuming an average portfolio transaction rated 5 (on the Bank's scale of 1 to 10, where 10 is the most risky) with adequate collateral coverage (i.e. Loss Given Default of 45 percent) and that the PSF will cover 50 percent of the Loss Given Default (for additional information, see ADF-13 Innovative Financing Instruments paper).

7. ADF-13 Resource Allocation Scenarios

Technical Contingencies

- 7.1. To be consistent with the ADF-12 resource allocation methodology, technical contingencies of 3 percent of donor contributions will be taken into account. This translates to approx. 2.39 percent of overall resources.

Allocation Methodology

- 7.2. In the scenarios that follow, the allocation of ADF-13 resources to various envelopes is calculated using the following formulas:

Total ADF-13 resources	(A) = (1) + (2)
Total donor contributions (subscribed amounts)	(1)
Internally generated resources	(2)
Add carry-overs from previous replenishments	(B) = UA 629 million
Less upfront deductions	(C) = (3) + (4) + (5)
Exchange rate contingency	(3) = 1%*(1)
Contingency for acceleration	(4) = 2%*(1)
Contingency for qualified and unsubscribed contributions	(5) = UA 350 million
ADF-13 resources available for allocation	(D) = (A) + (B) - (C)
Fragile States Facility	(6) = UA XX million
Regional Operations envelope	(7) = 20%*(D)
Set-aside proposed for Private Sector Facility	(8) = UA 165 million
Country Performance-Based Allocations	(E) = (D) - (6) - (7) - (8)

Presentation of the Scenarios

- 7.3. Table 7 presents, in nominal and percentage terms, how the ADF-13 resources would be allocated among the PBA envelope, RO envelope, the FSF and the Private Sector Facility under the two scenarios for the FSF presented in Section 4 (Table 6) and the three replenishment scenarios included in the ADF-13 Financing Framework and Capacity paper: Low, Consolidation and Transformation²⁶. Depending on the replenishment scenario, the size of the FSF would vary from 12.0 percent (Scenario 2, Transformation) to 17.3 percent (Scenario 1, Low) of ADF-13 resources. The RO envelope is fixed at 20 percent of resources, and the UA 165 million proposed for the Private Sector Facility implies between 2.4 percent and 3.2 percent. Consequently the PBA envelope would comprise between 59.6 percent (Scenario 1, Low) and 65.6 percent (Scenario 2, Transformation) of resources.

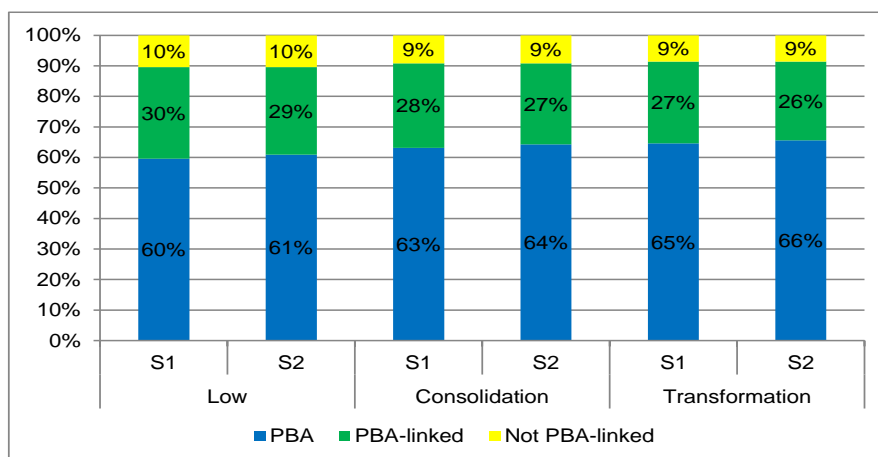
²⁶ Low scenario: the ADF-12 subscriptions from donors are adjusted by the cumulative SDR inflation rate (6.84 percent); Consolidation scenario: subscriptions increase such that a flat real growth in total ADF resources vis-à-vis ADF-12 is attained; Transformation scenario: subscriptions increase such that 10 percent real growth in total ADF resources vis-à-vis ADF-12 is achieved.

Table 7: ADF-13 Resource Allocation under Two Scenarios for the FSF

	Low		Consolidation		Transformation	
Scenario 1	UA million	%	UA million	%	UA million	%
Total ADF-13 Resources	5060		6203		6823	
Net Allocable Resources	5218	100	6333	100	6939	100
Fragile States Facility	902	17.3	902	14.2	902	13.0
<i>of which Pillar I: supplemental</i>	678	13.0	678	10.7	678	9.8
<i>of which Pillar II: arrears clearance</i>	180	3.4	180	2.8	180	2.6
<i>of which Pillar III: targeted</i>	44	0.8	44	0.7	44	0.6
Regional Operations envelope	1044	20.0	1267	20.0	1388	20.0
Set-aside for Private Sector Facility	165	3.2	165	2.6	165	2.4
Performance-Based Allocation resources	3108	59.6	4000	63.2	4484	64.6
Scenario 2	UA million	%	UA million	%	UA million	%
Total ADF-13 Resources	5060		6203		6823	
Net Allocable Resources	5218	100	6333	100	6939	100
Fragile States Facility	831	15.9	831	13.1	831	12.0
<i>of which Pillar I: supplemental</i>	608	11.6	608	9.6	608	8.8
<i>of which Pillar II: arrears clearance</i>	180	3.4	180	2.8	180	2.6
<i>of which Pillar III: targeted</i>	44	0.8	44	0.7	44	0.6
Regional Operations envelope	1044	20.0	1267	20.0	1388	20.0
Set-aside for Private Sector Facility	165	3.2	165	2.6	165	2.4
Performance-Based Allocation resources	3178	60.9	4070	64.3	4554	65.6

- 7.4. Figure 8 demonstrates that despite the reduction in the percentage of resources that would be allocated directly through the PBA system as compared to ADF-12, the percentage of resources that is linked to PBA (i.e. allocated on the basis of performance) still remains around 90 percent, like in ADF-11 and ADF-12 (see Figure 4). Performance thus remains the bedrock of the resource allocation system.

Figure 8: Share of Allocations Linked to the Performance-Based Allocation System under Two Scenarios for the FSF



Notes: PBA=Performance-Based Allocations; PBA-linked = FSF Pillar I + regional operations with cost-sharing; Not PBA linked = FSF Pillars II and III + regional operations exempted from cost-sharing + Private Sector Facility

8. Differentiated and Hardened ADF Lending Terms

- 8.1. As set out in detail in the ADF-13 Financing Framework and Capacity paper, during ADF-13 differentiated lending terms will be applied to more and less advanced ADF-only countries as well as blend, gap and graduating countries. The new terms will apply only to the loan portion of the allocation of those countries that are eligible for loans, i.e. that have a low (“green”) or moderate (“yellow”) risk of debt distress. Among the ADF-only countries, two groups are distinguished on the basis of the Africa Human and Infrastructure Development Index, resulting in:
- a more economically advanced group of ADF-only countries that will receive loans on “advance” terms (concessional level of 51 percent, the same level being proposed for all IDA countries in the context of the IDA-17 replenishment); and
 - a less economically advanced group of ADF-only countries, including the fragile states, that will receive “regular” lending terms with a concessional level of 61 percent.
- 8.2. The lending terms for blend, gap and graduating countries will also be hardened to reach a concessional level of 35 percent, in alignment with the IDA lending terms for blend and gap countries.

9. Conclusion and Recommendations

- 9.1. Management makes the following proposals, for Deputies’ guidance:
- 9.2. As concerns the PBA system, Management firstly recommends to increase the minimum allocation to UA 15 million per cycle in ADF-13. Secondly it proposes to add a new Cluster E on infrastructure development and regional integration to the CPIA questionnaire, with a coefficient of 0.06 in the performance component of the PBA formula, and to include the AIDI in the PBA formula with an exponent of -0.25.
- 9.3. Concerning the FSF, Management presents two scenarios for the estimated size of FSF Pillar I under ADF-13. Secondly, it proposes to allocate UA 179.8 million to Pillar II in order to be able to clear the full amount of arrears of Somalia, Sudan and Zimbabwe to the AfDB as these countries qualify. Thirdly, Management proposes that the resource envelope for Pillar III be set at the average of the resources available under ADF-11 and ADF-12 i.e. UA 44 million.
- 9.4. Concerning the ROs envelope, Management firstly proposes to allow FSF Pillar I allocations to leverage RO envelope funding and to offer a differentiated multiplier of 2 times for the countries eligible to FSF Pillar I, versus 1.5 times for other ADF recipients. Secondly, Management seeks Deputies’ views on the use of the RO incentive mechanism to promote policy reforms. Thirdly, for countries with small PBA allocations, Management proposes to require a contribution of at least 40 percent of project costs up to 10 percent of their PBA for each regional project undertaken.
- 9.5. Management envisages to allocate UA 165 million from ADF-13 resources to the Private Sector Facility.
- 9.6. Concerning the disposition of unused ADF-12 resources, Management proposes to maintain the arrangements agreed in 2010 for the unused ADF-11 resources, namely that (i) the balance of unused FSF Pillars I, II and III resources at end-2013 will be carried over to ADF-13 within the same pillar, and (ii) unused resources in the PBA and ROs envelopes will be carried over to ADF-13 and folded into the allocable pool of ADF-13 PBA resources.

Annex I: Classification of Regional Member Countries

A. Countries eligible only for ADF-resources*	B. Countries eligible for a blend of AfDB and ADF resources
<ol style="list-style-type: none"> 1. Benin 2. Burkina Faso 3. Burundi 4. Cameroon 5. Central African Republic 6. Chad 7. Comoros 8. Congo, Democratic Republic 9. Congo, Republic 10. Côte d'Ivoire 11. Djibouti 12. Eritrea 13. Ethiopia 14. Gambia 15. Ghana 16. Guinea 17. Guinea-Bissau 18. Kenya 19. Lesotho 20. Liberia 21. Madagascar 22. Malawi 23. Mali 24. Mauritania 25. Mozambique 26. Niger 27. Rwanda 28. Sao Tomé & Príncipe 29. Senegal 30. Sierra Leone 31. Somalia 32. South Sudan*** 33. Sudan 34. Tanzania 35. Togo 36. Uganda 37. Zambia 38. Zimbabwe 	<p>Nigeria</p> <p>C. Countries eligible only for AfDB resources</p> <ol style="list-style-type: none"> 1. Angola** 2. Algeria 3. Botswana 4. Cape Verde - in transition (2011-2015) 5. Egypt 6. Equatorial Guinea 7. Gabon 8. Libya 9. Mauritius 10. Morocco 11. Namibia 12. Seychelles 13. South Africa 14. Swaziland 15. Tunisia

* Except limited AfDB lending for enclave and private sector projects.

****** *Angola has completed its two-year transition period (2011-2012) to AfDB-only.*

*** Pending completion of the membership process.

Annex II: Status of ADF Subscriptions and Payments Received as of 22 May 2013

State Participants	Units of Oblig.	Amounts Pledged in UA	Amounts Pledged in Currency	Subscription in UA	Qualified Portion in UA	Payment Received in UA
Argentina	USD	9,771,350.40	15,000,000.00	9,771,350.40	9,771,350.40	-
Austria	EUR	95,706,247.84	107,475,245.14	95,706,247.84		95,706,247.72
Belgium	EUR	84,241,446.01	94,600,616.63	84,278,392.91		84,278,392.91
Brazil	USD	9,607,953.88	14,749,170.00	9,607,953.88		9,607,953.88
Canada	CAD	204,447,957.71	325,607,906.40	204,447,957.71		204,447,957.71
China	USD	83,921,666.45	128,828,150.17	83,921,666.45		83,921,666.45
Denmark	DKK	77,325,112.93	646,194,370.02	77,293,928.58		77,293,928.58
Egypt	USD	1,302,846.72	2,000,000.00	1,302,846.72		1,302,846.72
Finland	EUR	112,023,670.97	125,799,221.79	112,023,670.97		112,023,671.16
France	EUR	356,198,295.59	400,000,000.00	356,198,295.59		356,198,295.59
Germany	USD	399,991,166.25	614,026,439.30	399,991,166.25		399,991,166.25
India	INR	9,427,030.90	663,363,667.00	9,427,030.90		9,427,030.91
Italy	EUR	194,266,872.67	218,155,870.00			-
Japan	JPY	274,594,889.82	38,437,325,866.18	274,594,889.82		183,063,259.88
Korea	KRW	53,857,278.51	94,774,413,588.95	53,857,278.51		53,857,278.51
Kuwait	USD	7,361,324.55	11,300,369.32	7,361,324.55		7,361,325.00
The Netherlands	EUR	201,061,742.00	225,786,304.41	201,061,742.00		201,061,741.81
Norway	NOK	179,774,236.09	1,634,217,918.00	179,774,236.09		179,774,236.09
Portugal	EUR	29,564,458.53	33,200,000.00			-
Saudi Arabia	USD	19,542,700.80	30,000,000.00	19,542,700.80		19,542,700.80
South Africa	ZAR	10,424,062.28	119,969,803.15	10,424,062.28		10,883,181.80
Spain	EUR	122,681,727.81	137,767,899.88	122,681,727.81	108,433,795.99	14,247,931.82
Sweden	SEK	178,035,844.10	1,986,410,005.50	178,035,844.10	-	178,035,844.10
Switzerland	USD	100,838,740.95	154,797,551.23	100,838,740.95		100,838,740.95
United Kingdom	GBP	572,397,673.38	566,994,239.34	572,397,673.38		381,598,448.70
United States Of America	USD	381,070,168.92	584,980,816.31	381,070,168.92	248,598,017.27	132,472,151.65
Supplementary contribution		7,170,154.90		7,170,154.90		7,170,154.90
Total		3,776,606,620.98		3,552,781,052.32	366,803,163.66	2,904,106,153.86

Annex III: Allocation of PBA Resources for ADF-12

Figure III-1 presents the distribution of PBA resources by performance quintile over the 3 years of the ADF-12 cycle. While some countries have shifted from one quintile to another, the top performance quintile consistently attracts the most resources.

Figure III-1: PBA Resources per CPIA Quintile, 2011-2013

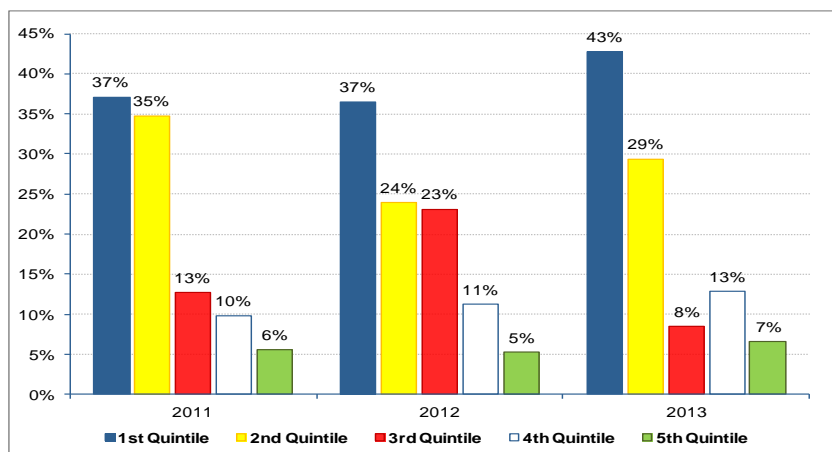


Figure III-2 presents the average per capita allocations by performance quintile for each year of the ADF-12. In general, it also shows higher allocations for higher-performing quintiles, and lower allocations for lower-performing quintiles. Average per capita allocation calculations can be vulnerable to the effect of outliers. The largest and smallest population countries, combined with allocation caps and the minimum allocation, can distort results. For that reason, the data presented in Figure III-2 exclude the outliers.

Figure III-2: Average per capita PBA allocations by CPIA Quintile, 2011-2013 (without outliers)

(UA)

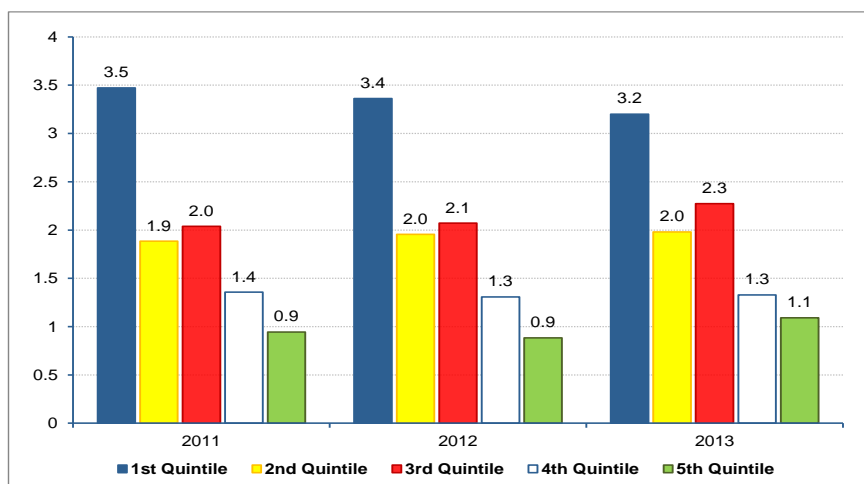


Table III-1 shows the 5 largest country allocations under ADF-12 in total volume.

Table III-1: Top 5 PBA recipients, ADF-12

Country Allocations in Units of Account	
1. Ethiopia	404.7 million
2. Tanzania	382.6 million
3. Kenya	357.2 million
4. Uganda	265.6 million
5. Ghana	230.4 million

Figure III-3 presents allocations by GNI per capita quintile under ADF-10, ADF-11 and ADF-12. It shows that the system allocates fewer resources to the two highest GNI per capita quintiles and more resources to the bottom three quintiles, as intended. However, the effect is not completely linear, most likely due to the higher weight of the performance assessment in the formula as compared to the GNI per capita factor.

Figure III-3: PBA resources by GNI per capita quintile, ADF-10 to ADF-12

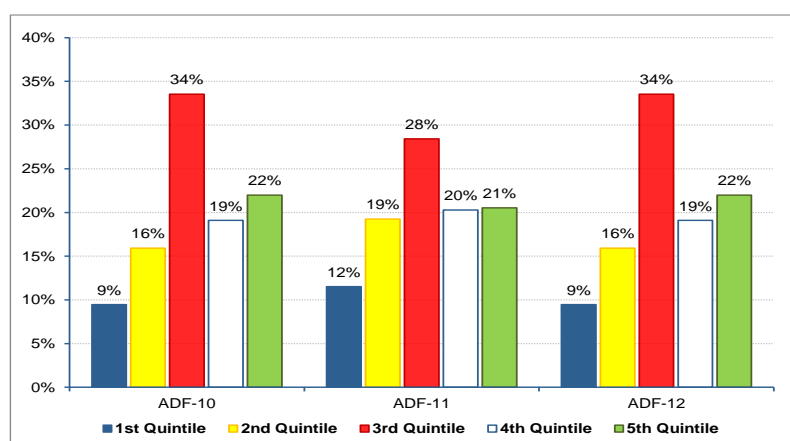


Figure III-4 presents allocations by population quintile under ADF-10, ADF-11 and ADF-12. The figure clearly demonstrates the effect of population as a needs component in the PBA formula over the three previous ADF cycles. The majority of resources is allocated to the most populous countries of the first population quintile.

Figure III-4: PBA resources by population quintile, ADF-10 to ADF-12

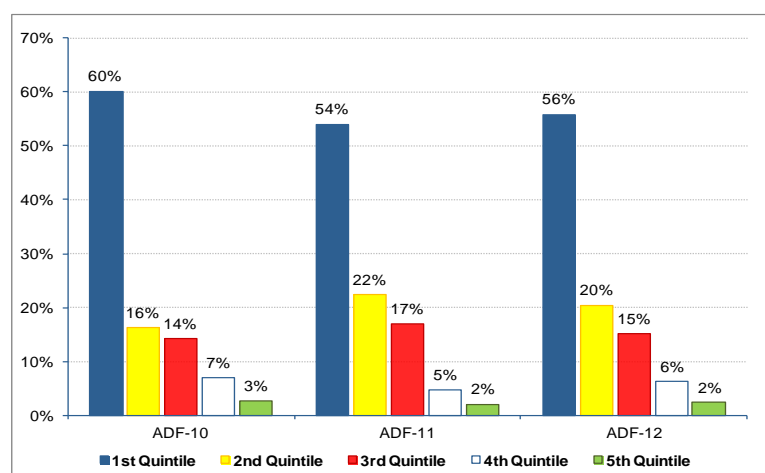
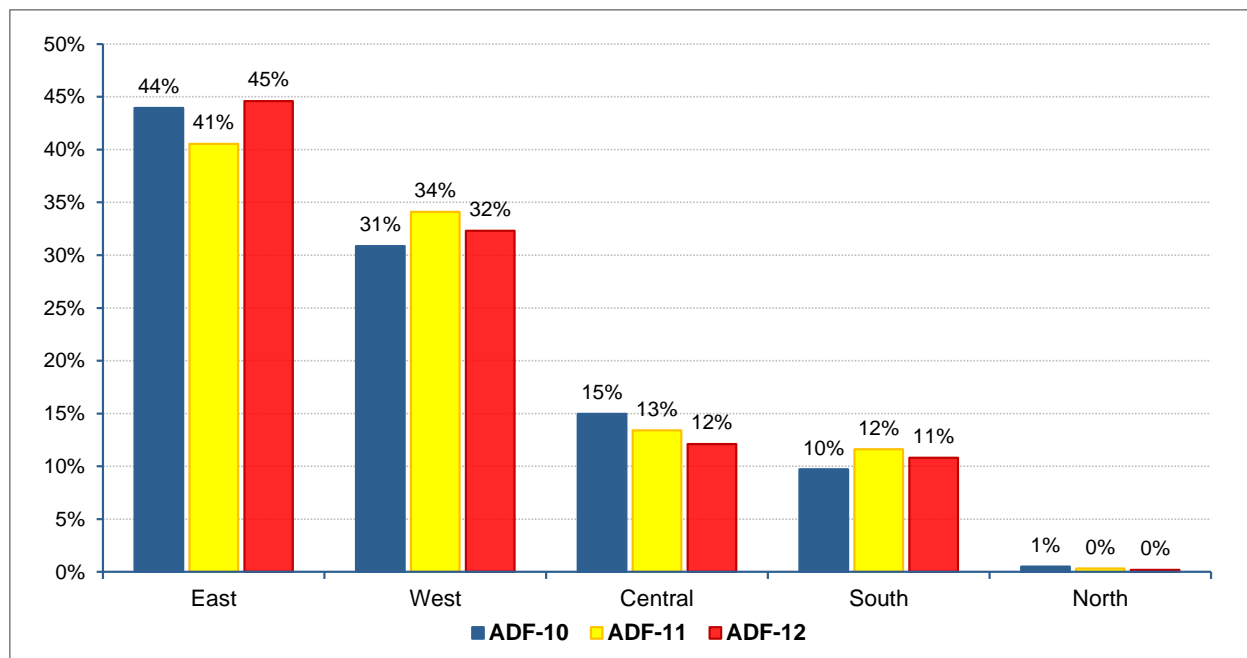


Figure III-5 presents the geographical distribution of PBA resources under ADF-10, ADF-11 and ADF-12. In general, it demonstrates a stable resource distribution by region over the previous three ADF cycles. Countries of the East region receive the largest share of PBA resources (around 43 percent of the resource volume) over the three cycles. The West region comes in the second place with around 32 percent of resource volume in each cycle.

Figure III-5: Geographical distribution of PBA resources, ADF-10 to ADF-12



Annex IV: A Comparative Table of Performance Based Allocation Systems - PBA Formulae

Institution	Began PBA	Allocation Formula			Min. Alloc.	Ceiling
		Needs Factors	Performance Factors	Result		
AfDB	1999	$POP^{1.0} \times GNIPC^{-0.125}$	$\times [(0.26CPIA_{A-C} + 0.58CPIA_D + 0.16PORT)]^{4.0}$	= Alloc. share weight	SDR 5 million/ replenishment	
AsDB	2001	$POP^{0.6} \times GNIPC^{-0.25}$	$\times [(ES_CPIA^{0.7} \times PORT^{0.3}) \times GOV]^{2.0}$	= Alloc. share weight	None	The largest AsDF borrowers are subject to a ceiling.
CDB	2000	$LogPOP \times POOR^{0.1} \times GNPPC^{-0.9} \times VUL^{2.0}$	$\times [0.7CPIA + 0.3PORT]^{2.0}$	= Alloc. share weight		Haiti is subject to a fixed ceiling and does not get a formula-based allocation.
EU (ACP)		$LogPOP \times 0.2GNIPC^{-1.0} \times 0.2HDI^{-1.0} \times DEBT \times VUL$		= Alloc. share weight		
GEF	2006	GBI ^{0.8} (The Global benefits Index is calculated separately for the two focal areas: The GBI for Biodiversity is 0.8 x TERRESTRIAL BIODIVERSITY + 0.2 MARINE BIODIVERSITY (Terrestrial Biodiversity is defined as 0.55 x represented species + 0.20 x threatened species + 0.15 x represented eco-regions + 0.10 * threatened eco-regions; and Marine Biodiversity is defined as represented marine species The GBI for Climate change is defined as Baseline GHG emissions X carbon intensity adjustment factor.)	$[0.2CPIA + 0.10PORT + 0.70CEPIA]$ (The World Bank CPIA scores are used, with 0.7 weight to environmental criteria and 0.2 weight to "broad framework indicator" (governance). Portfolio performance, PORT, is judged on ten years of GEF and World Bank environmental projects.)	= Alloc. share weight for each focal area	\$1 million for each focal area	
IDB (IFF)	2002 to 2008 (IFF discontinued after 2007)	$(0.133FUND) \left(\frac{POP}{\sum POP} \right) + (0.133FUND) \left(\frac{\frac{1}{GNIPC}}{\sum \frac{1}{GNIPC}} \right) + (0.133FUND) \left(\frac{DEBT}{\sum DEBT} \right)$	$+ (0.6FUND) \times \left[\frac{0.7CIPE + 0.3PORT}{\sum (0.7CIPE + 0.3PORT)} \right]$	= 50% \$ Alloc. (Component I)		
IDB (FSO)	2002 (current formula since 2007)	$Pop^{0.50} \times GNIPC^{-1}$	$\times [0.3PORT + 0.7CIPE]^{2.0}$	= 50% \$ Alloc. (Component II)		US\$25 Million per year
		$(0.22FUND) \left(\frac{POP}{\sum POP} \right) + (0.133FUND) \left(\frac{\frac{1}{GNIPC}}{\sum \frac{1}{GNIPC}} \right)$	$+ (0.6FUND) \times \left[\frac{0.7CIPE + 0.3PORT}{\sum (0.7CIPE + 0.3PORT)} \right]$	= 50% \$ Alloc. (Component I)		US\$54 Million per year
IFAD	2005	Rural $POP^{0.45} \times GNIPC^{-0.25}$	$\times [0.2CPIA + 0.35PORT + 0.45RuralCPIA]^{2.0}$	= Alloc. share weight	\$1 million	5% of total allocated
IDA-16	1977	$POP^{1.0} \times GNIPC^{-0.125}$	$\times [0.24CPIA_{A-C} + 0.68CPIA_D + 0.08PORT]^{5.0}$	= Alloc. share weight	SDR 9 / replenishment	SDR 19.8 per capita
IDA-17	1977	$POP^{1.0} \times GNIPC^{-0.125}$	$\times [0.24CPIA_{A-C} + 0.68CPIA_D + 0.08PORT]^{4.0}$	= Alloc. share weight	SDR 12 / replenishment	

Note: Variables: CIPE= Country Institutional and Policy Evaluation (IDB); CPIA = Country Policy and Institutional Assessment; DEBT = Debt service ratio; ES_CPIA= Economic and Social Performance Criteria in CPIA (for AfDB); FSO=Fund for Special Operations (IDB); Fund= Size of IFF and FSO Envelope; GOV= Average of the five criteria in the "public sector management cluster" for ADF; average of the six criteria in the Governance and Public Sector Performance for ADF; average of the five criteria in the public sector management cluster (Cluster D) for IDA; GNIPC = GNI per capita; GNPPC = GNP per capita; Log = logarithm; HDI = Human Development Index; PCEF= Post-conflict Enhancement Factor (AfDB); POOR = poverty variable; POP = Population; PORT= Portfolio rating; Rural CPIA= Performance rating on policies and institutions for rural development (IFAD); VUL = Country Vulnerability.

Annex V: Mapping the linkages between the current CPIA and the Strategy for 2013-2022 strategic priorities and focus areas


CPIA Cluster	#	CPIA Criterion/Sub-Criterion	Description	Weight	Strategy for 2013-2022 strategic priorities and special focus areas							
					I	RI	PSD	Gov.	ST	G	FS	AF S
A - ECONOMIC MANAGEMENT	1	Monetary Policy	Trends and policies regarding inflation, as well as the policy tools used to control it. Where relevant, the situation of Franc-zone countries vis-à-vis the convergence criteria of the regional central banks should also be discussed.	1								
		a. Monetary Policy		1								
	2	Fiscal Policy	The extent to which: (a) the primary balance is managed to ensure sustainability of the public fin.; (b) public expenditure/ revenue can be adjusted to absorb shocks if necessary; and (c) the provision of public goods, including infrastructure, is consistent with medium-term growth. Sustainability also refers to off-budget government spending and contingent liabilities.	1								
		a. Fiscal Policy		1	X							
	3	Debt Policy	Whether the debt management strategy aims at minimizing budgetary risks and ensuring long-term debt sustainability. Debt sustainability should also be discussed taking into account the joint Bank/Fund Debt Sustainability Framework and the AfDB traffic light system. The adequacy of the debt recording systems, the timelines of the public debt data, and the effectiveness of the debt management unit also need to be considered.	1								
		a. Debt Policy		1								
B -STRUCTURAL POLICIES	4	Economic Cooperation, Reg. Integration & Trade	This criterion is divided in two parts. The first part seeks to measure the extent to which a country supports regional organizations and its commitment to economic cooperation and regional integration initiatives. The second part focuses on trade and covers two areas: (a) trade regime restrictiveness focusing on the height of tariffs barriers, the extent to which non-tariff barriers (NTBs) are used, and the transparency and predictability of the trade regime; and (b) customs and trade facilitation, including the extent to which the 8 customs service is free of corruption, relies on risk management, processes duty collections and refunds promptly, and operates transparently.	1								
		a. Regional Integration and Economic Cooperation		0,5	X	X					X	X
		b. Trade restrictiveness		0,375								
		c. Customs/trade facilitation		0,125								
	5	Financial Development	Assessing sector's vulnerability to shocks, banking system's soundness, and adequacy of relevant institutional elements; Assessing efficiency, degree of competition, and ownership structure of the financial system, as well as its depth and resource mobilization strength; Access dimension covers institutional factors (such as the adequacy of payment and credit reporting systems), the regulatory framework affecting financial transactions (including collateral and bankruptcy laws and their enforcement) and the extent to which consumers and firms have access to financial services.	1								
		a. Financial stability		0,33								
		b. Sector's efficiency, depth, and resource mobilization strength		0,33								
		c. Access to financial services		0,33								X
	6	Business Regulatory Environment	Direct regulations of business activity and regulation of goods and factor markets. The analysis informing the rating on employment regulations consider hiring and firing costs for temporary and long-term contracts separately and take into account the overall cost of employing formal labor, i.e. payroll taxes and safety regulations. "Other labor institutions" should include the efficiency and reliability of labor courts as well as matching services that help employers find workers efficiently.	1								
		a. Regulations affecting entry, exit, and competition		0,33								
		b. Regulations of ongoing business operations		0,33								
		c. Regulations of factor markets (labor and land)		0,33								

C - POLICIES FOR SOCIAL INCLUSION/EQUITY	7	Gender Equality		1									
		a. Promotion of equal access for men and women to human capital development opportunities	This section must discuss progress in terms of achieving the Millennium Development Goal 3 on reducing gender disparity and include rating and rationale for CPIA Gender Equality Criterion, which assesses the extent to which the country has enacted and put in place institutions and programs to enforce laws and policies that: (a) promote equal access for men and women to human capital development opportunities; (b) promote equal access for men and women to productive and economic resources; and (c) give men and women equal status and protection under the law.	0,33									
		b. Promotion of equal access for men and women to productive and economic resources		0,33									
		c. Men/women equal status/protection under the law		0,33									
	8	Equity of Public Resource Use	The consistency of government spending with the poverty reduction priorities taking into account the extent to which: (a) individuals, groups, or localities that are poor, vulnerable, or have unequal access to services and opportunities are identified; (b) a national development strategy with explicit interventions to assist the groups identified has been adopted; and (c) the composition and incidence of public expenditures are tracked systematically and their results feedback into subsequent resource allocation decisions. The assessment of the revenue collection dimension takes into account the incidence of major taxes, e.g., whether they are progressive or regressive, and their alignment with the poverty reduction priorities. When relevant, expenditure and revenue collection trends at the national and sub-national levels should be considered.	1									
		a. Public Expenditures: Measurement		0,33									
		b. Public Expenditures: Priorities and strategies		0,33									
		c. Revenue Collection		0,33									
	9	Building Human Resources	Assessing national policies and public/private sector service delivery that affect access to and quality of the three dimensions hereheto. ECD refers to Early Child Development programs, including both formal/non-formal programs (which may combine education, health and nutrition interventions) aimed at children aged 0-6. Within each HD domain, the quality of both policies and program design and implementation should be assessed. In most cases, government performance will be stronger in some program areas than in others (i.e., basic health services vs. nutrition, primary education vs. tertiary, or HIV/AIDS vs. malaria). "Health" or "education" should reflect a judgment about the relative importance of each underlying policy/program in the country. Progress towards the Millennium Development Goals must also be taking into consideration.	1									
		a. Health and nutrition services		0,33									
		b. Education, ECD, training and literacy programs		0,33									
		c. Prevention/treatment HIV/AIDS, tuberculosis/malaria		0,33									
	10	Social Protection and Labor	Assessing government policies which reduce the risk of becoming poor, assist those who are poor to better manage further risks, and ensure a minimal level of welfare to all people. Within each area, policies and program design as well as implementation effectiveness should be assessed. Interventions include: social safety net programs, pension and old age savings programs; protection of basic labor standards; regulations to reduce segmentation and inequity in labor markets; active labor market programs, such as public works or job training; and community driven initiatives.	1									
		a. Social safety net programs		0,2									
		b. Protection of basic labour standards		0,2									
		c. Labour market regulations		0,2									
		d. Community driven initiatives		0,2									
		e. Pension and old age savings programs		0,2									
	11	Environmental Policies and Regulations	The extent to which environmental policies foster the protection and sustainable use of natural resources and the management of pollution. Assessment of environmental sustainability requires multi-dimension criteria (i.e. for air, water, waste, conservation management, coastal zones management, natural resources management).The two-way relationship between environmental degradation and poverty is well recognized. Poverty tends to lead to an extensive use of marginal land, water and forest resources, thus straining the already fragile and limited environment base. This question assesses the effectiveness of government's policies to protect the environment and promote sustainable development.	1									
		a. Environmental Policies and Regulations		1									


D - PUBLIC SECTOR MANAGEMENT AND INSTITUTIONS	12	Property Rights and Rule-based Governance	The extent to which private economic activity is facilitated by an effective legal system and rule-based governance structure in which property and contract rights are reliably respected and enforced. Each of four dimensions should be rated separately: (a) legal basis for secure property and contract rights; (b) predictability, transparency, and impartiality of laws affecting economic activity, and their application by the judiciary; (c) difficulty in obtaining business licenses; and (d) crime and violence as an impediment to economic activity.	1									
		a. Legal basis for secure property and contract rights		0,25									
		b. Predictability/transparency/impartiality of laws affecting economic activity		0,25									
		c. Difficulty in obtaining business licenses		0,25									
		d. Crime and violence as an impediment to economic activity		0,25								X	
	13	Quality of Budgetary and Financial Management	This criterion assesses the extent to which there is: (a) a comprehensive and credible budget, linked to policy priorities, which in turn are linked to a poverty reduction strategy; (b) effective financial 5 management systems to ensure that incurred expenditures are consistent with the approved budget, that budgeted revenues are achieved, and that aggregate fiscal control is maintained; (c) timely and accurate fiscal reporting, including timely and audited public accounts and effective arrangements for follow up; and (d) clear and balanced assignment of expenditures and revenues to each level of government. Each of these four dimensions should be rated separately. In countries without local governments with significant budgets, the fourth dimension should not be rated.	1									
		a. Comprehensive and credible budget		0,25	X	X				X	X		X
		b. Effective financial management systems		0,25									
		c. Timely and accurate fiscal reporting		0,25									
		d. Clear and balanced assignment of expenditures and revenues to each level of government		0,25									
	14	Efficiency of Revenue Mobilization	When assessing CPIA rating in Efficiency of Revenue Mobilization, the focus should be not only the tax structure as it exists on paper, but also actual revenue collection. Separate sub-ratings should be provided for (a) tax policy and; (b) tax administration.	1									
		a. Tax policy		0,5		X							
		b. Tax administration		0,5		X							
	15	Quality of Public Administration	The extent to which civilian central government staffs (including teachers, health workers, and police) are structured to design and implement government policy and deliver services effectively. Civilian central government staffs include the central executive together with all other ministries and administrative departments, including autonomous agencies. It excludes the armed forces, state-owned enterprises, and sub-national government. The key dimensions for assessment are: i) Policy coordination and responsiveness; ii) Service delivery and operational efficiency; iii) Merit and ethics; and iv) Pay adequacy and management of the wage bill.										
		a. Policy coordination and responsiveness		0,25									
		b. Service delivery and operational efficiency		0,25								X	
		c. Merit and ethics		0,25									
		d. Pay adequacy and management of the wage bill		0,25									
	16	Transparency, Accountability and Corruption in the Public Sector	The extent to which the executive can be held accountable for its use of funds and the results of its actions by the electorate and by the legislature and judiciary, and the extent to which public employees within the executive are required to account for the use of resources, administrative decisions, and results obtained. Both levels of accountability are enhanced by transparency in decision-making, public audit institutions, access to relevant and timely information, and public and media scrutiny. National and sub-national governments should be appropriately weighted.	1									
		a. Accountability of the executive to oversight institutions		0,33								X	
		b. Access of civil society to information on public affairs		0,33								X	
		c. State captured by narrow vested interests		0,33									

I: Infrastructure RI: Regional Integration PSD: Private Sector Development Gov.: Governance ST: Skills & Technology G: Gender FS: Fragile States AFS: Agriculture & Food Security

X: Criterion/Sub-Criterion partially/totally devoted to the theme but could be revised to better incorporate Strategy for 2013-2022 themes

 Criterion/Sub-Criterion somewhat linked to Strategy for 2013-22 theme

 Criterion/Sub-Criterion linked to Strategy theme

 Criterion/Sub-Criterion strongly linked to Strategy for 2013-22 theme

Annex VI: AIDI Methodological Note

The AfDB, as the host of the African Infrastructure Knowledge Program (AIKP)²⁷, developed the Africa Infrastructure Development Index (AIDI) in order to monitor infrastructure development progress and access to infrastructure across the continent.

The index is designed as a knowledge product to serve as a tool for researchers, analysts, investors, governments and development partners who desire to (i) have an accurate and up-to-date picture of the current state of infrastructure development and the extent to which access to infrastructure is effective in Africa, (ii) monitor and evaluate infrastructure's contribution to economic growth and productivity on the continent, (iii) design strategies and policies in the field of infrastructure, and (iv) deepen their understanding of the environment in which the private sector operates, and by doing so contribute to guiding investors' decisions to engage in Africa.

The AIDI has four major components: (i) Transport; (ii) Electricity, (iii) ICT and (iv) Water & Sanitation. These components are broken down into nine indicators that have a direct or indirect impact on productivity gains and generation of economic growth (see details in the table below).

The data for the nine indicators are sourced from well-known and reliable sources including the Food and Agriculture Organization (FAO), International Telecommunication Union (ITU), UNICEF and the World Bank. Scores for each country are available for a ten year period from 2000 to 2010²⁸. The AIDI will be updated and issued once a year. In future, data will be collected within the AIKP and the number of indicators to compute the AIDI is expected to increase in number and scope.

After compiling the data for the AIDI's four components, the components are normalized in order to adjust their values - which have originally been measured on different scales - and bring them to a common scale. The min-max normalization method is used to generate comparable values and adjust their distributions between 0 and 100.

The AIDI is then calculated following a linear combination of the four normalized components, where each component is multiplied by the ratio of the inverse of its standard deviation to the sum of the inverses of all components' standard deviations. This is a standard statistical method to reduce data variability and estimate a more robust index.

Therefore, for a given country, the AIDI is formulated as follows:

$$AIDI = \frac{1/\sigma_{Trans}}{Tot} \times \left(\frac{x_{Trans} - \min_{Trans}}{\max_{Trans} - \min_{Trans}} \right) + \frac{1/\sigma_{Elect}}{Tot} \times \left(\frac{x_{Elect} - \min_{Elect}}{\max_{Elect} - \min_{Elect}} \right) + \frac{1/\sigma_{ICT}}{Tot} \times \left(\frac{x_{ICT} - \min_{ICT}}{\max_{ICT} - \min_{ICT}} \right) + \frac{1/\sigma_{W\&S}}{Tot} \times \left(\frac{x_{W\&S} - \min_{W\&S}}{\max_{W\&S} - \min_{W\&S}} \right)$$

$$\text{Where: } Tot = 1/\sigma_{Trans} + 1/\sigma_{Elect} + 1/\sigma_{ICT} + 1/\sigma_{W\&S}$$

The AfDB Statistics Department has tested the variability of the AIDI over time and has found it to be a robust and stable index that gives a reliable picture of African countries' level of infrastructure development.

²⁷ <http://www.infrastructureafrica.org/>

²⁸ Further information on the methodology and scores for each country over the 2000-2010 period can be found on the Bank's website on economic briefs (select the Infrastructure topic in the menu Topic & Sector): Infrastructure): <http://www.afdb.org/en/documents/publications/economic-briefs/#c>

Table VI-1: Components and Indicators of the AIDI

Component	Indicator(s)	Definition of the indicator
Transport	- Total Paved Roads in km (per 10,000 inhabitants)	- The country's total road surface with crushed stone (macadam) and hydrocarbon binder or bituminized agents, with concrete, or with cobblestones. The indicator is measured in km per 10,000 inhabitants as a proxy of access to the paved road network.
	- Total Road Network in Km (per Exploitable Land Area in Km ²)	- The total road surface (both paved and non-paved roads) of a given country. The indicator is measured in km per exploitable land area in km ² . - Exploitable land area is the total surface area of a country minus the surface area of deserts, forest, mountains and other inaccessible areas.
Electricity	- Net Electricity Generation (million kilowatt hours per inhabitant)	- The total electricity production of a given country, including the energy imported from abroad. This includes both private and public energy generated. The indicator is measured by millions of kilowatt produced per hour and per inhabitant.
Information and Communication Technology (ICT)	- Total Phone Subscription (per 10,000 inhabitants)	- The total number of phone subscriptions in a country, both fixed telephone lines and mobile cellular telephone subscription, in a given year. For the purpose of the AIDI, the indicator is reported per 10,000 inhabitants. - <u>Fixed telephone lines</u> : Active line connecting the subscriber's terminal equipment to the public switched telephone network (PSTN) and which has a dedicated port in the telephone exchange equipment. - <u>Mobile cellular telephone subscriptions</u> : Refers to the subscriptions to a public mobile telephone service and provides access to Public Switched Telephone Network (PSTN) using cellular technology, including number of pre-paid SIM cards active during the past three months. This includes both analogue and digital cellular systems (IMT-2000 (Third Generation, 3G) and 4G subscriptions).
	- Number of Internet Users (per 100 inhabitants)	- The estimated number of Internet users out of total population. This includes those using the Internet from any device (including mobile phones) in the last 12 months. For the purpose of the AIDI, the indicator is reported per 100 inhabitants.
	- Total fixed (wired) broadband Internet subscriptions (per 100 inhabitants)	- Total Internet subscriptions using fixed (wired) broadband technologies to access the Internet. Subscriptions that have access to data communications (including the Internet) via mobile cellular networks are excluded. For the purpose of the AIDI, the indicator is reported per 100 inhabitants.
	- International Internet Bandwidth (Mbit/s)	- Total capacity of international Internet bandwidth in Mega Bits per Second (Mbit/s). If capacity is asymmetric (i.e., more incoming than outgoing), the incoming capacity should be provided. This is measured as the sum of capacity of all Internet exchanges offering international bandwidth.
Water & Sanitation	- Improved Water Source (as a percentage of population with access)	- Access to an improved water source refers to the percentage of the population with reasonable access to an adequate amount of water from an improved source, such as a household connection, public standpipe, borehole, protected well or spring, and rainwater collection. Unimproved sources include vendors, tanker trucks, and unprotected wells and springs. Reasonable access is defined as the availability of at least 20 liters a person a day from a source within one kilometer of the dwelling.
	- Improved sanitation facilities (as a percentage of population with access)	- Access to improved sanitation facilities refers to the percentage of the population with at least adequate access to excreta disposal facilities that can effectively prevent human, animal, and insect contact with excreta. Improved facilities range from simple but protected pit latrines to flush toilets with a sewerage connection. To be effective, facilities must be correctly constructed and properly maintained.

Source: FAO for Total road network indicator; ITU for the ICT indicators, UNICEF for Water and Sanitation indicators and World Bank for Total paved roads indicator.

Annex VII: Determining the appropriate AIDI exponent

Management undertook simulations with three possible exponents for the AIDI (-0.125, -0.25 and -0.5) and analyzed the results against the following criteria:

- the volume of resources that is reallocated,
- the number of countries that see their allocation increase/decrease,
- the average impact on the 10 smallest and 10 largest allocations,
- the largest individual increase/decrease, and
- the cumulative 5 largest increases/decreases (to measure concentration effect).

The simulations assume that the GNI per capita and population exponents in the PBA formula remain unchanged, a minimum allocation of UA 15 million and the coefficient of the new cluster E at 0.06. The results are shown in the table below.

Table VII-1: Criteria to determine the appropriate exponent of the AIDI

Criteria	Baseline Scenario ²⁹	AIDI -0.125		AIDI -0.25		AIDI -0.5	
Redistributed resources (UA Million)	-	63.16		75.05		109.21	
Sum of all increases	-	63.16		75.05		109.21	
Sum of all decreases ³⁰	-	-67.35		-78.69		-113.46	
# of countries with higher allocation	-	25		25		27	
# of countries with lower allocation	-	16		16		14	
Criteria		UA Million	%	UA Million	%	UA Million	%
Average impact on 10 smallest allocations		3.83	162.07	3.85	162.25	3.87	162.65
Average impact on 10 largest allocations		-5.44	-6.5	-5.75	-6.9	-6.52	-8.0
Largest individual increase (% of redistributed resources)		3.65	5.8	8.42	11.2	19.37	19.9
Largest individual decrease (% of redistributed resources)		-14.47	21.5	-16.97	21.4	-22.61	20.1
Cumulative 5 largest increases (% of redistributed resources) (% of their cumulative allocation)		16.99	26.9 27.7	24.68	32.9 21.9	53.45	48.9 27.1
Cumulative 5 largest decreases (% of redistributed resources) (% of their cumulative allocation)		-47.93	71.2 11.6	-54.47	68.7 13.4	-81.75	72.1 29.0

The table shows that the number of countries gaining and losing resources due to the redistribution is similar across all three scenarios, as are the average impacts on the 10 smallest and 10 largest allocations. The AIDI^{-0.25} scenario reallocates more resources than the AIDI^{-0.125} scenario but less than the AIDI^{-0.5} scenario. Its concentration effect in terms of percentage of redistributed resources is acceptable, with the single largest gain equivalent to 11 percent of the redistributed resources and the 5 largest gains representing 33 percent of these resources, as compared to 20 percent and 49 percent, respectively, under the AIDI^{-0.5} scenario. In terms of redistributed resources the cumulative five largest decreases are least concentrated in the AIDI^{-0.25} scenario, and while the UA 54.5 million decrease represents 68.7 percent of the redistributed resources, it only represents 13.4 percent of the 5 countries' cumulative allocation of more than UA 407 million.

²⁹ The baseline scenario is the 2012 PBA allocations.

³⁰ The sums of all increases and decreases are not equal due to the effect of the Modified Volume Approach (discount on grant allocations) in the allocation process.

Annex VIII: Simulations of proposed adjustments to the PBA system

In this annex, all simulations are based on the 2012 PBA allocations.

Table VIII-1 presents the average impact of the proposed adjustments on the PBA country allocations in terms of average increase/decrease per year, for the 10 and 5 smallest/ largest allocations and for fragile states/non fragile states. In general, more resources are redistributed under the UA 15 million minimum allocation scenario and using an AIDI exponent of -0.5. Therefore, the average increase and the average decrease are larger under the UA 15 million scenario than under the UA 12 million scenario. The same is observed as regards the average impact on the 5/10 smallest and largest allocations. Fragile states receive more resources under the UA 15 million scenario regardless of the exponent on the AIDI.

Table VIII-1: Impact of increasing the minimum allocation, adding new cluster E to the CPIA questionnaire and including the AIDI in the PBA formula

Minimum Allocation	Exponent AIDI	Total Redistributed Resources (UA/year)*	Average Increase (per year)		Average Decrease (per year)		Average Impact on 10 smallest allocations (per year)		Average Impact on 10 largest allocations (per year)		Average impact on 5 smallest allocations (per year)		Average impact on 5 largest allocations (per year)		Average impact on the 17 fragile states		Average impact on the 24 non fragile states	
			UA MM	%	UA MM	%	UA MM	%	UA MM	%	UA MM	%	UA MM	%	UA MM	%	UA MM	%
UA 12 Million	-0.125	47.71	1.91	51.2	-3.17	-4.9	2.66	112.4	-3.94	-4.7	3.35	177.6	-6.60	-6.6	1.73	49.4	-1.9	21.2
	-0.25	61.60	2.46	52.8	-4.04	-6.9	2.67	112.2	-4.25	-5.1	3.30	175.9	-7.75	-8.0	2.06	50.7	-2.2	20.4
	-0.5	102.80	3.81	52.8	-7.56	-13.8	2.68	112.1	-5.04	-6.2	2.76	53.4	-2.9	19.1	2.76	53.4	-2.9	19.1
UA 15 Million	-0.125	63.16	2.53	72.9	-4.21	-6.3	3.83	162.1	-5.44	-6.5	4.87	257.5	-8.85	-8.7	2.30	69.8	-2.6	31.5
	-0.25	75.05	3.00	74.5	-4.95	-7.9	3.85	162.2	-5.75	-7.0	4.85	256.8	-9.97	-10.1	2.62	71.1	-2.9	30.9
	-0.5	109.21	4.04	72.7	-8.10	-14.3	3.87	162.6	-6.52	-8.0	4.82	255.7	-12.4	-13.2	3.29	73.7	-3.5	29.9

* Sum of additional resources going to increased allocations.

Table VIII-2 shows the number of countries receiving a higher or a lower allocation as a result of the proposed adjustments. There are few changes in terms of the number of countries gaining or losing resources across the various scenarios. For example, 16 out of 17 fragile states receive additional resources under all the six scenarios. 5 out of 6 countries in the Central region benefit from the proposed adjustments, as does the single country in the North region. In the other three regions, the effect is more balanced, with 7-8 countries gaining and 4-5 countries losing in the East region, 3-4 countries gaining and the same number losing in the South region, and 8-9 countries gaining and 6-7 losing in the West region. In all scenarios, the number of countries with a higher allocation (25-27) as a result of the adjustments exceeds the number of countries with a lower allocation (14-16).

Table VIII-2: Number of countries with higher and lower allocations - fragile states (FS) vs. non-fragile states (NFS) and per region

Minimum Allocation	Exponent AIDI	# Higher Allocation			# Lower Allocation			# Higher Allocation						# Lower Allocation					
		FS	NFS	Total	FS	NFS	Tot	Central	East	North	South	West	Total	Central	East	North	South	West	Total
UA 12 Million	-0.125	17	8	25	0	16	16	5	7	1	3	9	25	1	5	0	4	6	16
	-0.25	16	9	25	1	15	16	5	7	1	3	9	25	1	5	0	4	6	16
	-0.5	16	11	27	1	13	14	5	8	1	4	9	27	1	4	0	3	6	14
UA 15 Million	-0.125	16	9	25	1	15	16	4	7	1	4	9	25	2	5	0	3	6	16
	-0.25	16	9	25	1	15	16	5	7	1	4	8	25	1	5	0	3	7	16
	-0.5	16	11	27	1	13	14	5	8	1	4	9	27	1	4	0	3	6	14

Table VIII-3 presents the distribution of resources per region under the various simulation scenarios (baseline = actual 2012 PBA allocations). For example, the South region, which received UA 144.68 million or 11.6 percent of PBA resources in 2012: assuming a minimum allocation of UA 15 million, it would receive nearly the same amount under the AIDI -0.125 scenario (UA 144.94 million, i.e. UA 0.26 million or 0.2 percent more); would receive UA 142.76 million or 11.4 percent of PBA resources under the AIDI -0.25 scenario (UA 1.92 million or 1.3 percent less than under the baseline scenario); and would receive UA 138.04 million or 11.1 percent of PBA resources under the AIDI -0.5 scenario (UA 6.64 million or 4.6 percent less than under the baseline scenario). In general, an AIDI with a higher exponent benefits the Central region regardless of the minimum allocation scenario. As the North region encompasses only one country which receives the minimum allocation, the exponent of the AIDI has no effect for this region. The East region sees its allocation reduced the most as compared to the baseline scenario, between -2.6 percent and -5.3 percent. The South region also observes a lower allocation (up to -5.7 percent), except in the case of the UA 15 million with AIDI -0.125 scenario. The West region sees its allocation increase when the AIDI has an exponent of -0.125 or -0.25, but decrease slightly with an AIDI exponent of -0.5.

Table VIII-3: Distribution of resources per region after increasing the minimum allocation, adding new cluster E and incorporating the AIDI

Minimum Allocation	Region	# of ADF Countries	Baseline		AIDI -0.125 + Cluster E				AIDI -0.25 + Cluster E				AIDI -0.5 + Cluster E			
			UA Million	% of total	Simulation		Variation		Simulation		Variation		Simulation		Variation	
					UA Million	% of total	UA Million	%	UA Million	% of total	UA Million	%	UA Million	% of total	UA Million	%
UA 12 Million	Central	6	150.59	12.0	158.03	12.7	7.44	4.9	164.70	13.2	14.11	9.4	179.04	4.3	28.45	18.9
	East	12	543.75	43.5	529.71	42.4	-14.04	-2.6	526.58	42.2	-17.17	-3.2	518.66	41.3	-25.09	-5.3
	North	1	1.67	0.1	4.00	0.3	2.33	140.0	4.00	0.3	2.33	140.0	4.00	0.4	2.33	140.0
	South	7	144.68	11.6	143.65	11.5	-1.03	-0.7	141.39	11.3	-3.29	-2.3	136.48	11.1	-8.20	-5.7
	West	15	410.36	32.8	412.63	33.1	2.27	0.6	411.32	33.0	0.97	0.2	409.76	32.9	-0.60	-0.1
UA 15 Million	Central	6	150.59	12.0	158.43	12.7	7.84	5.2	164.82	13.2	14.23	9.4	178.55	14.3	27.96	18.6
	East	12	543.75	43.5	525.66	42.2	-18.09	-3.3	522.61	41.9	-21.14	-3.9	514.97	41.3	-28.78	-5.3
	North	1	1.67	0.1	5.00	0.4	3.33	200.0	5.00	0.4	3.33	200.0	5.00	0.4	3.33	200.0
	South	7	144.68	11.6	144.94	11.6	0.26	0.2	142.76	11.4	-1.92	-1.3	138.04	11.1	-6.64	-4.6
	West	15	410.36	32.8	412.82	33.1	2.47	0.6	411.65	33.0	1.29	0.3	410.23	32.9	-0.13	0.0

Table VIII-4 analyses the impact of the proposed adjustments on the distribution of PBA resources by performance quintile. Simulations show that the first and second quintiles (the 16 best performing countries) receive between 66.17 and 69.28 percent of the PBA resources in all scenarios while the bottom two quintiles receive between 17.95 and 20.51 percent. Regardless of the minimum allocation considered (UA 12 million or UA 15 million), PBA resources allocated to the fourth and fifth quintiles increase with a larger AIDI exponent.

Table VIII-4: PBA Resources per CPA Quintile (%)

Quintile	Minimum Allocation - UA 12 Million			Minimum Allocation - UA 15 Million		
	AIDI-0.125	AIDI-0.25	AIDI-0.5	AIDI-0.125	AIDI-0.25	AIDI-0.5
First	23.76	22.96	21.35	23.42	22.66	21.12
Second	45.52	45.62	45.80	44.79	44.88	45.05
Third	12.78	12.87	13.00	13.10	13.18	13.31
Fourth	8.23	8.53	9.19	8.57	8.86	9.49
Fifth	9.72	10.03	10.66	10.12	10.41	11.02

Table VIII-5 presents the distribution of PBA resources per AIDI quintile. The simulations confirm that the proposed adjustments entail more resources allocated to countries with a low level of infrastructure development (fourth and fifth quintiles).

Table VIII-5: PBA Resources per AIDI Quintile (%)

Quintile	Minimum Allocation - UA 12 Million			Minimum Allocation - UA 15 Million		
	AIDI-0.125	AIDI-0.25	AIDI-0.5	AIDI-0.125	AIDI-0.25	AIDI-0.5
First	7.83	7.45	6.72	8.22	7.86	7.17
Second	28.86	27.83	25.75	28.51	27.52	25.53
Third	18.13	17.80	17.05	18.06	17.75	17.02
Fourth	18.00	18.49	19.37	17.98	18.46	19.30
Fifth	27.19	28.43	31.11	27.22	28.41	30.98

Table VIII-6 presents the impact of the proposed adjustments on the distribution of resources per GNI per capita quintile. The simulations show a redistribution of PBA resources between quintiles similar to the one presented in Table VIII-4: the first and second quintiles (countries with higher GNI per capita) see their cumulative allocation reduced by approx. 3 percentage points, and the corresponding resources are transferred to the third, fourth and fifth quintiles (countries with lower GNI per capita). While modest, this redistribution of PBA resources from the higher GNI per capita countries to the poorer ones supports Management's recommendation to ensure meaningful engagement with recipient countries through the PBA allocation system.

Table VIII-6: PBA Resources per GNI per capita Quintile (%)

Quintile	Minimum Allocation - UA 12 Million			Minimum Allocation - UA 15 Million		
	AIDI-0.125	AIDI-0.25	AIDI-0.5	AIDI-0.125	AIDI-0.25	AIDI-0.5
First	18.0	17.5	16.5	18.0	17.6	16.6
Second	17.2	16.6	15.4	17.3	16.7	15.5
Third	23.5	23.9	24.6	23.2	23.6	24.3
Fourth	16.0	16.0	16.0	16.0	16.1	16.1
Fifth	25.3	26.0	27.5	25.4	26.1	27.6

Annex IX: The Performance-Based Allocation Framework for ADF-13

The allocation of available African Development Fund (ADF) resources to ADF-eligible regional member countries (RMCs) for projects, programs and technical assistance during ADF-13 will be a process with three main steps. First, resources will be allocated to eligible countries using the Performance-Based Allocation (PBA) formula. Second, country-specific financing terms (loan, grant, or loan/grant combination) will be determined using the Debt Sustainability Framework (DSF). Third, Multilateral Debt Relief Initiative (MDRI) debt relief to eligible RMCs will be netted out of those countries' allocations and donor replacement funds will be reallocated to all ADF-only RMCs.

First Step: Applying the PBA Formula

Available resources will be allocated using the PBA formula:

$$A_i = (CPA_i)^4 \times \left(\frac{GNI}{P}\right)_i^{-0.125} \times P_i^1 \times (AIDI_i)^{-0.25}$$

$$CPA_i = 0.20 CPIA_{(ABC)_i} + 0.58 CPIA_{D_i} + 0.06 CPIA_{E_i} + 0.16 PPA_i$$

Where: A_i	is the allocation for country i
$AIDI_i$	is the Africa Infrastructure Development Index score for country i
CPA_i	is the country performance assessment for country i
$CPIA_{(ABC)_i}$	is the rating for clusters A, B and C of the Country Policy and Institutional Assessment (CPIA) for country i
$CPIA_{D_i}$	is the rating of CPIA cluster D (Governance) for country i
$CPIA_{E_i}$	is the rating of the new CPIA Cluster E for country i
$(GNI/P)_i$	is the gross national income per capita for country i
PPA_i	is the Portfolio Performance Assessment for country i
P_i	is the population for country i

The PBA formula has two main determinants:

- country need as indicated by gross national income per capita (GNI/P), country population (P) and the AIDI;
- country performance as per the country performance assessment score (CPA).

An increase in GNI/P will decrease the per capita allocation, while an increase in the CPA due to the net positive impact of $CPIA_{ABC}$, $CPIA_D$, $CPIA_E$ and/or PPA will increase the per capita allocation. The population variable (P) converts per capita country allocations to total country allocations. Countries with relatively large populations will be allocated more resources in absolute terms. Countries with a poor level of infrastructure development as measured by the AIDI will see an increase in their PBA country allocation.

In addition, the following procedures will be applied:

- Single country allocations will not be permitted to exceed 10 percent of all resources available. The cap will be applied at the basic allocation stage, i.e., on the initial results of the PBA process. Any excess over capped amounts will be reallocated to the rest of the countries using the PBA formula.
- A minimum allocation of UA 15 million will be applied to all countries, with the exception of countries in transition to blend or AfDB-only status.

Second Step: Using the Debt Sustainability Framework and the Modified Volume Approach

The DSF is used to determine each country's risk of debt distress. It is based on two criteria: the institutional strength and quality of a country's policies to withstand debt distress, and country-specific debt burden indicators (namely, the net present value of debt/gross domestic product ratio, the net present value of debt/exports ratio, and the debt service/exports ratio). Countries are classified by three "traffic lights," where red indicates a high risk of debt distress, yellow indicates a moderate risk, and green indicates a low risk. Countries in the red category qualify for 100 percent grants, countries in the green category qualify for 100 percent loans, and countries in the yellow category qualify for a 50/50 loan/grant combination.

A modified volume approach will be applied to PBA allocations under ADF-13. The primary purpose of the approach is to cover administrative charges for grant allocations up front and to strengthen the incentive structure of the PBA system. The approach will apply a 20 percent volume discount to all grants. This discount will be sub-divided into a 15.0 percent charges-related portion and a 5.0 percent incentives-related portion. The incentives-related portion will then be reallocated to all ADF-only countries, using the PBA method, to help reinforce the PBA system's incentive structure. The PBA-related country allocations of fragile states eligible for grants will be subject to the charges-related discount of 15.0 percent. These countries will be excluded from the allocation of the incentives-related portion of the volume discount.

The modified volume approach including discount on grants will not apply to top-up allocations under Pillar I of the Fragile States Facility.

Third Step: Multilateral Debt Relief Initiative Netting Out and Topping-up to the Minimum Allocation

The foregone debt service payments of countries qualifying for debt relief under the MDRI are deducted from these countries' allocations through the MDRI netting-out mechanism. Resources provided by donors to compensate the ADF for the MDRI are reallocated to all ADF-only countries using the PBA system.

Any country whose allocation, due to the application of the DSF, MVA or MDRI netting out, has fallen below the minimum allocation of UA 15 million (UA 5 million per year) will see its allocation topped up to the minimum level. This provision shall not apply to countries in transition to blend or AfDB-only status.

Resource Allocation to Blend Countries

Each blend country will receive 50 percent of what it would receive if it were an ADF-only country, subject to the minimum allocation of UA 15 million for all ADF-eligible countries.