
APPENDIX AA: STATEMENT BY THE EXTERNAL ADVISORY PANEL

The Panel welcomes this rich and thought-provoking report and the opportunity to share some of its impressions. The subject—how to manage support by the donor community to LICUS—is of major importance, given the number of fragile states, the hardships endured by their inhabitants, and the spillovers to neighbors, as well as the fact that in certain instances such states may form a breeding ground for terrorism.

The Bank and other members of the international donor community have grappled for several years now with the question of how to help LICUS emerge from their frequently desperate situations. Given the defining characteristics of LICUS, weakness of governance, institutions, and policies, and the outcome of earlier research and experience that financial assistance against such a background tends to be ineffective, it was clear that useful engagement with these countries would require a new framework. The Bank is to be commended for having played and for continuing to play a leading role in developing such a framework.

The Panel was impressed by the methodology of the IEG report. It believes that the right questions have been asked and that the combination of analysis, common sense, and the underpinning of findings by wide-flung surveys has resulted in highly relevant lessons and recommendations. To no small extent this is also thanks to interaction with management that has clearly been fruitful.

While one may argue in general with a rush to evaluate before the necessary data are available, in this case an evaluation with a carefully restricted scope is very useful. The report is right to point out that the question of ultimate effectiveness of Bank interventions cannot yet be addressed.

However, in our language, effectiveness in the more limited sense of whether the Bank has been doing what it says it wishes to do and whether this can be done better is worth examining now, as is the question of the relevance of the formal determinants of LICUS and of their performance. Addressing these questions rigorously is essential to assess later, when adequate data are available, whether the approach chosen delivers acceptable outcomes in the use of scarce development resources.

The Bank has made commendable progress in its engagement with LICUS and in the performance of closed projects (see chapter 2 and appendix Q). However, the donor community has shifted the goal posts for intervention with the relatively recent, intensified, and explicit focus on state building and, where relevant, conflict prevention. This shift is logical in the context of the problems posed by LICUS. The Panel agrees with IEG, however, that the Bank needs to undertake major efforts to fit in with the new focus.

While the narrowing of the focus to state and peace building should induce the Bank to move away from overly broad reform agendas, which “do not augur well for effectiveness,” the Bank’s effectiveness in the area of governance and capacity building needs to be improved. IEG is right to recommend that the Bank spell out concrete strategies and policies for this purpose. That, at the country level, strategies need to be underpinned by internalized socio/political analysis may appear self-evident, but in practice proves to be difficult. Without such analysis, Bank engagement as well as that of other donors runs the risk of being ineffective and wasteful of resources. Without wishing to attribute responsibility, the recent experience in Timor-Leste appears to illustrate the point.

IEG also rightly stresses that capacity building must be a major part of state-building programs and that the Bank's track record indicates a need to strengthen the design and delivery thereof. The lesson that country ownership and absorptive-capacity constraints apply as much to knowledge products as to financial products does not make the challenge any easier. The Panel is convinced that unless weaknesses in state and capacity building are overcome, future outcomes will be disappointing, distorting judgments on the usefulness of multilateral and bilateral donor support to LICUS.

The joint responsibility of donors in the areas of state building and conflict prevention and across the range of issues involved in supporting LICUS once again leads to an obvious lesson: the need for donors to coordinate to provide more effective support jointly and severally. And once again the simple lesson is difficult to translate into systematic practice at the country level. Yet, as IEG's report brings out, the failure to do so can mean the difference between a whole that is larger or smaller than the sum of the parts, between effective and ineffective support.

The Panel agrees with IEG on the importance of further work on criteria by which to identify LICUS and on the need for a break-down by business models. Similarly, performance indicators require elaboration in order to determine the kinds and amounts of support to be given. Post-conflict LICUS are already treated very differently from the others, and have proven to be fertile recipients of certain kinds of financial aid. Careful specification could also strengthen decision making vis-à-vis resource-rich countries. Moreover, without such

criteria and indicators, monitoring and evaluation will not have at its disposal the toeholds needed for learning adequately from experience and for timely adjustment of country strategies.

The Panel agrees with the lessons drawn on how to improve the Bank's internal organization to meet the challenges posed by LICUS more effectively. Criteria for successful performance of staff in LICUS, where the traditional criteria only partly apply, need to be elaborated. Also, IEG's point is well taken that the selection of people for work on LICUS must take account of their willingness and ability to communicate and collaborate effectively inside the Bank and with other donors and the recipients.

The Panel has high regard for how the Bank has immersed itself in the challenging and risky area of support for LICUS. It welcomes the positive interaction between practice and evaluation, as evinced in the present report. In the Panel's view, IEG's comments are balanced and its recommendations sensible. Implementing them will not be easy, but is necessary to improve the effectiveness of Bank support to LICUS, as well as that of other donors. We would be surprised if further progress based on inescapable realities does not materialize. Such progress is all the more necessary because the tipping point between success and failure with equal effort lies much closer to failure in LICUS than in other countries. Adoption of the eminently practical lessons and recommendations of IEG can shift the tipping point onto more favorable terrain. The possibility of emergence from extreme fragility of the state and the associated misery of its inhabitants will be greatly enhanced.

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APPENDIX BB: MANAGEMENT RESPONSE

Introduction

Management welcomes IEG's review of the effectiveness of Bank support to Low-Income Countries Under Stress (LICUS) and is grateful for the review team's effort to incorporate many of management's comments in the review. As the review indicates, fragile states represent a critical challenge for the Bank and other development actors and make up an increasingly significant segment of the Bank's portfolio. The review provides useful analysis of a wide range of issues and contributes substance to the Bank's understanding of difficult engagements in fragile states. Management also notes that early conclusions of the IEG evaluation were useful in feeding in to the Good Practice Note on Country Assistance Strategies in fragile states (World Bank 2005e) and would like to thank the IEG team for its close cooperation in this regard.

As the review notes, the Bank has played a leading role in global policy development on fragile states. In pointing to several areas for future improvement, the review reinforces important messages for the Bank's engagement in fragile states that were set out in the LICUS Update (World Bank 2005h), which the Board endorsed on January 17, 2006. Management therefore agrees with IEG on many of the principles and ideas raised in the review, some of which have been the subject of *Fragile States: Good Practices for Country Assistance Strategies* and other guidance and good practice notes issued by OPCS. (By way of illustration, Attachment A provides a matrix showing key issues raised in the review and guidance on that issue that has been provided in one of the notes issued by the Fragile States Group [formerly the LICUS Unit] in OPCS.)

Key Issues of Agreement and Divergence

This Management Response first outlines the areas in which management agrees with the review and then discusses areas in which management believes that IEG has missed critical factors or could have given a fuller account of efforts the Bank is already making.

A. Areas of agreement

Management agrees with many of the review's findings, and the review serves as a powerful, targeted, and well-timed renewal of these arguments. Indeed, many of the areas are already part of an ongoing work program.

Improved institutional response. Management concurs with IEG's diagnosis of the various institutional bottlenecks where the Bank needs to redouble its efforts to restructure for a better performance. Increased field presence in fragile states, better incentives and skills development for staff, and improved surge capacity are all critical challenges that the review correctly highlights; these were areas of attention at the January 2006 Board discussions. Since then, the Fragile States Group has been addressing this set of issues in the review "Strengthening the Organizational Response to Fragile States," to be completed in fiscal 2007. The review examines issues of particular importance, including achieving the right level of field presence through incentives for staff, and the organization and capacity necessary to support the needs of country teams. Likewise, IEG has rightly identified some of the Bank's procedures as barriers to rapid responses. Right-fitting aid allocations to ensure positive, not perverse, incentives to countries is a complex and Bank-

wide challenge. And while management concurs with IEG that LICUS face the problem of too little or too much aid, it also would draw attention to the considerable progress made since the LICUS Initiative first raised these concerns (see Management Action Record).

Differentiated approach. Management welcomes IEG’s emphasis on the particular challenges that countries in “deterioration” or “prolonged crisis/political impasse” and post-conflict countries transitioning from the immediate post-conflict phase pose for the Bank and other donors. The Bank’s Fragile States Group is now working with partners in OECD-DAC’s Fragile States Group to take a more detailed look at differentiating approaches by business models, as the LICUS Update explains. Recent experience in such countries has highlighted the need to articulate common messages from the international community and focus both on national unity and accountability within the state-building agenda and on longer-term capacity building.

Learning space. Management also welcomes the review’s emphasis on lesson learning as a critical part of the Fragile States Group’s role. Regular LICUS learning seminars, often cohosted by SDV or PREM, provide a forum for informal exchange among practitioners and outside experts across a balanced agenda of themes and country cases. The Fragile States Group has also organized more targeted events with country teams to address in real time specific issues of interest—as recent examples, a review of political economy factors in Ethiopia and Sudan and a discussion of development policy operations in deteriorating governance situations. In addition, the Fragile States Group has regularly produced Good Practice Notes, most recently on harmonization and alignment.¹ Management concurs that there is increasing demand for operational guidance for field actors and innovative approaches that have a proven track record for capacity development; however, it notes that substantial operational guidance and learning activities have already been provided, and more are in the work plan articulated in the LICUS Update.

B. Areas of divergence

Overall, the review brings out less clearly the positive trends in performance data and some interesting and innovative approaches that the LICUS Initiative has encouraged and supported. Three areas of particular concern are the review’s presentation of performance data and country examples; its discussion of state building, governance, and capacity development; and its assessment of selectivity and prioritization, results measurement, and in-country donor collaboration.

1. Performance data and country examples

Management notes that the review tends to bring out a relatively negative side of the picture; for example, the summary makes use of 18 country examples, 17 of which are negative. While management welcomes identification of weak spots where they exist, it would note that many Bank country teams have also innovated and found successful modes of engagement that others can learn from. *Fragile States: Good Practices in Country Assistance Strategies* (World Bank 2005e) records 25 of these cases, ranging from the use of nontraditional partnerships to secure a robust economic intervention in Liberia to a results-focused strategy in Tajikistan (World Bank 2005e), but they are not reflected in IEG’s review.

Project performance data. While the country cases dominate, the summary discussion downplays data on project performance. When unbundled, the data provided in the review for project performance and at-risk projects reveal a positive year-on-year trend, both absolutely and vis-à-vis non-LICUS low-income countries.² In 2005 projects in LICUS actually achieved higher levels of performance than projects in non-LICUS low-income countries, a testament to the efforts of country teams working under difficult conditions. Management views this as a positive trend that should be supported and sustained as a real step to more effective engagement. However, the summary makes only cursory mention of it, despite the fact that the LICUS Update (World Bank 2005h) identified project performance as one of the key indicators of the Bank’s performance in LICUS (see section below on results measurement).

Data clarity. The review also gives the impression that it is basing judgments on some implementation evaluations that relate to operations begun before the initiative.³ Management recognizes that three years does not allow for much data to be gathered; however, the use of pre-initiative data and country examples could have been more clearly separated from newer data. Sidebar texts do little to clarify this confusion; for example, one reads that “IEG ratings for LICUS CASs completed thus far have mostly been unsatisfactory” (chapter 2) despite the fact, noted in the text, that of these only one was for a period fully postdating the initiative.

2. State building, governance, and capacity development

Management agrees that the state-building agenda addresses the critical areas of capacity and governance head on. However, the review repeats the formula that the Bank “has made a traditional area of weakness [governance and capacity development] a central part of its focus” and often couples this idea with the concept of overambition, which it further ties to the areas of selectivity and results measurement. In fragile states, governance and capacity are central to longer-term stabilization and development and require early and sustained engagement from the international community. Management agrees that in these countries the state-building agenda is an enormous challenge for governments and other stakeholders, as well as for the international community. The fact that these are hard goals to achieve does not mean the Bank should not make them central to the agenda. The very reason for adopting a state-building agenda that puts these issues front and center is that in the past the international community has been too ready to ignore the task of making state institutions more effective and accountable to their people, focusing instead on delivering quick fixes through parallel and unsustainable structures.

Importance of state building. In adopting this stance the Fragile States Group is in line both with international partners and with other parts of the Bank. The OECD-DAC Principles of Good International Engagement in Fragile States state

(principles 3 and 11) that state building should be a focus and that this in turn requires a long-term commitment to capacity development. Among other groups in the Bank, the PREM public sector governance team has undertaken critical analysis of the failings of past capacity development efforts that bolster, not undermine, the rationale for state building:

By the early 1990s the realization began to dawn that policies themselves were built on an underpinning of social, political, and state institutions and that weaknesses in this institutional foundation could undercut the economic policy reform agenda in three ways: by short-circuiting efforts at policy change, by failing to provide a robust platform of credibility and conflict resolution for market activity, and by being unable to provide complementary physical and social infrastructures (Levy and Kpundeh 2004).

Thus many experts see state building as a response to the failure of past development initiatives to see the bigger context in which the technocratic policy reforms advocated by the Bank and others would inevitably fail. The fragile states work has attempted to place these approaches within a broader political context to ensure greater impact, ownership, and sustainability; emphasize Bank staff’s knowledge of basic administrative systems; and balance invisible and visible results to maintain political momentum for reform.⁴

Capacity development and governance. The review is relatively dismissive of the Bank’s record on capacity development and governance—which have become areas of increasing focus under the LICUS Initiative. It is beyond the scope of this response to address this claim; however, it should be noted at least that the record is more nuanced. The Sector Strategy Implementation Update on Public Sector Governance concludes, among other things, that the overall quality of economic and sector work (89 percent) and country analytic and advisory activities (97 percent) for projects on public sector governance is significantly higher than Bank averages (84

percent and 91 percent, respectively), and that within the public sector governance portfolio, the success rate of public financial management operations was approximately 84 percent, regardless of the larger governance environment (World Bank 2005e, 2005k). While there are no easy solutions in the field of state building, management notes that there *is* a role for the Bank to identify catalytic entry points for reform where the Bank also has a comparative advantage.

3. Selectivity and prioritization, results measurement, and in-country donor collaboration

As the review notes, prioritization and sequencing, donor collaboration, and effective monitoring are all critical components of a successful reform agenda in a fragile state. The review marks the implementation experience in all three areas as low. Management would highlight three responses.

Donor coordination. Regarding donor coordination, the review tends to downplay the achievements of the Bank that management feels has been highly innovative in terms of instruments deployed, such as the transitional results matrix, the LICUS Trust Fund, and country examples of joint strategies. The LICUS Trust Fund mandates multidonor approaches; the Transitional Results Matrices used in the Liberian, Haitian, Timorese, and Central African Republic transitions all supported strong coordination at the country level among actors within a government-owned matrix. Joint country strategies have been completed in Cambodia, Togo, Somalia, and Nigeria and are under way for the Democratic Republic of Congo and the Central African Republic (a proportion that is at least as high as that for joint strategies in non-LICUS low-income countries). In addition, the Comprehensive Development Framework report notes that “improved coordination among external partners around the TRM is providing a basis for strengthening government leadership of development assistance coordination” (World Bank 2005c). (Attachment A highlights where the Bank has provided guidance on selectivity and prioritization issues.)

Selectivity and prioritization. Selectivity and prioritization are logical corollaries of an

emphasis on state building that encourages development actors to take a comprehensive perspective on the context while taking action along a “critical path” of feasible reforms. The review highlights one CAS that was not particularly selective—that of São Tomé and Príncipe, which covers a period straddling the initiative’s inception. Management would highlight that several country teams have more recently adopted innovative approaches with tighter prioritization and sequencing, both in the Bank’s work with national counterparts on overarching recovery strategies and in the Bank’s own CAS processes. The Central African Republic, Tajikistan, Cambodia, Liberia, Nigeria, Togo, and Zimbabwe are examples of interim strategy notes or CASs that have adopted a conscious LICUS approach with strong selectivity and prioritization.

Results measurement. Management concurs that results measurement must be a critical element of the LICUS approach. At a central level the Fragile States Group in OPCS has focused on CPIA and IEG data on project performance, both of which have improved consistently since the initiative began (the LICUS Update [World Bank 2005h] provides comprehensive reporting). At the country level, results measurement is as per Bank norms and depends critically on the availability of budget and staffing to support identification of results in national development plans and Bank assistance strategies. These are issues that the Fragile States Group is addressing both through its strategic advice to country teams on selectivity, reform sequencing, and results focus and through its strategic staffing report—which advocates for more dedicated staff posted in the field, where identification of key results for the national recovery strategy and the Bank’s strategy needs to occur. Management concurs with the view that the identification of indicators to monitor progress against peace building is at an early stage in the international community and is committed to working with other actors at the OECD-DAC and the United Nations Peace-Building Commission to further a common sense of progress measurement.

Management Action Record

IEG recommendation	Management response
<p><i>Clarify the scope and content of the Bank's state-building agenda and strengthen the design and delivery of capacity development and governance support in LICUS.</i></p> <p>Given its weak record on capacity development and governance, as well as its focus now on the more ambitious and complex state-building objective in LICUS, the Bank needs to clarify its areas of comparative advantage vis-à-vis other donors and adopt innovative approaches that ensure better capacity and governance outcomes. Innovative approaches need to be developed to achieve a better fit between the Bank's interventions and the capacity of a LICUS to perform core state functions; ensuring implementation of focused and well-sequenced interventions in LICUS environments, where virtually every aspect of capacity and governance may need significant improvement; and effectively monitoring capacity and governance outcomes.</p>	<p><i>Partly done, partly ongoing</i></p> <p>In January 2006 <i>Fragile States: Good Practice in Country Assistance Strategies</i> (World Bank 2005e) was discussed with and endorsed by Board. The paper gives more detailed and differentiated guidance on country strategy and operations than other agencies have given to date, clarifying both the Bank's comparative advantage within the sphere of state building ("core economic and development competences") and setting out innovative practices that can have a positive effect on capacity development.</p> <p>The Fragile States Group (formerly the LICUS Unit) is responsible for disseminating the good practice to support country team application of the lessons in the implementation of their programs in fragile states. This work is ongoing and integrated, as a priority, into the work program for fiscal 2007—see the LICUS Update also endorsed by Board in 2006 (p. 9).</p> <p>In addition, the Fragile States Group will roll out, during fiscal 2007, a program of learning activities based on examples of innovative approaches taken from the Good Practice Note.</p> <p>The Bank has organized two key state-building events. One in September 2005 convened a group of national reformers in New York from post-conflict situations for two days of facilitated discussions on state building. The second, in January 2006, convened a mixture of academics and policymakers to discuss state building with Bank staff in a one-day learning session. Both sessions provided a forum for intensive debate on core state functions, ways to match assistance with capacity, and how international organizations should engage.</p> <p>The September session has resulted in a joint work plan with the UNDP on state building that includes country-level work, policy research, and thematic workshops for lesson learning and discussion. Funding is in place and activities are under way, including research on peace agreements and state building, post-conflict planning processes and state building, as well as country work involving Sudan.</p>

IEG recommendation	Management response
	<p>This work, which supports considerable clarification of the definition, objectives, and division of labor of state building, will also feed into OECD-DAC's planned work around state building as part of the Fragile States Group work stream and will help the Bank play a role in shaping this agenda. The activities of OECD-DAC's work stream are to be defined in the first half of fiscal 2007 and activities to begin in the second half of fiscal 2007. By the end of calendar year 2008 the work is expected to have helped support the development of policy clarification on many of these issues.</p> <p>The forthcoming (first half of fiscal 2007) publication <i>Aid that Works: Successful Development in Fragile States</i> contributes some practical insights into project-level approaches for fragile states. It explores in particular the role of local-level governance institutions, the potential for complementarity between short-term results and long-term capacity development, and the importance of "bringing the state back in."</p> <p>Management agrees to support the conclusion of these activities according to their respective schedules. In management's view, these actions will provide a substantive response to the recommendations made.</p>
<p><i>Develop aid-allocation criteria for LICUS that ensure that these countries are not under- or over-aided.</i></p> <p>The Bank needs to conduct a technical review of the cumulative effect of the various adjustments to the performance-based allocation system on aid volumes to LICUS. Aid-allocation criteria that reflect the Bank's objectives in LICUS and ensure that these countries are not under- or over-aided need to be developed. Whether and to what extent the criteria should be based on factors other than policy performance (such as levels of other donor assistance, assessment of potential risks and rewards, and regional and global spillovers) needs to be examined, keeping in mind that aid is limited and trade-offs will have to be made.</p>	<p><i>Ongoing/Not agreed</i></p> <p>Management believes that the current IDA allocation system reflects fairly on the one hand the consensus in the larger development community that a performance-based system is needed to steer scarce resources where they are most likely to alleviate poverty most effectively, and on the other hand the IDA donors' specific views on how much allocations should be increased in stronger-performing countries. Accordingly, the weaker performers—broadly constituting the LICUS group—receive smaller allocations per capita. Within this broad framework there is already a recognition of some of the points raised by IEG, as evidenced by special allocations for (a) countries coming out of severe conflict, (b) qualifying regional projects, and (c) in exceptional cases countries reengaging with IDA.</p> <p>IDA donors no doubt will continue to raise points about the performance-based allocation system. One point relates to the role of governance. A technical note on this area is being prepared for discussion during the IDA14 Mid-Term Review in</p>

IEG recommendation	Management response
	<p>November. In the meantime, management continues to see broad support for the current approach described above and does not think that reopening basic allocation questions would be helpful in preserving the broad policy consensus that should underpin a strong IDA15 replenishment.</p>
<p><i>Strengthen internal Bank support for LICUS work over the next three years.</i></p> <p>Two aspects of internal Bank support need attention. First, staffing numbers, skills, and incentives for working on LICUS need to be prioritized. Ensuring adequate incentives to attract qualified staff—both at headquarters and in field offices—to work on LICUS will require giving clear signals of what is deemed to be success in LICUS, what outcomes staff will be held accountable for, how much risk it is reasonable to take, how failure will be judged, and how overall performance evaluation ratings and staff career development will take these into account. As in Olympic diving, where the scoring system factors in both the technical perfection as well as the difficulty of the dive, staff performance in LICUS should be similarly judged by assigning due weight to the extent of challenges presented by varying LICUS environments. Signaling the importance of LICUS work throughout the management hierarchy will also be required.</p> <p>Apart from incentives, the Bank needs to ensure that staff working on LICUS have relevant skills, such as in public sector management, are capable of seeking and using political knowledge, and are willing and able to work in interdisciplinary teams. Current plans to address these issues in the forthcoming Strengthening the Organizational Response to Fragile States are welcome, even if late. More systematic thinking is needed on staffing decisions for LICUS within the context of the Bank's overall staffing, recognizing that assigning more and better-qualified staff to work on LICUS would likely mean trade-offs for other Bank country teams. Trade-offs to benefit LICUS may or may not be justified depending on the Bank's objectives for LICUS as well as other Bank clients' need for assistance.</p> <p>Second, the organizational structure for LICUS and conflict work needs to be streamlined. The Bank needs to ensure an efficient organizational arrangement that removes duplication and fragmentation of support between the LICUS Unit and the Conflict Prevention and Reconstruction Unit.</p>	<p><i>Ongoing/Agreed in part</i></p> <p>This is being addressed through the review <i>Strengthening the Organizational Response to Fragile States</i>, now in final draft and to be completed in fiscal 2007. The review examines issues of particular importance, including achieving the right level of field presence through incentives for staff and the organization and capacity necessary to support the needs of country teams. Discussions are under way with all the Regions on how to strengthen the field presence in fragile states. The Fragile States Group will update management and the Board with recommendations and their attendant cost estimates in fiscal 2007. Following discussion of this paper, OPCS will also take steps to strengthen the Bank's surge capacity, staff guidance, and training in fragile states, in line with the IEG recommendations.</p> <p>Work is now under way to develop a comprehensive program of critical skills training based on the assessed need for staff in field offices. This training program—which management considers to be the response to this recommendation—is to be rolled out in fiscal 2007 and will include modules for basic public administration reforms, including the budget function, as well as gaming scenarios to test Bank staff response skills in complex or rapid transitions.</p> <p>Discussion of the overlap of roles and responsibilities between the Fragile States Group and CPR in SDV hides the useful collaboration that is taking place between the two teams. Notably, these include joint management of the LICUS Trust Fund grants, collaboration on post-conflict needs assessment work, and peer-review functions. Management needs to ensure that all its priorities on fragile states are covered and cannot commit to a change in structure.</p>

IEG recommendation	Management response
<p><i>Reassess the value added of the LICUS approach after three years.</i></p> <p>The value of the LICUS category and approach, including the operational usefulness of the business models, needs to be independently evaluated after three years, when sufficient experience on the outcomes of the approach will be available. At that time, it should be possible to address the more fundamental question of whether and to what extent Bank assistance can effectively support sustainable state building. Continued Bank support for the LICUS category and approach should be based on the findings of that reassessment.</p>	<p><i>Agreed</i></p>

Attachment A. Review Recommendations Already Covered in Bank Guidance

IEG review	Reference to policy notes
<p>Executive Summary</p> <p>The review focuses on selectivity and prioritization of reform efforts in fragile states. For example:</p> <p>p. xxx: The review notes the importance of selectivity and prioritization of reform agendas and within the Bank's CASs, stating: "[E]ven if collective donor selectivity is not immediately achieved, the Bank itself needs to ensure focus and selectivity in its own assistance program...."</p> <p>and</p> <p>p. xxviii: The review emphasizes the need for donors, including the Bank, to understand that "in the absence of a clear and relevant reform agenda, early successes of engagement may be short lived and contribute little to the achievement of country strategy objectives."</p> <p>p. xviii: The review states that "In the deterioration and prolonged crisis or impasse business models, given that there is often little consensus between donors and government on development strategy, engagement needs to include policy dialogue aimed at creating an opening for reform, and simultaneously work on a reform agenda should a window of opportunity arise."</p> <p>p. xxx: The review notes that "since capacity to use aid effectively in post-conflict LICUS is low and governance is often poor, the focus from day one also needs to be on the development of capacity and improvement of governance, not just physical infrastructure."</p>	<p>Selectivity and practicality of approach is also a pillar of the Bank's core guidance on fragile states. For example, the Good Practice Note on Transitional Results Matrices (TRM GPN) notes five "core principles for developing TRMs"—the first two of which are "Simple" and "Selective," noting both the strong forces against selectivity in fragile states and the risks faced by an overambitious reform strategy.</p> <p>The TRM GPN also states that "the desirable end result [of developing a TRM] is a matrix that focuses on a few key reform goals that will generate visible results and strengthen a platform for further reform and reconstruction."</p> <p>In addition, the Good Practice Note <i>Fragile States: Good Practice in Country Assistance Strategies</i> (CAS GPN) clearly sets out criteria for prioritization of reforms: "Building on the zero generation reform approach laid out by the LICUS task force, parameters used to determine priorities in different fragile states have included: (i) actions necessary to lock in promising reforms or lay the basis for future improvements in state delivery; (ii) actions necessary to prevent potential instability; (iii) actions necessary to build popular momentum for reform by generating visible results."</p> <p>In addition, the CAS GPN notes, "Efforts to build state capacity and accountability in all fragile states will tend to put particular emphasis on the <i>prioritization</i> needed to continue improvement in state performance or prevent failure of key functions" (p. 3, para 11).</p> <p>The CAS GPN notes "restarting dialogue" as one of the priorities for prolonged crisis countries, stating that "in some situations of prolonged conflict or political impasse, relatively noncontroversial development issues may provide an entry point for constructive dialogue between the parties to a conflict." In deteriorating governance countries, the CAS GPN notes that the Bank can provide "input on specific economic issues which are important for mediation efforts and may serve as a way to restart dialogue."</p> <p>The CAS GPN notes the importance of early capacity-building efforts: "In close collaboration with the International Monetary Fund, the Bank plays a key role in rebuilding capacity on economic policy, public financial management systems, and civil service reform or strengthening. It is therefore critical that the Bank is involved in the immediate post-conflict period (and indeed prior to this), when many critical decisions on the size, scope, and parameters of public administration will be taken. Assistance in this area may include policy dialogue, analytical work, capacity building and support to recurrent expenditures: since state institutions are often new or extremely weak, much stronger knowledge of basic public financial and administrative systems is needed than</p>

IEG review	Reference to policy notes
	<p>in the Bank’s regular IDA clients. The Bank is also engaging more closely with leadership capacity building in the early stages of post-conflict transitions, in recognition that leadership that is new to peace-time government may require exceptional support to make this transition successfully.”</p> <p>The TRM GPN states: “As important as the early and visible delivery of tangible benefits can be, there are other much less visible actions that must be initiated early on, even though their benefits will not be felt for some time. Strategic and planning efforts must not be delayed; sector visioning, strategy development and policy formulation, definition of institutional capacity needs and planning for the associated capacity development” (p. 7).</p>
<p>Chapter 2</p> <p>p. 21: The review states: “Critical to the Bank’s effectiveness is its ability to reflect sound political analysis in its strategy adequately. This has been an area of weakness in the Bank.”</p> <p>p. 26: The review claims: (a) “Building stronger state institutions and governance are not merely technocratic processes involving the state, but...”</p> <p>(b) “...requires social transformations including those of civil society and the relationship between the state and civil society. Bank approaches need to be adequately informed by such considerations.”</p>	<p>The CAS GPN emphasizes the importance of political understanding: “The Bank should continue to encourage country teams to incorporate analysis of the political economy... in both CAS/ISN processes and upstream project preparation” (p. 8).</p> <p>The CAS GPN states, “It is therefore important that institution-building initiatives avoid purely technocratic approaches, devoting considerable attention to the process of decision making and implementation, and to well-designed participation and widespread communication of reform initiatives” (p. 5).</p> <p>The CAS GPN also highlights the importance of demand-side reform: “A vibrant civil society and private sector are critical for effective governance: indeed, without a strong private sector to generate jobs, incomes and tax revenues, or without popular and civil society demand for accountable services, public sector reforms are unlikely to be sustained. Assistance for ‘state-building’ therefore includes support for private sector and civil society development, in all fragile state contexts” (pp. 5–6).</p>
<p>Chapter 4</p> <p>p. 61: The review claims: “Other areas where the Bank needs to further develop its operational approach include ...address linkages between politics, security, and development...”</p>	<p>The CAS GPN lays out for the first time a coherent framework for addressing the political, security, and development nexus from the Bank’s perspective:</p> <p>“Moving forward, there is justification to extend successful country experiences in linking development and peace building to a deeper and more systematic consideration of these linkages in the Bank’s operational engagement. Recognizing the need for peace-building to be nationally driven and the constraints posed by the Bank’s mandate and expertise, an emphasis on responsiveness to requests from national counterparts for support; maintaining a focus on the Bank’s core economic and development competences; and partnerships with other institutions should be the underlying principles of assistance in this area. In particular, experience from country programs indicates that:</p> <ul style="list-style-type: none"> • Political economy and conflict analysis are important to inform the selection and sequencing of priorities for country assistance strategies, as well as project design issues. The Bank should continue to encourage country teams to incorporate analysis

IEG review	Reference to policy notes
	<p>of the political economy and conflict dynamics in both CAS/ISN processes and upstream project preparation.</p> <ul style="list-style-type: none"> • The Bank plays an important role in supporting various cross-cutting development processes where peace building may emerge as a priority such as post-conflict needs assessments, recovery plans and results frameworks, PRSPs, public expenditure and governance assessments, multidonor budget support operations, multi-sector/multidonor trust funds and donor-coordination processes. These processes are by their nature integrative: precluding peace and security issues and institutions from consideration, or placing them on a separate track, creates the real risk of diminishing their importance, missing opportunities for synergy, or ignoring factors which may undermine longer-term development outcomes. The Bank's role in engaging with political and security sector institutions should focus on its core economic and development competences (such as generic development planning or public finance capacity building), developing as appropriate partnerships with other donors or institutions that have expertise in specialized technical reform or capacity building in the peace and security areas. • While retaining an emphasis on the Bank's core economic and development activities, there is scope to increase emphasis on peace-building goals. Peace building is a valid goal to use in country assistance strategies, where sustaining a fragile peace, preventing escalation of conflict or addressing crime and violence which constrain the welfare and development opportunities of the poor have emerged as national priorities. Activities which contribute to peace-building goals are not only those which directly touch on the security sector, such as demobilization and reintegration of ex-combatants. All economic and development activities infrastructure, human and social sector development, economic management, private sector and agricultural recovery, etc. can potentially be selected or designed to contribute to peace-building goals. <p>Bank assistance strategies and programs can also include the development of partnerships with other donors and national counterparts which combine respective technical capacities to support peace-building priorities. For example, the Bank may work with the UN (or other institutions taking the lead on political governance and peace building, including civil society organizations) to provide economic inputs or training to the parties to peace and national reconciliation talks; constitutional reform processes; or economic and development training to political parties and parliamentarians, provided that in all cases this dialogue is nonpartisan and part of a multidonor effort.</p> <p>This approach allows the Bank to make a more systematic contribution to the evolving international partnership for peace-building. It acknowledges that the Bank is still learning about the linkages between peace-building and development; signals a respect for the mandate and expertise of other international institutions; and recognizes that close partnerships are needed" (pp. 7–9).</p>

APPENDIX CC: CHAIRMAN'S SUMMARY: COMMITTEE ON DEVELOPMENT EFFECTIVENESS (CODE)

On July 26, 2006 the Committee on Development Effectiveness (CODE) considered the report *World Bank Support to Low-Income Countries Under Stress: An IEG Review* and the draft Management Response. The statement by the External Advisory Panel on the IEG review was circulated as background document.

Background. The Bank outlined its approach to Low-Income Countries Under Stress (LICUS) in 2002. In January 2006 the Board considered the LICUS Update, together with the staff guidance note *Fragile States: Good Practices in Country Assistance Strategies*. The LICUS Update called for: (i) increased attention to peace- and state-building goals in fragile state assistance strategies; (ii) stronger partnership with other organizations; and (iii) stronger Bank organizational response. In January 2006, the Board also supported the replenishment of the LICUS Trust Fund created in 2004. The LICUS Trust Fund is the only fund that can provide significant assistance to recovering countries in non-accrual status with the Bank, although there are other trust funds to support LICUS, including the Post-Conflict Fund. In the past year, the Board discussed several LICUS country assistance strategies, including for Afghanistan, Kosovo, Tajikistan, Timor-Leste, and Sudan (update), and a group of Executive Directors visited the Central African Republic.

Main Findings and Recommendations of the IEG Review. IEG found that the LICUS Initiative has increased Bank attention to these countries, but implementation experience to date has been mixed, although it is too early to assess full outcomes. It noted that significant challenges remained, including the need to: (i) increase

selectivity and prioritization required in donor and Bank reform agendas; (ii) improve Bank effectiveness in fragile states in deterioration and prolonged crisis or impasse; (iii) improve the Bank's donor coordination at the country level to match its strong coordination at the international policy level; (iv) clarify the Bank's central goals in fragile states, state and peace building; (v) finalize and implement critical human resource reforms (for example, staffing, incentives); and (vi) take stock of the various adjustments made over the years to the Performance-Based Allocation System (PBA), whose cumulative effect on financing for fragile states is not clear. The four IEG recommendations were: (i) clarify the scope and content of the Bank's state-building agenda and strengthen the design and delivery of capacity development and governance support; (ii) develop aid-allocation criteria for LICUS that ensures that countries are not under- or over-aided; (iii) strengthen internal Bank support for LICUS work over the next three years; and (iv) reassess the value added of the LICUS approach after three years.

Draft Management Response. Management welcomed the IEG review, noting that many points reinforced the key messages in the LICUS Update, and echoed the issues considered in *Fragile States: Good Practices for Country Assistance Strategies*. It noted that the preliminary conclusions of the IEG evaluation had been particularly useful in helping staff refine the fragile state business models presented to Board in January. However, management found that the IEG review could have been more balanced in reflecting positive trends in the performance data and country examples; discussing state building,

governance, and capacity building; and assessing selectivity and prioritization, results measurement, and in-country donor collaboration. Country team speakers presented a range of examples of application of fragile state approaches and international partnerships in country strategy and operations, as well as underscoring the importance of senior management attention and staffing issues. Management emphasized the newness of the LICUS Initiative whereby the Bank is learning by doing and the need to level the expectation given the difficulties faced in fragile states and the high-risk–high-reward nature of work. It elaborated on Bank efforts to address much of the IEG findings, providing country examples. Management partially agreed to IEG recommendation (iii) and noted its ongoing work on strengthening the organizational response to fragile states. Management disagreed with IEG recommendation (ii), and believed the current IDA allocation system fairly reflects the consensus in the larger development community and the IDA donors on the need for a PBA system to ensure aid effectiveness.

Overall Conclusions. The Committee welcomed the opportunity to discuss the IEG review and the draft Management Response. While it may be too early to draw definitive conclusions about outcomes, given the complexity of issues faced in fragile states, speakers considered it imperative to learn from experience on a frequent ongoing basis. The IEG review was commended for being informative and incisive, raising critical issues, and promoting substantive and constructive dialogue acknowledged by both IEG and management. CODE also appreciated the presentation of country experiences by operational staff.

The Committee strongly supported continued Bank engagement in fragile states, and several speakers expressed appreciation for the dedicated staff working in difficult environments. While encouraged by the preliminary findings and early successes of the Bank's engagement, members agreed with IEG that there is little room for complacency. Emphasizing the importance of "raising the game" in implement-

ing the LICUS Initiative, speakers' comments focused on the following: role and comparative advantage of the Bank especially in peace and state building; possible refinements of the existing business models and use of instruments; need to strengthen the knowledge base; aid-allocation mechanism and possible need for its adjustment; measurement of results; and donor coordination. There was consensus regarding the importance of strengthening internal support for LICUS (for example, staffing, incentives, and organizational structures).

Next Steps. The IEG review (including the Management Response and CODE Chairman's Summary) will be disclosed in September 2006, in absence of a request for a full Board discussion. There was agreement to reassess the value added of the LICUS approach after three years, as recommended by IEG.

The main issues raised during the meeting were the following:

General Comments. Several speakers noted that it was too early to assess the outcome and cautioned against drawing hasty conclusions; they viewed the report as more about learning than an assessment. Others were disappointed about poor funding for and slow and regionally variable implementation of the Board-endorsed LICUS guidelines, although a number of speakers also highlighted the risk and uncertainty of fragile states, the challenge of producing results, and the narrow difference between success and failure in difficult country environments. *Staff commented on the tradeoffs between speed, good governance, and capacity development in providing support to fragile states and on the need to better address them.* A member asked about the prioritization and sequencing of the IEG recommendations, while another speaker requested IEG to review the messages included in the summary of the report, to make sure that they match the analysis. *IEG considered clarifying and monitoring of the state-building agenda as most important, followed by making the resource allocation more systematic, and addressing internal*

organizational issues. A speaker expressed appreciation for the Norwegian Aid Agency's cooperation and support to the preparation of the IEG review.

The Bank's Role. Speakers strongly endorsed the Bank's continued engagement in LICUS and the focus on state building. They had questions about the comparative advantage of the Bank, the scope and content of the Bank's state- and peace-building agenda, conflict prevention, promotion of macroeconomic stability, and capacity development and governance support. In this connection, one speaker observed that the fundamental issue is the alignment between the security and development agenda. Some other speaker noted that these countries face periodic setbacks, such as Timor-Leste, which was referred to in the IEG review and the Statement by the External Advisory Panel. This speaker viewed that while lessons should be learned from such crises, setbacks should be considered a normal part of engagement in fragile situations, and not necessarily an indication of failure of donor assistance, including of the Bank. Where countries are able to rapidly recover within their constitutional structures and without descending into state failure, this institutional resilience demonstrates a positive result of international investment in institution building. Some members cautioned against overly optimistic expectations, especially the fiduciary aspects and absorptive capacity. Other speakers stressed selectivity and prioritization, addressing gender issues and continuous efforts in monitoring, evaluation, and measuring results.

Management considered state capacity and accountability as core issues faced by fragile states. It referred back to the LICUS Update of January 2006, where it clarified the basis of the Bank's engagement in state and peace building (based on country ownership, the Bank's core economic and development competencies, and partnerships with other donors to address peace, security, and development linkages in an integrated manner). Management also stressed that there have been more Bank

successes in this area, particularly in-country donor partnerships and capacity development in public finance systems, than implied in the IEG review, and provided examples.

Instruments of Support. A number of speakers suggested refining the existing business model, tailoring the approach to varied country situations within the LICUS group, and effective use of various Bank Group instruments, especially the analytical and advisory activities. Some members also emphasized the importance of the knowledge base of LICUS, particularly the analysis of political economy, drawing on existing information, involving local stakeholders to build country ownership, and outsourcing as necessarily. The need to strengthen the quality and relevance of analytic work and of sharing of experiences was emphasized. *Management emphasized that the Bank is adjusting its support and use of instruments to match the changing country context. It also assured the Committee of its efforts to work with countries and donors in delivering economic sector work and technical assistance, building on available information—a point that had also been emphasized in the LICUS Update. Management responded in affirmative to a member's question about whether the new Operational Policy on Emergency Lending will address the procurement and financial management issues faced in fragile states; the OP will be accompanied by appropriate guidelines.*

Classification of Countries. Some members sought more transparency in classifying countries as LICUS or fragile states. A few of them proposed introducing a criterion to define "fragility" of a country, while one sought more involvement of partner government in the classification of countries as fragile states. The Chair requested IEG to review the use of term "LICUS" in its report in view of the recent broad preference to refer to these countries as "fragile states." A speaker proposed monitoring "countries at risk," reporting annually to the Board. *Management acknowledged that the Bank does not*

have a strong system of analyzing the risks of fragility, which it was prepared to examine further.

Aid-Allocation System. Diverse views were expressed with respect to IEG's recommendation to develop aid-allocation criteria for LICUS to ensure these countries are not under- or over-aided. While some speakers suggested clarifying whether LICUS are under- or over-aided, taking into consideration the countries' absorptive capacity, others observed that this matter is beyond the Bank's control, given the importance of other donor allocations. *On the issue of absorptive capacity, management mentioned that two changes in IDA 14 had been made to address the needs of fragile state: (i) stretch the resource allocations for post-conflict countries, based on research that indicates improvements in absorptive capacity three to four years after the end of conflict; and (ii) introduce an exceptional provision for countries newly re-engaging with the international community. It also echoed a member's emphasis on need for sustained and predictable financial support for fragile states, noting that some of these countries (for example, Timor-Leste) do face periodic setbacks, and the Bank and donors need to be prepared to stand by these countries throughout.*

Many speakers thought the PBA mechanism could be adjusted or fine tuned. However, a member wanted to maintain the current system while others cautioned against major adjustments and allocation criteria based on factors other than performance. The need for a clearly articulated and defined framework for allocation was also stressed. One member requested management views on IEG findings about the "patched-up" nature of the current aid-allocation system for fragile states. The limitations of the CPIA were discussed, including the need to react quickly to quick turnaround or sharp deterioration of the country situation. *Management agreed with IEG that at each round of IDA replenishment, some adjustments are made to the allocation system. Accordingly, there should be a periodic review of it, including ways to simplify and enhance transparency, while*

maintaining focus on governance. Management assured CODE that the issues of time lag of CPIA and resource allocation for turnaround situations were on its radar screen, but there was no easy solution given the careful due process required for CPIA. Speakers looked forward to the IDA 14 Mid-Term Review, which was expected to address some of these issues.

Partnership. Members commented on strengthening donor coordination, assessing effectiveness of partnerships, and ensuring the Bank's country assistance complements that of the UN and other donors. *Staff provided examples of donor coordination in Sudan, Liberia, and the Central African Republic; speakers appreciated hearing about the improvements in this area. In response to the interest expressed in UN-Bank cooperation, management said there have been improvements, and in countries such as Democratic Republic of Congo, Timor-Leste, Liberia, and Haiti, the UN brings their expertise in political governance and security sector reform, while the Bank contributes to economic recovery and public finance and civil service reforms under an integrated strategy or results framework.*

Internal Coordination. Many speakers asked about roles and responsibilities, overlaps, and the pros and cons of merging the LICUS Unit and the Conflict Prevention and Reconstruction (CPR) Unit. A few of them noted the confusion among external partners and the need to strengthen the case for maintaining two separate units. Some also wondered about the implications, if any, of the new Sustainable Development Network (SDN). Other questions related to the link between the LICUS and other Bank initiatives (for example, Africa capacity building) and the effective use of Trust Funds, which could be assessed. *Management responded that the CPR Unit in the Social Development Department is a technical unit that works with Regions, while the LICUS Unit was established to reinforce support for fragile stages through enhanced cross-sectoral coordination. It had a more positive view about the collaboration between the two units than IEG, but also accepted the*

need to further consider the IEG recommendation in the context of the recently constituted SDN. Management expected the new SDN would enhance the synergy between social, environment, and infrastructure to support CPR work, as well as better linkage with Hazard Risk Management Team (also under SDN), in places where conflict and natural disasters converge, such as in Aceh.

Staffing. Speakers stressed the need for change in organizational culture and improved deployment of internal resources to support fragile states, commenting on issues related to deployment of experienced staff in the field, the setting up of supportive incentive systems (for example, promotion, family support, special benefits), and more transparency regarding allocation of staff resources for LICUS. *Management*

elaborated on recent efforts to differentiate incentives between service in LICUS and other countries by introducing better locality premium, hazard pay, and R & R; improving reentry guarantees; establishing LICUS service as a criterion for technical promotion at level H; and accommodating family needs. At the same time, management acknowledged that more needed to be done, and Operations Policy and Country Services and Human Resource Departments, together with the Regions, were working to further improve the incentive structure for LICUS assignments. A member asked management to commit to a timetable for presenting concrete proposals to address internal organizational issues, to which management responded that draft paper on strengthening the organizational response to fragile states is expected to be ready later in 2006.

Pietro Veglio
Chairman