

**CONCEPT NOTE**

**2015 DEVELOPMENT POLICY FINANCING  
RETROSPECTIVE**

**OPERATIONS POLICY AND COUNTRY SERVICES  
THE WORLD BANK**

# 2015 DEVELOPMENT POLICY FINANCING RETROSPECTIVE CONCEPT NOTE<sup>1</sup>

## I. INTRODUCTION

1. **Objectives of the 2015 DPF Retrospective.** The objective of the 2015 Development Policy Financing<sup>2</sup> (DPF) Retrospective is to distill lessons from the Bank experience with the use of DPF in the last three years (i.e. since the last Retrospective). In alignment with the World Bank Group Strategy, the Retrospective will focus on three key questions: (1) How are countries' policies supported by DPF conceptually linked to poverty reduction and shared prosperity? (2) How successful have Development Policy Operations (DPOs) been at achieving their intended results, and have the results been sustained? (3) To what extent do countries' development reforms supported by DPF account for environmental, social and economic sustainability?
2. **Coverage and timing.** The Retrospective will cover the period between April 1, 2012 (the cut-off date for the 2012 Retrospective) and December 31, 2014. As of June 30, 2014, 136 DPOs have been approved during this period, with another 32 anticipated for the next two quarters. The Retrospective will also present long-term trends of DPF, covering the entire first 10 years of the instrument. The Retrospective will be completed by October 2015. A proposed calendar is included in Section V.
3. **Outline of the Concept Note.** This concept note is structured as follows. Following this brief introduction, Section II presents a summary of the main findings of previous reviews of DPF. Section III discusses DPF in the context of the 2013 World Bank Group (WBG) Strategy. Section IV presents key trends in DPF. Section V spells out how the three key questions that represent the focus of the 2015 Retrospective will be analyzed (chapter by chapter). Section VI concludes with a brief description of the proposed consultations, process and timeframe. Annex 1 sets out an outline for the Retrospective, Annex 2 presents the proposed Consultation Plan, and Annex 3 provides additional DPF summary data.

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<sup>1</sup> This Concept Note was prepared by Jasmin Chakeri and Manuela Francisco with substantive inputs from Adelita Barrett, Uwi Basaninyenzi, Larry Bouton, Stefano Curto, Saudamini Dabak, Patricia Geli, Fernando Loayza, Jason Mayfield, Muthukumara Mani, Appolenia Mbowe, Peter Moll, Pablo Saavedra and Adriana Weisman. Kyle Peters, Linda van Gelder and Ed Mountfield provided overall guidance and quality assurance. Valuable comments and suggestions received from Jeff Chelsky, Maria Davalos, Melissa Fossberg, Gabriela Inchauste, Toyin Jagha, Mark King, Luis Felipe Lopez-Calva, Kseniya Lvovsky, Lisandro Martin, Una Meades, Glenn Morgan, Ambar Narayan, Carolina Sanchez, Sarosh Sattar and Sanjay Vani are gratefully acknowledged. Hiwot Demeke provided outstanding assistance.

<sup>2</sup> In July 2014 with the mainstreaming of Policy Based Guarantees into OP8.60 Development Policy Lending was renamed to Development Policy Financing (DPF). Hereafter any loan, credit, grant or guarantee will be referred to as DPF even if approved before July 2014.

## II. REVIEWS OF BANK DEVELOPMENT POLICY FINANCING

### *Retrospectives*

4. The Bank has systematically analyzed its experience with policy-based lending since the introduction of this instrument in the early 1980s.<sup>3</sup> Similarly, since the introduction of OP8.60 in August 2004 the Bank has conducted reviews of Development Policy Financing about every three years (in 2006, 2009, and most recently in 2012). These exercises consisted of a review of the entire universe of operations approved during the three-year period to take stock of the use of the instrument and distill key lessons.

5. Both the 2009 and 2012 Retrospectives, together covering a period of six years of DPF (over 380 operations), confirmed the overall robustness of DPF as a useful instrument to provide financing and policy advice in support of a country's medium-term development goals. The 2012 Retrospective concluded that DPF has continued to be a flexible instrument to respond to client country needs. During the global financial crisis, its nimbleness proved to be valuable in supporting critical reforms and pursuing key development outcomes across a broad range of countries. Client countries, international financing institutions, and other development partners continue to value the convening framework for policy dialogue and structural reforms it offers.

6. Despite overall good performance and significant progress made in many areas (including significant improvement in the results frameworks, lessening of conditionality, and strengthened country ownership and leadership of the reform programs) the last DPF Retrospective highlighted a number of areas that could be further strengthened. These included the need to increase focus on the most critical actions to achieve the intended results; a more thorough and consistent assessment of risks and opportunities; a strengthened assessment of the adequacy of the macroeconomic policy framework; an improved linkage between analytical underpinnings and the design of the operation; and an increased use of environment analysis and PSIA to inform DPOs.

7. Several measures were taken to strengthen these aspects of DPF: (i) preparation of a guidance note on results; (ii) issuance of a guidance note on the macroeconomic policy framework and collaboration with the IMF; and (iii) development of a guidance note on poverty and social impact analysis. The Bank has also revised the template of the program document with the objective of strengthening the relations between prior actions and results, and analytical underpinnings and reforms supported. To strengthen the risk/opportunities assessment, a new framework for operations risk management that applies to all operations (including DPF) and CPFs was launched on October 1, 2014. The new framework is expected to improve the way the Bank manages risk in operations

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<sup>3</sup> For earlier reviews, see: Structural Adjustment Lending: A First Review of Experience, Operations Evaluation Report No. 6409, World Bank, September 24, 1986; Report on Adjustment lending: Policies for the Recovery of Growth (R90-51, IDA/R90-49), March 26, 1990; Third Report on Adjustment Lending: Private and Public Resources for Growth (R92-47, IDA/R92-29), March 24, 1992.

in order to facilitate greater impact on development results. In addition, as part of the guarantee reform – the most significant reform to Bank guarantees in the last 20 years – Policy-Based Guarantees were mainstreamed into OP8.60. This reform will help the Bank leverage further its financial resources and synergies across the World Bank Group by mobilizing private-sector financing for our clients.

### *Other reviews of the instrument*

8. There have also been reviews of experience with DPF by DEC and the Bank’s Independent Evaluation Group (IEG). These reviews are complemented by analyses by independent researchers, other development partners and civil society organizations on the track record of budget support more broadly. Over time, this pool of knowledge is used to adapt the instrument to a changing world and to undertake policy and practice reforms to improve its development impact.

9. *Impact of DPF on economic policy.* Development Policy Financing has been found to have positive effects on economic policy. An analysis by Smets and Knack (2014) looks at “market reform” DPF (i.e. loans that support macroeconomic policy reforms) from 1995 to 2008 and finds that such financing has a positive but diminishing effect on the quality of economic policy, as measured by the CPIA score for clusters A (Economic Management) and B (Structural Policies). In other words, the CPIA scores increase with each additional DPF and each additional market reform prior action, up to a certain point.

10. *DPF in fragile and conflict-affected states.* A recent evaluation of the World Bank Group’s support to fragile and conflict-affected states (FCS) carried out by IEG finds that regular and predictable budget support is correlated with improvements in policy and institutional reforms, especially when the reforms are complemented by related investment lending and technical assistance. The IEG analysis shows a positive and statistically significant correlation between improvements in CPIA ratings with the number of DPLs received by the FCS. In particular, budget support is most highly associated with improvement in the CPIA ratings related to public sector management. Dom and Gordon (2011) in a paper commissioned by Oxfam confirm that general budget support is a useful instrument in FCS contexts when it supports capacity development and legitimacy building effects.

11. *Impact of general budget support on Public Financial Management (PFM).* General budget support has been found to be associated with improvements in PFM in non-FCS countries as well. A review by the Ministry of Finance of Denmark (2014) confirms that General Budget Support (GBS) contributes to strengthened PFM systems both through the expanded use of country PFM systems by budget support funds (as opposed to investment-linked funds) and through the focus on reforms related to PFM systems. In many cases, parallel capacity building operations have played an important role as well.

12. *Impact of general budget support on pro-poor expenditures.* Several studies have found general budget support to be associated with increased pro-poor spending. Furukawa and Takahata (2013) find that GBS increases the budget allocation for health; a

similar effect was found in the education sector (Ministry of Foreign Affairs of the Netherlands, 2012). The effect of GBS on increased pro-poor spending was greater than a corresponding increase in tax revenues; and, in some countries, greater than the financial transfer associated with the GBS. The research also found that countries that received substantial GBS climbed more *on average* on the UN development index than countries with little or no budget support, even after controlling for economic growth, good governance and debt relief. Despite these findings, there is a general acknowledgement that the increased spending on social sectors has not been accompanied by a sufficient improvement in the quality of public services (Ministry of Foreign Affairs of Denmark, 2014).

13. *Predictability of funds and transaction costs associated with general budget support.* The benefits of multi-year general budget support depend to a great extent on its predictability. However, the evidence on this is somewhat mixed. While in some countries, GBS has contributed to more predictability in aid flows (Caputo, Kemp and Lawson, 2011), delays remain in other cases, often as a consequence of issues related to underlying principles, such as the governance and the adequacy of the macroeconomic policy framework (Ministry of Foreign Affairs of the Netherlands, 2012). Several studies also found that general budget support entails lower transaction costs than project-based support, and that the transaction costs associated with GBS can be expected to decrease in the medium term. However, where a large number of donors are involved, and many different sectors are part of the policy dialogue, transaction costs (both for the client and the development partners) remain significant (Ministry of Foreign Affairs of Denmark, 2014).

### III. DPF AND THE 2013 WORLD BANK GROUP STRATEGY

14. The 2013 Strategy outlines how the World Bank Group (WBG) will work in partnership to help countries end extreme poverty and promote shared prosperity in a sustainable manner. The WBG has set two ambitious goals:

- (i) *End extreme poverty*: reduce the percentage of people living on less than \$1.25 a day to 3 percent by 2030.
- (ii) *Promote shared prosperity*: foster income growth of the bottom 40 percent of the population in every country.

15. The strategy also emphasizes the WBG's commitment to supporting countries achieve these goals in a sustainable manner: "Environmental, social and economic sustainability require action to secure the future of the planet, ensure social inclusion, and set a solid foundation for the well-being of future generations" (page 5, WBG Strategy).

16. As one of the key instruments to support country reforms that contribute to growth and poverty reduction, DPF supports a diverse set of countries ranging from low-income countries such as Liberia to middle-income countries such as Brazil. Reform content varies greatly, in line with the country's priorities and national development programs, and spans many different sectors. DPF policy pays particular attention to risks

related to environmental, social and economic sustainability of reforms supported by DPF. Accordingly, a key objective of this Retrospective is to assess how DPO-supported reforms are conceptually linked to poverty and shared prosperity in the short, medium and long term; and how they take into account environmental, social and economic sustainability. It also looks at sustainability of the development results throughout time as well as the factors that explain success in DPOs, that is, in achieving the intended development results.

#### IV. TRENDS IN THE PROVISION OF DPOS

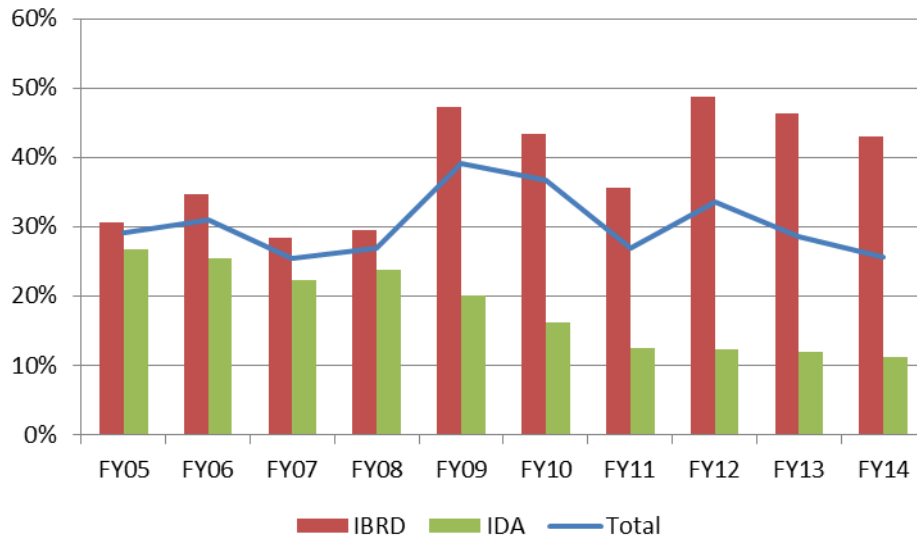
17. **Financing commitments.** Between FY05 and FY14, the Board approved a total of 632 DPOs, an average of 63 DPOs a year. This reflects a spike in the approval of DPOs during the global financial crisis, when member countries' financing needs increased. In the two years between Q4 of FY12 and Q3 of FY14, the annual average was 56, closer to the pre-crisis average. The total amount of development policy financing since FY05 amounts to US\$112 billion, an average annual commitment of US\$11 billion. From an average of US\$7 billion a year during the period FY05-08, commitments increased three-fold in FY09-10 to US\$20 billion but have since fallen to US\$11 billion. Since 2005, 4 PBGs have been approved by the Board (all of them in ECA) for a total commitment of US\$816 million.

Table 1: Development Policy Financing, FY05-14

	FY05	FY06	FY07	FY08	FY09	FY10	FY11	FY12	FY13	FY14
<b>IDA</b>										
Number of DPOs	33	30	35	29	33	33	34	28	32	29
Commitments (US\$m)	2,291	2,435	2,645	2,672	2,820	2,378	2,057	1,827	1,964	2,489
<b>IBRD</b>										
Number of DPOs	19	21	22	18	39	48	36	28	30	31
Commitments (US\$m)	3,804	4,906	3,635	4,022	15,635	19,210	9,609	10,131	7,120	8,155
<b>Total</b>										
Number of DPOs	54	51	57	47	72	81	70	56	62	60
Commitments (US\$m)	6,370	7,340	6,280	6,694	18,455	21,588	11,665	11,958	9,084	10,644
<b>PBGs</b>										
Number of PBGs	0	0	0	0	0	0	1	2	1	0
Commitments (US\$m)	0	0	0	0	0	0	400	214	202	0

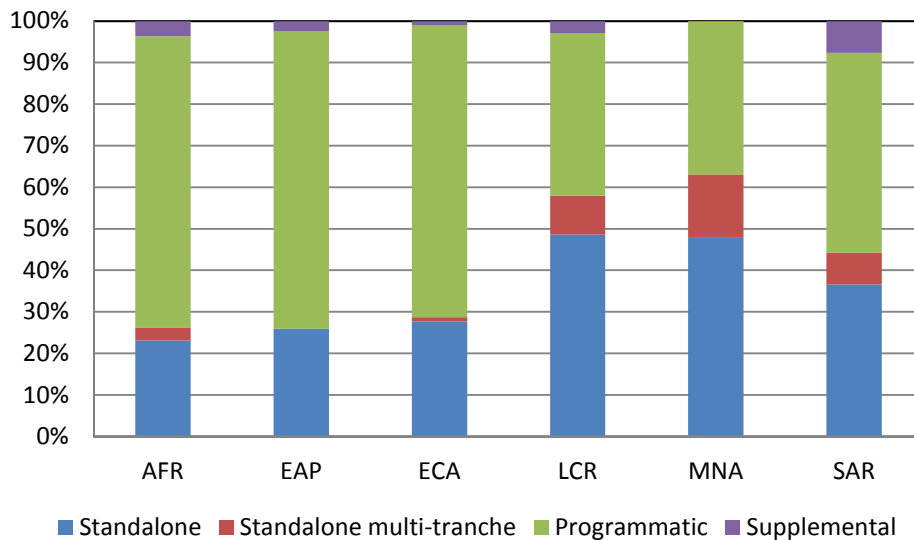
18. **IBRD/IDA shares.** Since FY05, IBRD countries have accounted, on average, for 75 percent of DPO commitments. The share of IBRD in total DPO commitments reached a peak in FY10 when it accounted for 89 percent. Since then, the IBRD share has fallen to 77 percent in FY14. DPF has accounted for an average of 39 percent of annual IBRD commitments and 18 percent of IDA commitments (Figure 1). Overall, DPF has accounted for one-third of total World Bank commitments since FY05.

Figure 1: Share of DPOs in total commitments, FY05-14



19. **Stand-alone operations vs. programmatic series.** Following the spike in stand-alone DPOs in FY10 in the wake of the global financial crisis, their share of total DPOs has fallen back to 31 percent between Q4FY12 and Q1FY15. The LCR and MNA regions account for the highest share of stand-alone operations, with 58 percent and 36 percent of DPOs, respectively. In the case of LCR, this includes 2 multi-tranche operations.<sup>4</sup> Finally, one supplemental financing DPO (to the Philippines) was approved in this period (Figure 2).

Figure 2: Types of DPOs by region (Q1FY05-Q1FY15)



<sup>4</sup> Acre Strengthening Public Policies DPL (P147913) and Bahia DPL (P126351), both in Brazil.

20. ***DPO options.*** Since 2005, 36 sub-national DPOs have been approved by the Board. These include 19 sub-national DPOs in Brazil, 8 in Pakistan, 6 in India, 3 in Nigeria and 1 in Russia. In the same timeframe, the Board approved 15 Deferred Drawdown (DDO) DPOs, 10 Catastrophe DDOs (all but one of which in LCR) and 3 Special DPOs (all of which in ECA).

21. ***Fragile and conflict affected countries.*** The Board has approved 93 DPOs for fragile and conflict affected countries since FY05, with total commitments reaching US\$4 billion. Since the last DPF Retrospective (Q4FY12), on average 9 DPOs to fragile and conflict affected countries were approved per year, accounting for 16 percent of IDA development policy support during that period.

22. ***Small states.*** Since FY05, 57 DPOs targeting small states have been approved with US\$830 million in commitments. In the period since the last DPF Retrospective, 22 DPOs were approved by the Board, averaging US\$80 million a year in commitments. These were distributed across AFR (11), EAP (9), LAC (1) and SAR (1). Sixteen of these operations were financed by IDA and all but five were part of a programmatic series.

## **V. PROPOSED STRUCTURE AND CONTENT OF THE REPORT**

23. The Retrospective will be structured in 7 chapters. The first chapter will set the stage for the report, including the context and objectives. The second chapter will analyze the main trends in the provision of DPF in the 10 years of the instrument. The third chapter will discuss the conceptual linkages between DPF prior actions and poverty reduction and shared prosperity in the medium/long term. The fourth chapter will discuss aspects related to environmental, social and economic sustainability. Chapter five will review DPO performance at the operation and result level and will present findings of an empirical analysis on determinants of DPO performance. Chapter six will review implementation of recent reforms, including an in-depth review of DPOs with DDO and DPOs with Cat-DDO. The seventh and last chapter will conclude with a set of recommendations based on the main lessons learned from the DPF experience over the past three years.

### **Chapter I – Introduction**

24. This chapter will set out the objectives and motivation of the Retrospective. It will also review the main recommendations of the 2012 Retrospective as well as the follow-up actions implemented since its publication.



## **Chapter II – 10 years of Development Policy Financing: Overall Trends**

25. This chapter will look at the key features of DPOs since their introduction in FY05. It will present the changes in the volume of commitments and in the share of DPOs in total Bank financing by client segment, region, and Global Practices (GPs) and Cross Cutting Solutions Areas (CCSAs). It will also provide a breakdown of DPOs by design features (programmatic, stand-alone, multi-tranche, supplemental financing) and options (DDO, CAT-DDO, Special DPOs).

26. The chapter will pay special attention to the steady decline in DPO commitments (as a share of total commitments) in IDA countries since the introduction of OP8.60 in 2004. Several hypotheses will be examined, including those related to (i) the reduction in macro-fiscal imbalances, which may reduce the need for budget support; (ii) the increased need for infrastructure investments (especially in transport and energy), which call for more project financing; (iii) the constraints imposed by joint budget support (involving several donors); and (iv) the reluctance to re-engage in DPOs following the discontinuation of a series due to reform slippages.

## **Chapter III – Reforms Supported by DPF and Their Conceptual Linkage to Poverty and Shared Prosperity**

21. This chapter will present an overview of the reforms supported by DPF. First, some descriptive statistics of the prior actions during the 10 years of DPF will be presented. This will include a breakdown of prior actions by client segment, region and GP/CCSA. This section will also examine whether there has been a shift from “first generation” reforms (such as public financial management) supported by DPF in the early years, to “second generation” reforms (including sector-specific reforms supporting infrastructure and private investment) supported by DPF more recently; and if so, what the operational implications of this shift are.

22. For the period covered by this Retrospective (Q4FY12-Q2FY15), a review of the prior actions and their conceptual linkages to poverty reduction and shared prosperity in the short and medium to long term will be completed. All prior actions supported by DPOs are expected to contribute to poverty reduction and shared prosperity in the *medium and long run*, even though only a relatively small share of DPOs support prior actions that *directly* impact poverty and income distribution *in the short run*. This is because the vast majority of prior actions support policy and institutional measures in public sector governance, financial and private sector development and other areas that do not immediately affect the income of the poor. This chapter will identify the sector and thematic coverage of prior actions for the period under review and classify them by policy content. The analysis will first consider how many of the reforms supported by DPOs during the period under review were likely to have significant *short-term* poverty and distributional impacts. It will then seek to sketch out the conceptual linkages explaining how each sub-group of prior actions is expected to contribute to poverty reduction and shared prosperity in the *medium- to long run*. The analysis will draw on the

framework developed by the Poverty Global Practice and presented in the report “Shared Prosperity: Paving the Way in Europe and Central Asia” (2014). The framework offers a schematic way to map possible *transmission mechanisms* between policy interventions and poverty reduction/shared prosperity. The mapping will draw on data from the OPCS Development Policy Actions Database (DPAD) that is updated annually and made available to the public. It is important to note, however, that the analysis will not attempt to quantify the impact of prior actions on poverty reduction and shared prosperity, but rather sketch out the “theory of change” for each of the policy areas.

#### **Chapter IV – Sustainability of Reforms Supported by Development Policy Financing**

23. Environmental, social and economic sustainability is a key consideration in Bank operations, including DPF. Environmental and social impacts (positive or negative) of DPF-supported reforms have to be carefully considered as they may affect sustainability in the medium to long run. Similarly, the macroeconomic environment in which the reforms take place, and its sustainability, also need to be carefully assessed. This chapter will analyze each of these considerations by assessing the implementation of provisions in the operational policy related to social, environmental and economic aspects.

24. ***Environmental impacts.*** Many DPOs include prior actions intended to support environmental sustainability. However, the policy also recognizes that some DPF-supported reforms could carry the risk of adverse environmental impacts. OP8.60 requires Bank staff to determine whether specific policy actions to be supported by the operation are likely to cause significant effects on the country’s environment, forests and other natural resources. For policies with likely significant effects, the Bank discusses in the PD the borrower’s systems for reducing such adverse effects and enhancing positive ones, drawing on relevant country-level or sectoral environment analysis. If there are significant gaps in the analysis or shortcomings in the country’s system or capacity, the PD should describe how these shortcomings would be addressed before or during program implementation.

25. This section will analyze (i) how many prior actions supported by all the DPOs approved in the period of the Retrospective were/are likely to have significant positive or adverse environmental effects, and what the key characteristics of these prior actions are; (ii) to what extent Program Documents adequately identified such effects; (iii) whether specific analytical tools or studies have been used to make this assessment (toolkit, sector study, among others); (iv) whether, in the case of potential significant negative (or positive) effects, the PD adequately discusses the borrower’s systems for reducing (or enhancing) such effects; and (v) whether the assessment of the borrower systems is grounded on analytical foundations (Country Environment Analysis, Policy Strategic Environment Assessments, among others).

26. The analysis will be conducted by a team that includes experienced environment specialists/environmental economists. The desk review of the prior actions supported by DPF will follow the requirements as set out in OP8.60. It will seek to distinguish between prior actions that are likely to have direct, “primary” effects; and those that may contribute to more indirect, “secondary” effects, considering the likely transmission

channels. These transmission channels depend on how well environmental resources are managed and on what policies the government introduces to mitigate any negative or strengthen positive environmental impacts of the reforms.<sup>5</sup>

27. The desk review may be complemented, in some cases, by in-depth analysis at the country level. The work will be informed by stakeholder consultations with clients and civil society. The findings of the analyses carried out in this section of the Retrospective will inform revisions of the existing guidance and toolkit to ensure that DPF supports policies in an environmentally sustainable manner. In parallel, IEG is preparing a learning product exploring the assessment of environmental and social effects in DPOs. This report is expected to be completed in the spring of 2014 and taken into consideration in this section of the DPF Retrospective.

**Box 1: Adequacy of OP8.60 to manage environmental impacts**

All Bank instruments include policies to protect people and the environment in a manner appropriate to each instrument. In the case of Development Policy Financing (DPF), the Operation Policy (OP8.60) has provisions on poverty, social and environmental effects that are tailored to an instrument that supports policy and institutional reforms.

DPF provides budget support upon completion of a program of reforms to help countries improve the livelihoods of people, build institutions, and strengthen capacity in a sustainable manner. As such, DPF is an instrument with different characteristics to IPF. Unlike IPF, DPF does not finance specific investments, such as roads, dams or power plants. IPF safeguards are designed for financing of specific goods and services within projects with a physical footprint. Thus IPF safeguards are neither conceptually appropriate nor applicable in practice to DPF, which disburses into the general budget and supports policies at the country level.

28. **Social impacts.** OP8.60 requires that the Bank determine whether specific country policies supported by the operation are likely to have significant poverty and social consequences, especially on poor people and vulnerable groups. Complementing the analysis of the likely direct, short-term impacts of DPF-supported policies on poverty reduction and shared prosperity (see Chapter III), this section will review to what extent the program documents discussed relevant analytic knowledge of such impacts and of the borrower's systems for reducing negative (and enhancing positive) effects associated with the specific policies being supported. The analysis will be based on a desk review of the Program Documents of all DPF approved since the last Retrospective. This section

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<sup>5</sup> The potential transmission channels are discussed in greater detail in the Toolkit on "Assessing the Environmental, Forest and Other Natural Resource Aspects of Development Policy Lending", published in 2008.

will also review the discussion of consultations on DPF supported reforms in the Program Document.

29. *Economic sustainability.* In addition to environmental and social sustainability, the economic sustainability of policy reforms supported by DPOs also needs to be taken into account. OP 8.60 states that the Bank undertakes development policy financing in a country only when it has determined that the country's macroeconomic policy framework is adequate. The assessment of the adequacy of the policy framework needs to be underpinned by a discussion of the sustainability of economic policies (including those supported by the DPO) affecting the real sector, external sector, financial sector, monetary aggregates and fiscal accounts (including debt sustainability).<sup>6</sup> The 2012 Retrospective found that the assessment of the macroeconomic policy framework in DPOs had improved, but that the comprehensiveness of the analysis could be further strengthened, especially with respect to the discussion of public expenditure and of the economic outlook at the sub-national level (for DPOs to political subdivisions). This section will review to what extent DPO Program Documents include a comprehensive discussion of these aspects.

## **Chapter V – Results in Development Policy Financing**

30. This chapter will assess to what extent the expected results have been achieved. The chapter will be divided into three sections. The first will present descriptive statistics of the performance of DPF at the operation level and at the individual-results level (based on ICRs and IEG evaluations). The second section will present the findings of an empirical analysis that aims at identifying key factors associated with better DPO performance. The third and final section of this chapter will assess the long term impact and sustainability of some reforms supported by several DPOs.

31. *Descriptive statistics of DPF performance.* This section will present key descriptive statistics of: (i) characteristics of results frameworks, including the number of result indicators, existence of baseline and target values, and the overall quality of the framework; (ii) DPO performance (at the operation level), as per the ICR and IEG evaluations, broken down by client segment, regions and GP and CSSAs; and (iii) analysis of performance at the result level. Based on a desk review, this will consist of an assessment of whether target results were achieved according to the results documented in the ICR. The descriptive statistics on the achievement of results indicators will be presented by sectoral and thematic breakdown. Finally, case studies of results achieved by DPF in a select number of thematic areas and/or countries will be presented. The selected areas of IDA commitments will receive particular attention.

32. The analysis in this section will draw on the OPCS database of all results included in the policy matrices for which there is an ICR. While there will be an estimated 136 operations in the total universe (not including the current pipeline for Q1-Q2 of FY15) to be covered by the Retrospective, it is anticipated that a much smaller number of ICRs and

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<sup>6</sup> A revised, more detailed guidance note on the “Macroeconomic Policy Framework and Collaboration with the IMF in Development Policy Operations” was issued in September 2013.

IEG evaluations of ICRs will be available for the review (because programmatic series have only one ICR at the end of the series and because the ICRs and IEG evaluations of ICRs will often not yet be available for operations that closed in the previous 18 months).

33. ***Empirical analysis of DPF performance.*** Building on past work by previous researchers, all DPOs since their inception (FY05) will be studied to identify common elements associated with success, using a regression analysis approach. The objective of this inquiry is to understand better what factors could help to improve the success of the instrument. In particular, it is of interest to know how much of the success of DPOs depends on givens such as country factors, and how much depends on factors under the control of the task team leader. Therefore, the analysis of the correlates of success in DPOs will estimate, using econometric techniques, the relationship between DPO performance (measured by IEG ratings) and a number of variables such as TTL experience, type and number of prior actions, quality of the results framework, programmatic vs. stand-alone operations and the loan size. Our preliminary evidence is that factors associated with the operation itself, and which are clearly in evidence from the program document at the time of presentation to the Board, are important correlates of the operation's success; so that improved design provides an avenue for further strengthening of the impact of development policy financing.

34. ***Long-term impact of reforms supported by DPOs.*** This section will include three analyses. First, it will examine the sustainability of DPO-supported reforms in the area Public Financial Management (PFM). Overtime, PFM has represented the single most common area of support (21% of prior actions of the total universe). This is a reflection of the fact that DPOs disburse into the general budget and thus require the strengthening of public finance systems. The drill-down in the area of PFM reforms will also use the PEFA database and select for analysis those instances in which there are at least three PEFA diagnostics, between the first two of which there has been a DPO with prior actions in public finance management.

35. Second, it will update the research carried out by Smets and Knack (2014) of the impact of “market reform” DPF on the quality of economic policy, to include DPF approved after 2008. This analysis would cover an additional 25% of prior actions and link them to longer term outcomes as measured by the relevant CPIA indicators.

36. Third, country case studies will examine the fate of a selected number of DPO-supported reforms in the several years following the completion of the DPO and the issuance of the implementation completion report (ICR). The ICR gives, in a systematic way, an assessment of the short-term results of the DPO-supported reforms. Based on a selected number of countries and operations, this section will analyze whether the short-term achievements were maintained in the medium-to-long term; or whether there was a tendency to reverse the reforms over time.

## **Chapter VI – Reforms**

37. This chapter will review the reforms that the Bank has undertaken in recent years with respect to DPF. This includes three sets of measures: (i) the Enhanced DDO and

introduction of Cat-DDO feature; (ii) the new operational framework on guarantees, and (iii) the new framework for operations risk management.

38. ***Enhanced DDO and introduction of Cat DDO.*** The DDO feature gives IBRD-eligible countries the option to defer disbursement up to three years with the possibility of renewing, with Board approval, for an additional period of up to three years. DDO for policy-based lending instruments was introduced in 2001 but was severely underutilized until a change in policy was introduced in 2008 to make the availability of the funds more predictable.<sup>7</sup> The Bank also introduced a specialized DDO feature to provide immediate liquidity in emergency situations caused by natural disasters and catastrophes. The main purpose of this option is to support countries' efforts to enhance their capacity to manage natural hazard risk and provide a source of bridge financing while other resources are being mobilized. DPOs with Cat-DDO can be renewed up to 4 times and be active for 15 years. Given that DPOs with Cat-DDOs can be disbursed even if the macroeconomic framework is not adequate (an exception in the policy reserved to this option only) a ceiling on the amount has been established (0.25 percent of GDP or US\$500 million, whichever is smaller). This review, to be completed as part of this Retrospective and together with Treasury and the relevant GPs, will be the first comprehensive review on the enhanced DDO and Cat-DDO since their introduction 7 years ago.

39. ***Operational policy framework on guarantees.*** In December 2013, the Board approved a major reform of the Bank's operational policy framework on guarantees, which became effective on July 1, 2014. Under the revised framework, guarantees are no longer a separate instrument, but are fully integrated into Investment Project Financing (for project-based guarantees) and Development Policy Financing (for policy-based guarantees - PBGs)<sup>8</sup> and their respective operational policies. The objective of the reform is to enhance the visibility of guarantees, facilitate their use by Bank teams and demand from client countries, and lift various constraints that arise from having separate policies.

40. The reforms are expected to contribute to an increase in the use of guarantees, including PBGs. Since the introduction of policy-based guarantees, there have only been a total of six PBG operations: Argentina (FY00), Colombia (FY01), Serbia (FY11), Macedonia (FY12 and FY13) and Montenegro (FY12). Despite the sharp increase in lending following the global financial crisis, the use of PBGs has remained limited, with only four post-crisis operations, all in the ECA region. This section will review the experience with the PBGs approved during the period under review and draw lessons for the use of this source of financing under DPF.

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<sup>7</sup> A review in 2008 found that borrowers were hesitant to use this feature because of its harder financing terms and the perception that funds could not be available when required, given that withdrawal required the Bank's reconfirmation that the macroeconomic policy framework and overall program implementation were adequate. As a result, the Bank introduced a streamlined verification protocol in 2008, under which the Bank continues to monitor the macroeconomic policy framework and adherence to the overall program, and advises the borrower of the need for a review if at any time the conditions are not satisfied. Once both drawdown conditions are satisfied, the Bank confirms that the eligibility to submit disbursement requests has been restored.

<sup>8</sup> PBGs provide partial credit guarantees to help borrowers access external financing for general budgetary borrowing associated with policy and institutional reforms.

41. **Framework for risk management in operations.** The 2012 DPL Retrospective recommended a more systematic approach to discussing risks in development policy lending. As part of a general overhaul of the Bank’s framework for risk management in operations, the Systematic Operations Risk-Rating Tool (SORT) was launched in October 2014 to support more consistent and systematic risk assessments across all Bank operations and Country Partnership Frameworks. The SORT is a simple matrix consisting of nine risk categories, plus an overall risk assessment; risk under each category is rated high, substantial, moderate or low. The Program Document will discuss the overall risk and the most relevant risks among the nine categories, as well as the relevant risk management measures. The risk assessed in the SORT is defined as the client’s risks to development results associated with the operation or operational engagement, including risks to the development objectives of the operation/CPF and risks of unintended adverse impacts. The SORT covers risks during both the preparation and the implementation stages, in an integrated manner, and is updated throughout the life of the operation/CPF.

42. This chapter will review the risk ratings of DPF that were approved during the period under review and compare them against the achievement of outcomes as well as other indicators. For DPF using the new SORT, a more detailed breakdown of risk ratings by category will be provided, although the number of operations included in this analysis will be limited.

## **Chapter VII – Conclusions and Recommendations**

43. Finally, the Retrospective will distill lessons of the experience with the use of DPOs over the period under review, identify areas that need to be strengthened in the future and recommend concrete measure to strengthen them (including adjustments in staff guidance where needed).

### **VI. CONSULTATIONS, PROCESS AND TIMEFRAME**

44. **Consultations.** Stakeholder consultations will take place during the preparation of the Retrospective. The team will design a dedicated website for the Retrospective to keep interested stakeholders informed and to solicit and receive feedback as the preparation of the Retrospective advances. In addition, there will be face-to-face events at key stages to provide opportunities to directly engage with stakeholders on the scope of the Retrospective. A more detailed consultation plan is included in Annex 2.

45. **Process.** The team will include staff from units across OPCS with responsibilities for results, risk, country economics, and knowledge. The OPCS team will work with the GPs and CCSAs that typically review important aspects of DPOs to jointly evaluate the Program Documents and ICRs of DPOs in their respective areas of expertise, including the Poverty GP (on PSIA), the Environment and Natural Resources GP (on environmental aspects), DEC and others. OPCS will also cooperate with TRE as well as with DEC in updating relevant research. Finally, OPCS will draw on inputs from extensive internal and external consultations.

46. ***Timeframe.*** The proposed timeframe for the Retrospective is as follows:

- December 2014: Bank-wide concept note review
- December 2014 – January 2015: Notification/Online comment period
- December 2014 – April 2015: Preparation of draft report
- April-May 2015: Face-to-Face consultations with stakeholders (including Spring Meetings)
- June 2015: OVP review of draft report
- July 2015: CODE meeting
- October 2015: Presentation to Board (IDA Mid-Term Review)



## **Annex 1: Suggested Outline of the Retrospective**

### **1. Introduction and Context of the Retrospective**

- 1.1. Motivation and objectives
- 1.2. Key findings of the 2012 DPL Retrospective and follow-up actions

### **2. 10 years of Development Policy Financing: Overall Trends**

- 2.1. Number and commitment volumes of DPF
- 2.2. Key characteristics of DPF
- 2.3. DPF in IDA countries

### **3. Reforms Supported by DPF and Their Conceptual Linkage to Poverty and Shared Prosperity**

- 3.1. Analysis of reforms supported by DPF in the last 10 years
- 3.2. Prior actions and their conceptual link to poverty reduction and shared prosperity

### **4. Sustainability of Reforms Supported by Development Policy Financing**

- 4.1. Environmental impacts
- 4.2. Social impacts
- 4.3. Economic sustainability

### **5. Results in Development Policy Financing**

- 5.1. Descriptive statistics on DPF performance
- 5.2. Empirical analysis of what drives success in DPF
- 5.3. DPF contribution to longer term country results:
  - 5.3.1. Public financial management
  - 5.3.2. Quality of economic policy
- 5.4. Case studies

### **6. Reforms**

- 6.1. DDO and Cat DDO
- 6.2. Operational policy framework on guarantees
- 6.3. Framework for risk management in operations

### **7. Lessons learned**

## **Annex 2: Proposed Consultation Plan**

Stakeholder consultations will take place during the preparation of the Retrospective. The feedback received will be compiled and summarized for the team's review and will be considered as the Retrospective moves forward.

**Objectives:** The objectives of the consultations is to elicit feedback from a wide variety of experts in as broad and inclusive manner as possible to provide input on (1) the objectives and direction of the Concept Note; and (2) key issues to be addressed in the World Bank's experience with the use of DPFs in the last three years along with trends in the last ten years.

**Stakeholders/Experts:** The stakeholders to be consulted include client governments, civil society organizations, shareholders, private sector actors and business associations, subject area experts (environmental, social, and governance), academics, bilateral and multilateral development organizations, and other interested development groups.

**Notification/Online Comment Period (December 2014- January 2015):** A notification period will take place to inform stakeholders about the process behind the Retrospective and forthcoming consultations. During this period, the Concept Note will be publicly posted and stakeholders will be invited to provide their comments on a dedicated consultation website over a period of thirty working days. The comments received on the concept note will inform the team as it conducts the analysis and develops preliminary findings.

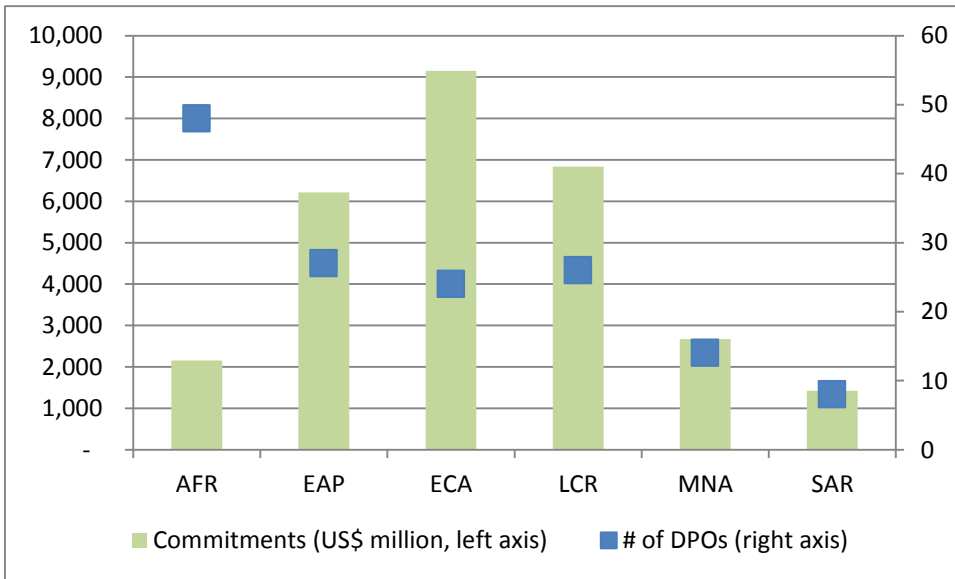
**Face-to-Face Consultations (April – May 2015):** A broad group of stakeholders will be invited to provide their comments on the preliminary findings of the Retrospective, including consultations during the Spring Meetings. This will be followed by consultations in countries, which may also include video-conference sessions.

**Online/Website:** A dedicated consultation webpage will provide a platform for stakeholders to provide input to the Retrospective. The webpage will include information related to the consultation process, timeline, relevant background information, and other related resources as the consultation process progresses. Arrangements will be made to translate materials into other languages.

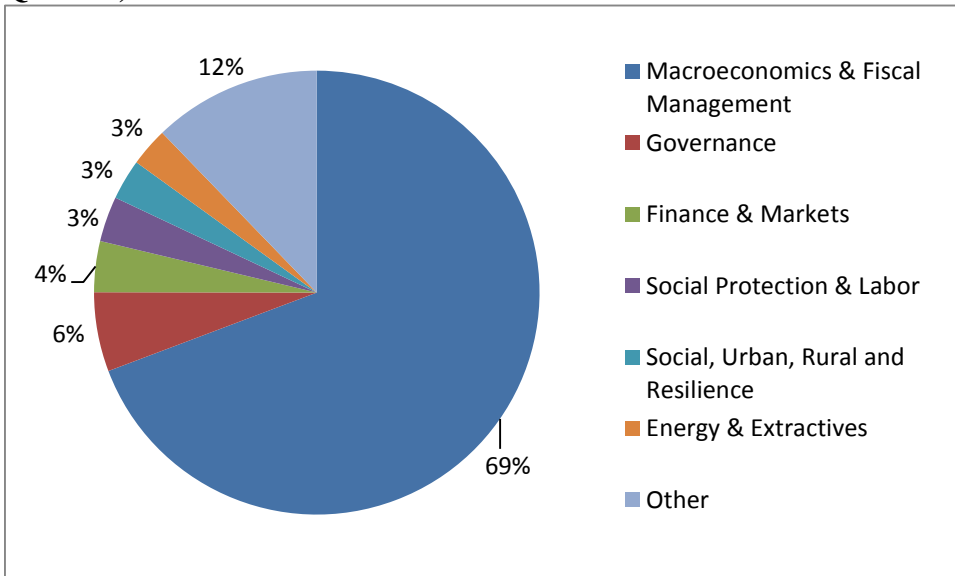
A summary of the feedback received on the preliminary findings will be made public. This feedback will inform the Retrospective.

**Annex 3: Data Annex**

**Figure 3: DPOs by region (Q4FY12-Q1FY15)**



**Figure 4: DPOs by Global Practice/Cross-Cutting Solutions Area (Q4FY12-Q1FY15)**



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