

**Chair's Summary of the Development Effectiveness Committee**

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26 March 2014

**Thematic Evaluation Study: ADB's Support for Inclusive Growth (IN.49-14)**

1. DEC discussed the evaluation study on ADB's support for inclusive growth circulated on 5 March 2014 by the Independent Evaluation department (IED). The DEC noted recent progress made in ADB with the adoption of indicators for inclusive economic growth in ADB's corporate results framework, the issuance of staff guidelines on inclusive economic growth in the CPS, and a revised project classification system. DEC agreed with the study's recommendation that there is a need to focus on both poverty and inequality to achieve inclusive growth.

2. A DEC member inquired how IED arrived at the conclusion that inequality increased because household consumption grew slower than the gross domestic product (GDP), considering that GDP is also a function of investment and government expenditure. IED responded that the study revealed that the average standard of living (and thus poverty, but not necessarily inequality) is impacted by slower growth in household consumption than in GDP. The DEC member stressed that indirect effects of pillar 1 interventions are equally important, and inquired about the classification system employed by IED in disaggregating effects on various pillars, given that ADB projects have overlapping effects on the different pillars. IED responded that the study had used the same system that was used by ADB to calculate the share of financing allocated to the pillars, but had done this for a longer period, from 2000 to 2012. On the 80-20 core to noncore allocation, the DEC member was of the view that given the limited resources, ADB's interventions should be based on country demand and maintain the 80-20 allocation at the corporate level.

**Definition of inclusive growth**

3. DEC discussed with IED and Management the issue of differing definitions of inclusive growth used by comparators and within ADB. Some DEC members expressed views on the suitability of the definition and whether the definition is conducive for driving ADB operations in a certain direction. A DEC member noted that the three pillar framework in Strategy 2020 seems to allow for projects that are solely growth related to be classified under pillar 1 and therefore included as contributing to inclusive growth. For example, a transmission line might contribute to high growth and so would be included under pillar 1 of inclusive growth without any element of inclusiveness. The DEC member inquired whether the new project classification system addresses the risk that everything can be considered inclusive. Management responded that inclusive growth was defined as combination of three pillars: pillar 1 - creating opportunities through growth, pillar 2 - improving access to opportunities, and pillar 3 - providing social protection. Through which of these pillars ADB contributes to inclusive growth will be decided through CPS, taking into account binding constraints in each country, what the government and other partners are doing, and where ADB can add value. Management considered that, there is nothing wrong if a project in pillar 1 contributes mostly to economic growth, as long as it forms part of the country's efforts for inclusive growth as analyzed in the CPS. Management also noted that ADB's results framework monitors distribution of operations to pillar 1, pillar 2 and pillar 3, rather than lumping them into a single inclusive growth operations category. The monitoring shows that while the share of pillar 1 is larger, the share of pillar 2 is also significant. Further, Management emphasized the issuance of staff guidelines to strengthen analysis of inclusive growth in the CPS.

**Country Partnership Strategy level vs. project level approach to inclusive growth**

4. DEC agreed with the study's point that ADB's support for inclusive growth must be tailored to the specific needs of individual DMCs. DEC members found the country case studies useful for bringing the discussion down to a practical level. It was noted that in some countries, a focus on growth has been sufficient to achieve significant reductions in poverty but in countries like the Philippines and Papua New Guinea, economic growth has not led to poverty reduction and in those countries ADB should be focusing on inclusive growth.

5. A DEC member was of the opinion that since ADB's mission is a region free of poverty, the total impact of its country operations should benefit poor population groups relatively more. The member agreed with Management that ADB's inclusive growth agenda should be anchored in strong CPS processes, which identify

constraints for inclusive growth and poverty reduction, identifying operational priorities where ADB can maximize its impact on poverty reduction. The DEC member was of the view that ADB needs both well designed indirect and direct interventions for poverty reduction, and the balance should arise from country constraints identified in the respective CPSs, as one size do not fit all. The DEC member noted however, that the organizational incentives in ADB to utilize targeted, more direct, interventions, in particular to deal with remaining challenges on extreme poverty are currently too weak.

6. DEC discussed the study's finding that CPS analysis usually focuses on pillar 1 of the inclusive growth framework but analysis on the other two pillars is often limited. It was noted that this finding contrasts with ADB's Development Effectiveness Review which asserts that 100% of ADB country diagnostics for inclusive growth in 2013 were rated satisfactory. A DEC member noted that ADB project documents categorized projects either as general interventions or as targeted interventions with focus on the poorer regions or marginalized groups, and that targeted interventions had fallen from a high of 50% in 2004 to less than 20% in 2012. The DEC member opined that although not all projects should be focused directly on marginal groups, that for an organization with a poverty mandate, at 20% and on a declining trend, the level of targeted projects appeared to be low.

7. DEC noted that the evaluation study points out that ADB as an organization mostly does projects and thus the focus on inclusive growth needs to be not only at the country level but also at the project level. Some DEC members however did not agree with the recommendation that ADB should design projects to disproportionately benefit lower-income groups. Nevertheless, a DEC member was of the view that the project design guidelines should prompt staff and consultants to look for opportunities to add an inclusive element to projects, for example through tariff policies, or complementary investments to improve access to services.

8. A DEC member was of the view that not all projects need to be categorized as inclusive but considered that the study has made a convincing argument that ADB has favored pillar 1 over the other two pillars, which seemed to be supported by the midterm review (MTR) of Strategy 2020 as it commits to increase investments in pillar 2 and pillar 3. The DEC member considered that ADB should look to do more in education and social protection in countries with high and increasing inequality, pockets of persistent poverty, or unequal access to education.

9. DEC noted Management's strong opposition to this particular IED recommendation and the debate about choosing a CPS or project based approach for inclusive growth. DEC was of the view that ADB needs both strong CPS's and well-designed projects that reduce poverty directly or indirectly and provide opportunities for low income groups. IED responded that the study calls for strengthening both CPS analysis and project design and implementation with attention to benefiting lower-income groups.

#### **Direct vs. indirect interventions and targeting low income groups**

10. DEC agreed with the main recommendations of the study and appreciated that Management had agreed with these, for instance the need for strengthened attention to inequality, improving CPS diagnostics and prioritization as well as country level tracking on progress on inclusive growth. DEC appreciated that many of these points were already incorporated into the Working Paper on the MTR of Strategy 2020. The DEC noted that the inclusive growth section in the W-paper has benefited also more broadly from a series of IED evaluations and reports discussed at the DEC such as on the Millennium Development Goals, Social Protection, Private Sector Operations and the MTR Commentary Report. A DEC member noted the importance of more inclusive infrastructure, increased resources for education, health, social protection and inclusive business, which have been highlighted by IED and which have helped the Board and Management to build consensus during the MTR process on many inclusive growth priorities moving forward. However, DEC noted that there still seems to be a fundamental difference between Management and IED on one major area of the inclusive growth debate, about the operational consequences of IED's statement that each inclusive growth pillar should pay special attention to benefiting lower-income groups relatively more.

11. DEC noted that this question is connected to the issue of the role of indirect and direct interventions in poverty reduction, which has been debated in DEC several times. DEC noted that IED has in many evaluations and reports highlighted the important role of operations in targeting poverty constraints in developing member countries (DMCs) more directly. DEC noted that IED is recommending a stronger translation of the strategic objectives into project design and implementation, but that Management responses have been of a diverging view on this topic, noting that while direct impacts are important, indirect effects, which may take longer time to show, should not be neglected. Management reiterated its strong belief that inclusive economic growth should be seen

and assessed in the wider context of ADB's strategy and operational program at the country level as reflected in the CPS, and not be pursued at the level of each individual project. DEC also noted IED's response that the study does not call for every project to focus on lower-income groups.

12. Some DEC members were of the view that IED's evaluations have provided evidence that ADB should strengthen its preparedness and incentives to utilize - when the country context so demands - well designed interventions that provide more direct poverty reduction benefits. Some DEC members considered that Management should therefore act upon IED's recommendation to include more interventions that directly target poverty reduction. A DEC member considered that it was important for the upcoming R-paper on the MTR of Strategy 2020 to emphasize the importance of stronger project impacts for low income groups, especially extremely poor but also other vulnerable groups, as well as actions and concrete guidance on how to achieve this. However, a DEC member emphasized that the indirect impact of projects to low income groups through accelerating economic growth was equally important.

### **Responding to challenges confronting middle income countries**

13. Inclusive growth in Indonesia and Viet Nam was discussed, and DEC was in agreement that poverty reduction is about the pace of overall economic growth as well as its distribution, and about the common challenge of the poorest population groups to benefit from growth to the same extent as others. As ADB's DMCs are already largely middle income countries (MICs) and more will become so in the medium term, the remaining poverty in these countries is likely to be more and more about issues of poor and lagging areas, particular vulnerabilities and inequalities in opportunities for the poorest. Some DEC members noted that in this context, IED's recommendation about increased focus on operational benefits to lower-income groups is important. A DEC member further noted that in poorer countries (non MICs), these challenges are even greater.

### **Request for informal board seminar**

14. DEC members proposed that an informal Board seminar (IBS) be held on this topic as it is of interest to the whole Board. However, a DEC member mentioned that given the disagreements expressed at the meeting, some clarifications should be considered before an IBS is conducted with the Board.