ARTF FINANCING STRATEGY FY1394-1396 (2015-2017)

Background: The ARTF Financing Strategy (FS) was first introduced at the London Conference in 2010 as a planning tool outlining priorities for ARTF financing. The previous Financing Strategy ran from FY1391 to 1393 (2012 to 2014). The Financing Strategy FY1391-1393 outlined the three-year financing for a total of $3.6 billion, averaging $1.2 billion per year, covering recurrent cost support, policy reforms and core development, and service provision programs including agriculture, rural development, infrastructure, education, health, and governance.

The New ARTF Financing Strategy: The new Financing Strategy covers a three-year period from FY1394 to 1396 (2015-2017) and outlines financing for a total of $2.7 billion. The objective of the FS is to align development interventions to emerging government priorities as articulated in the *Realizing Self Reliance* reform paper in London 2014, including a move towards programmatic approaches as a core government priority and to strengthen government ownership. The FS also outlines key development priorities for Afghanistan in the coming years and agrees on how ARTF funds are best prioritized in support of the Government of Afghanistan's reform priorities. The FS ensures strong government ownership and leadership of ARTF direction, and effective use of available resources as it is entirely aligned with government strategy and priorities and based on input from government. The FS will be updated on an annual basis to evaluate emerging needs and priorities against incoming donor contributions to ensure supply and demand meet.

Process: The FS is prepared in close cooperation among the ARTF stakeholders: the Government of Afghanistan, ARTF donors and the World Bank as the ARTF Administrator. The Administrator has arranged monthly meetings in the Strategy Group since January 2014 to inform donors of relevant issues to ensure that various stakeholders are able to engage in informed discussions on the FS. Following the inauguration of President Mohammad Ashraf Ghani on September 29, 2014, ARTF donors and the World Bank entered into focused discussions on the draft Financing Strategy. The first draft put forward by the World Bank was based on initial discussions with the new government. The draft agreed with government was discussed in the Strategy Group and following its agreement, the draft was sent to the ARTF Steering Committee for final endorsement. Due to the prolonged election period and the settling in of the new government, this Financing Strategy was delayed and did not go into effect in time for the start of FY1394. An Interim Arrangement was agreed with government and donors to enable select activities to proceed but requiring the new Financing Strategy to be approved by June 30, 2015. Please refer to Annex VII for more details on the Interim Arrangement.

Document Structure: The **Executive Summary** highlights the keys messages of the new Financing Strategy. **Section I** outlines how the ARTF operates, reflecting alignment with government priorities and with key global principles of aid effectiveness. **Section II** focuses on the operating context of the ARTF, analyzing key challenges of the country including fragility, poverty, and macroeconomic stability. **Section III** outlines the ARTF risk framework and explains how risks are managed at both the trust fund and project levels. **Section IV** draws out some of the key results and lessons learned from the previous Financing Strategy FY1391-1393. **Section V** outlines the financial framework for the new Financing Strategy FY1394-1396 and proposes the priorities for funding during FY1394, 1395, and 1396, including recurrent costs, investment programs and analytical activities. It also highlights the risks to development results given recent and current donor pledges and inflow trends into the ARTF.

EXECUTIVE SUMMARY

Background: The ARTF Financing Strategy was first introduced at the London Conference in 2010 as a planning and prioritization tool for the ARTF and to align financing to government priorities and strengthen government ownership of the ARTF and its resources. The previous Financing Strategy FY1391-1393 outlined a three-year program for a total of $3.6 billion and covered recurrent cost support, policy reforms as well as core service provision and capacity building programs in agriculture, rural development, infrastructure, education, health, and governance.

Alignment with Government Strategy: The new ARTF Financing Strategy FY1394-1396 aims to fully align with priorities of the new government as outlined in its *Realizing Self-Reliance* paper. It builds on the accomplishments and lessons of the previous strategy and a record of effectiveness and innovation in the past decade. Besides funding on-budget government programs, the ARTF structure ensures predictability of aid, convenes government and donors around critical development issues, and enhances transparency and ownership of aid. The ARTF, both through its Recurrent Cost Window (RCW) and the Investment Window (IW), is and expects to continue supporting programs that strengthen government systems and build sustainable implementation capacity in government institutions through the Transformation Decade as proposed by the *Realizing Self-Reliance* paper.

The *Realizing Self-Reliance* paper emphasizes the importance of programmatic approaches, understood as long-term, strategic arrangements consisting of interlinked projects with a common larger-scale objective. A programmatic approach aligns well with the use of the ARTF to pool funds in support of a government-led agenda, while making efficient use of limited capacity available in line ministries.

Governance reform is another top government priority, which focuses on building government capacity and strengthening anti-corruption efforts. The ARTF supports this through the Capacity Building for Results program, the Public Financial Management Reform Program II, and its general focus on capacity building as a cross-cutting theme across its portfolio. Anti-corruption efforts are supported through a rigid fiduciary framework that is continuously refined to ensure risks are mitigated. New initiatives are also being explored under the RCW and IP in support of government's renewed focus on transparency and accountability.

Finally, gender is a key cross-cutting theme highlighted by the *Realizing Self-Reliance* paper. The ARTF continues to support gender mainstreaming as a cross-cutting theme in all its projects to ensure tangible results at the community level.

Continuing Challenge of Poverty and Fragility: Afghanistan has seen considerable progress over the past 12 years. In spite of positive developments and results, the country has substantial needs and continues to face volatility and setbacks. Afghanistan is in the midst of multiple transitions toward self-sufficiency, including security, financial, and political. These multiple transition processes add to the stresses of an already fragile state. As a result, in 2014, Afghanistan recorded the lowest gross domestic product (GDP) growth rate of the past decade (1.9 percent) and government ran a fiscal deficit of over $500 million. Poverty levels have also remained stagnant at 36 per cent since 2008, with the highest incidence in rural areas. Afghanistan is therefore facing daunting challenges of high poverty levels, economic slowdown as a result of political and security transitions in 2014, a large fiscal deficit, and a range of development issues, all in the midst of an active conflict.

Supporting Fragility-sensitive Programming: Consolidating peace and development in Afghanistan remains vulnerable and volatile. Just as it is critical for the government to state its priorities, it is important for ARTF donors to continue to provide stable support for the new government in support of a positive change, while accepting the inevitable setbacks—seeing these challenges as part of the evolution of a maturing system rather than as signs of failure. The ARTF portfolio already responds to this context through the design of its RCW (e.g., the Incentive Program) and its focus on areas key to building government legitimacy such as national integration (National Solidarity Program and governance), expanding reach in service delivery areas (education and health), and expanding opportunities (economic management and infrastructure). In full alignment with the *Realizing Self-Reliance* paper, the new FS will prioritize areas that support government efforts to enhance governance, improve investment opportunities and human capacity, and further consolidate peace and national integration, while paying attention to regional dynamics and opportunities.

Fiscal Realities and the Need to Rebalance ARTF Financing: The government confronts a new fiscal reality as it recovers from the 1393 fiscal crisis and adjusts to the impact of lower growth, leading to planned constrained spending in the 1394 budget and continuing fiscal pressure in the coming years. Similarly, donors confront a constrained fiscal environment leading to modest or yet-to-be confirmed outlays for supporting Afghanistan. The Administrator estimates an overall financing envelope of approximately $2.8 billion for the three-year period FY1394-1396 (assuming donors provide similar levels of funding as last year). With outstanding commitments of $790 million for current projects, and recurrent cost support of $1.2 billion, the ARTF will have only $800 million for the three years ($266 million per year) for new investment projects under the new FS 1394-1396. This Financing Strategy presents and discusses the need to rebalance recurrent costs and investment projects as well as to prioritize limited funding available for new development projects.

Preliminary Proposals for Discussion: To ensure the ARTF continues substantial recurrent cost support in the coming year (1394) at a critical time for the new government, the Administrator proposes to continue the current level of recurrent cost financing of $400 million per year. Keeping the level of recurrent financing stable would allow the new government time to reform and increase its own revenues in support of fiscal sustainability, while also safeguarding funds for core development activities. The Administrator proposes to allocate the remaining $800 million to the pipeline of new investment projects over the coming three years, focused on service delivery, capacity and institution-building, and expanding economic opportunities. The pipeline estimated cost exceeds the projected available financing, thus an urgent prioritization exercise is required. Finally, the Administrator is establishing a research program to underpin a knowledge-driven development agenda as well as a Technical Assistance Facility to support capacity for key government priority areas. Government and donors have endorsed a fee increase to ensure effective program administration.[1]

[1]On March 17, 2015, the ARTF Steering Committee endorsed a fee increase from 2 to 3 percent on January 1, 2016, and further to 4 percent on January 1, 2017. The fee on Ad Hoc Payments will remain at 2 percent.

I. ARTF ALIGNMENT TO AFGHANISTAN'S DEVELOPMENT PRIORITIES

The ARTF is operating within the context of the Kabul Process,[2] initiated at the London Conference in 2010, feeding into four closely interlinked documents/processes: (i) The Afghanistan National Development Strategy (ANDS); (ii) the National Priority Programs (NPPs); (iii) the Tokyo Mutual Accountability Framework (TMAF); and (iv) the *Realizing Self-Reliance* paper, which establishes a mechanism to regularly monitor and review mutual commitments of the Afghan government and the international community to help Afghanistan achieve its development and governance goals. The ARTF supports two of the three ANDS pillars: (i) Good Governance, Rule of Law and Human rights; and (ii) Economic and Social Development. This support for the ANDS is achieved by aligning ARTF funding to key NPPs.

As government strategy and priorities develop and more details unfold, the ARTF will continue to progress in support of alignment. The annual update to the FS will capture such new developments. The next update to the FS is due at the beginning of FY1395.

i. Towards Self-reliance: Tokyo Conference on Afghanistan, July 2012

The TMAF, emerging from the Tokyo conference and Senior Officials Meeting in 2013, sets the stage for an interactive aid management engagement between the Government of Afghanistan and development partners. The TMAF outlines a number of areas for government and development partners to deliver on. The ARTF is a critical mechanism in this regard. The ARTF provides the mechanism for incentive financing through (i) the ARTF Incentive Program (IP); and (ii) the Ad-Hoc Payments (AHP).

One specific commitment in the TMAF is for donors to adhere to the principles of aid effectiveness, which includes a requirement for 50 percent of development aid being on-budget and 80 percent to be aligned with Afghan priorities as set out in the NPPs. ARTF financing is 100 percent on-budget and fully aligned with the NPPs at the strategic and programmatic level, and 95 percent at project level. The ARTF is therefore fully aligned with these TMAF commitments and provides a critical mechanism for donors to meet these targets, while ensuring the safeguarding of donor funds due to its strong fiduciary framework.

ii. Realizing Self-Reliance: The London Conference on Afghanistan, December 2014

At the London Conference in December 2014 the new Government of Afghanistan set out an ambitious reform agenda covering seven priorities: (i) improving security and political stability; (ii) tackling the underlying drivers of corruption; (iii) building better governance; (iv) restoring fiscal sustainability; (v) reforming development planning and management; (vi) bolstering private sector confidence; and (vii) ensuring citizen development and securing human rights. Underlying these priorities is a strong commitment to improve aid effectiveness in order to increase the impact of development programs on the lives of Afghans. The ARTF Financing Strategy aims to fully align with government priorities and be the

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[2] With the objective of setting the path for an "*economically sustainable, socially vibrant and stable Afghanistan, led by Afghans for Afghans, supported by the International Community.*"

main instrument of development reforms over the coming three years, building on its record for effectiveness and innovation to fit the changing context in Afghanistan. This includes programmatic approaches, governance reform, including strengthening anti-corruption efforts, as well as gender mainstreaming and capacity building as cross-cutting themes. Most critically though, strategy and prioritization must be government led to ensure that the ARTF support a country-owned agenda.

iii. ARTF's Aid Effectiveness—Supporting Development Priorities of Afghanistan

Afghanistan's reform priorities as articulated in the London paper on *Realizing Self Reliance* requires government and donors to deliver more on-budget assistance, align with national priorities, adjust technical assistance to build enduring systems, and share aid information in order to fulfill their commitments to an effective development partnership with Afghanistan. The ARTF embodies these principles and is globally a best-practice example of trust fund administration. The World Bank's Independent Evaluation Group (IEG) in its *Evaluation of the World Bank Group Program in Afghanistan (2002-2011)* noted the ARTF's successful role in pooling and using resources and recognized ARTF as an effective vehicle for donor coordination and resource mobilization. Furthermore, the IEG has singled out the ARTF's Incentive Program as an effective model for aligning government and donor priorities to support state-building reforms in Fragile and Conflict-affected Situations. The ARTF, both through its Recurrent Cost Window (RCW) and Investment Window (IW), is supporting programs that strengthen government systems and that aim to build sustainable implementation capacity in government institutions. Besides funding on-budget government programs, the overall structure of the ARTF ensures predictability of aid, convenes government and donors around critical development issues, and enhances transparency and ownership of aid. The 2012 external review of the ARTF (*ARTF at Cross-Roads: History and Future, 2012*) concluded that "*ARTF remains the mechanism of choice for on-budget funding, with low overhead/transaction costs, excellent transparency and high accountability, and provides a well-functioning arena for policy debate and consensus creation*."

Since its establishment in 2002, the ARTF has embodied the principles of aid effectiveness developed in various high-level meetings held over the past decade. The 2005 Paris Declaration on Aid Effectiveness asks donors to align aid with country priorities and help build recipient country institutions. The 2008 Accra Agenda for Action further recommends the use of recipient country systems, especially in public financial management. The New Deal for Engagement in Fragile States adopted in Busan in 2011 further enshrines country ownership, capacity building, and systems building in the aid effectiveness framework. The ARTF is very well aligned with these international aid effectiveness principles. The ARTF is on-budget, is fully aligned with the Afghanistan National Development Strategy, and has from its inception had a strong focus on helping establish government systems and capacity in Afghanistan.

Government, donors, and the World Bank agree that strong government ownership of the ARTF is critical. The Financing Strategy ensures full transparency on the operating context of the ARTF, including the available funding, which allows for government leadership to prioritize funds in alignment with its strategy and vision. As government capacity increases and the new government vision evolves, the ARTF will facilitate discussions on an exit strategy for the trust fund, allowing government to take the lead on how its ownership of ARTF management could be further strengthened over time.

II. THE OPERATING CONTEXT OF THE ARTF

The ARTF has achieved a number of significant results over the past decade of on-budget support to the Government of Afghanistan. However, results remain at risk in the context of fragility, nascent institutions, and a rapidly changing environment. This new Financing Strategy is being devised to a backdrop of stagnant poverty, deteriorating fiscal and economic environment as well as institutional changes. The next sections highlight these factors, the role the ARTF plays in systematically addressing these issues, and how the new Financing Strategy aligns with government priorities as outlined in the *Realizing Self-Reliance* paper.

i. Operating in a Context of Fragility

Afghanistan has seen considerable progress over the past 12 years. In spite of positive developments and results, progress is fragile and the country continues to face volatility and setbacks. Overcoming fragility and conflict necessitates the creation of robust and legitimate institutions, however this is a long and arduous process that can take a generation or more to achieve. Historically, countries that have managed to move out of fragility and conflict are not characterized by a one point in time decisive 'make it or break it' moment but rather go through a series of transitions. According to the *World Development Report 2011 on Conflict, Security and Development*: "*Just as violence repeats, efforts to build confidence and transform institutions typically follow a repeated spiral.*"[3] The repeated process, or spiral, provides opportunities for systems and capacities to develop: "*For each loop of the spiral, the same two phases recur: building confidence that positive chance is possible, prior to deepening the institutional transformation and strengthening governance outcomes.*"[4]

It is critical that government and donors understand the vulnerabilities facing Afghanistan and align themselves to focus on issues and activities that can support a positive direction in the spiral's trajectory over time while accepting the inevitable setbacks, seeing those challenges as part of the evolution of a maturing system rather than as signs of failure. The *World Development Report 2011* also notes that multiple stresses, including economic, justice, and security factors, increase the risk of repeated conflict and violence. There are a number of critical economic stress factors that apply and can trigger setbacks in the positive spiral and trigger renewed conflict in a fragile state like Afghanistan (see Table 1).

TABLE 1: Economic Stresses in Afghanistan

STRESSES	INTERNAL	EXTERNAL
Economic	• High levels of poverty • Youth unemployment and underemployment • Natural resource wealth • Corruption	• Declining donor financing • Security transition • Declining financing for Afghan security apparatus

[3] World Bank, World Development Report 2011: Conflict, Security and Development, page 12.
[4] World Bank, World Development Report 2011: Conflict, Security and Development, page 12.

- Fiscal gap and declining revenues
- Illicit economy
- Political transition

Addressing these vulnerabilities will be critical to build confidence in the state and strengthen institutional progress. While Afghanistan has experienced much institutional progress since 2001, much remains to be done to build robust institutions. Some institutions have become strong, but others remain weak. Economic growth and job creation will be critical as well as continued improvements in service delivery to build increasing confidence in government and state institutions.

Afghanistan is in the midst of several transitions in its efforts to gain self-sufficiency in the coming years, including security, financial, and political. These multiple transition processes add to the stresses of an already fragile state. By providing predictable and continuing support, the international community can be a decisive player in easing the key stresses in Afghanistan and in moving the spiral trajectory in a positive direction over time, accepting temporary setbacks as unavoidable in a maturing fragile state.

In this context of fragility, a strong government demanding programmatic approaches and having a solid focus on governance reform presents a positive opportunity for change. Government ownership is critical, especially within the area of corruption, which undermines government legitimacy and solidifies fragility.

The ARTF has had a strong focus on addressing drivers of fragility since inception in 2002. The RCW has helped ensure a stable flow of funding for core government expenditures, including civilian salaries, and maintain a certain degree of fiscal and macroeconomic stability. In light of the current fiscal situation, recurrent cost support will help to close the close fiscal deficit in the coming years and remain critical for macroeconomic stability.

The IW is equally critical in supporting fragility sensitive development. Large-scale national programs covering all 34 provinces of the country have been financed through the ARTF. This includes, among others, basic education, health, and the National Solidarity Program (NSP). The latter builds on strong community inclusion and has supported more than 50 million days in short-term labor. Both these funding windows are expected to play a key role in the National Unity Government's reform objectives of *realizing self-reliance*.

ii. Improving Governance and Building Government Capacity

In its *Realizing Self-Reliance* paper, the government has committed to "Building Better Governance" and identified strengthening government systems and technical capacity as key reform priorities. The ARTF has throughout the last decade been the major funding mechanism for efforts to strengthen institutions and establish sustainable capacity for the government's core operations.

When the ARTF was first established in 2002, it was primarily focused on providing a predictable flow of financing for the recurrent budget to ensure fiscal and social stability, and the necessary space for government to build institutions and develop its revenue basis. Recognizing the importance of building sustainable systems and government capacity, the World Bank started a public financial management project in 2002, with funding from the International Development Association (IDA), as its very first project in Afghanistan. The strength of a country's Public Financial Management (PFM) system is an important factor in establishing system credibility and is critical in determining the level of on-budget aid it can attract and effectively manage.

The PFM and Accountability Assessment (World Bank 2013) using the Public Expenditure and Financial Accountability (PEFA) approach highlights major and rapid improvements in the PFM system. Indeed, Afghanistan's performance in the PEFA assessment outshines scores of Fragile States as well as several Low Income Countries. These improvements in Afghanistan's PFM systems are an encouraging signal of the evolving strength of systems and capacity to maintain them.

Over time, and with the increased support of donors, the ARTF scaled up its financing for government's emerging priorities through the ARTF Investment Window, with a strong focus on capacity and institution building. This consists of two approaches: First, the ARTF is financing a set of programs specifically focusing on capacity; this currently includes a second phase of the public financial management program and the Capacity Building for Results (CBR) program. Second, all development projects financed by the ARTF, using different implementation models, include activities focusing on building the capacity of the implementing ministry/government agency to ensure sustainability. It is challenging to strike a balance between ensuring efficient and fast service delivery on the one hand and building sustainable capacity on the other hand.

Going forward, the ARTF will continue this approach, while also supporting a move towards programmatic approaches and strengthening governance reforms, focusing on capacity building and anti-corruption efforts.

Adaptation of Implementation Modalities: Reflecting constraints in capacity at provincial levels, insecurity and access throughout the country, ARTF projects have been implemented using different models ranging from implementation units established within a ministry (example: Ministry of Rural Rehabilitation and Development's NSP) to service delivery being contracted out with the ministry playing a role in contract management (example: Ministry of Public Health) to being fully integrated into the ministry structure and making use of existing capacity (example: Ministry of Education).

The decision to adopt different modalities arises from the realization that government capacity does not always allow for direct delivery of essential development services. One solution is to leverage government strengths in oversight and overall accountability with private sector capability for speedy delivery, including in hard-to-access areas. This has garnered tremendous results in service delivery in the past decade. In NSP and SEHAT (System Enhancement for Health Action in Transition) type models, the government takes supervisory and overall management role while nongovernmental organizations and private sector contractors deliver services. This approach leverages optimal institutional and functional responsibilities of both the government and contractors. Different implementation models have been introduced trying to balance the requirement for (medium to long term) capacity building and (short to medium term) critical service delivery. Hence, each implementation modality has its trade-offs in terms of capacity building and service delivery.

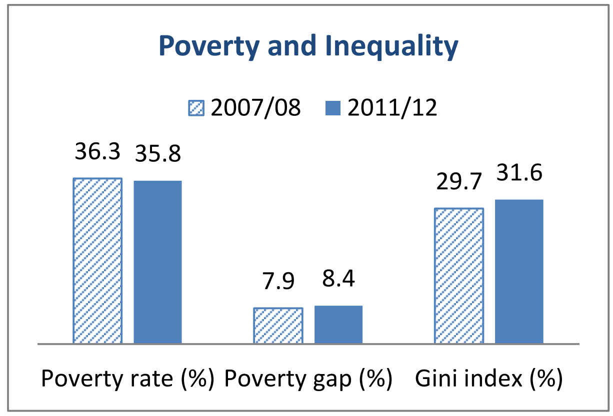
Strengthening Systems and Capacity through Projects: The London 2014 *Realizing Self-Reliance* paper also highlights the need for adopting new delivery models that will ensure greater sustainability and inclusion of marginalized groups. Most of the systems and capacity that has been built depend on the 'second civil service'—qualified staff paid by donor agencies and project funds. Technical staff are vital for the administration of systems such as PFM and delivery of development projects. The ARTF-funded CBR project aims to embed the 'second civil service' into civil service and strengthen its core and decrease reliance on external and sometimes 'parallel' structures. The effective implementation of CBR will not only strengthen capacity to operate government systems, it will also help improve service delivery through targeted reforms in essential public services.

The Incentive Program (IP) is another example of a program designed to support key economic policy reforms vital to system strengthening and capacity building. The IP supports reforms in PFM, investment climate and trade facilitation, governance, and revenue mobilization and has achieved significant policy reforms in the past six years of IP implementation. Under this upcoming Financing Strategy, the ARTF proposes to continue support for capacity and institution building in close cooperation with the government, which also recognizes the ARTF as an appropriate vehicle of systematic capacity building (Aid Management Policy, Ministry of Finance 2013).

iii. The Challenge of Persistent Poverty in Afghanistan

Despite robust growth in the years 2007-2011, poverty levels in Afghanistan have remained stagnant, recording the highest incidence in rural areas. The latest National Risk and Vulnerability Assessment (NRVA) data from 2011-2012 show that more than one-third (36 percent) of the population live below the national poverty line—a statistic that has remained the same since 2008. As population growth has continued to rise, an unchanged poverty rate translates into a higher number of people living in poverty. In addition to spatial disparities in poverty rates, inequality over time has also increased. Between 2008 and 2012, consumption of the richest 20 percent has grown faster than that of the poorest 40 percent. In raw numbers, about 600,000 more Afghans were living in poverty in 2012 than in 2008, and the country's 'poverty deficit'—defined as the amount of resources it would take, if perfectly targeted, to lift all families out of poverty—increased from $575 million (28.6 billion Afs) in 2008 to $993 million (47.4 billion Afs) in 2012.

FIGURE 1: Trends in Poverty

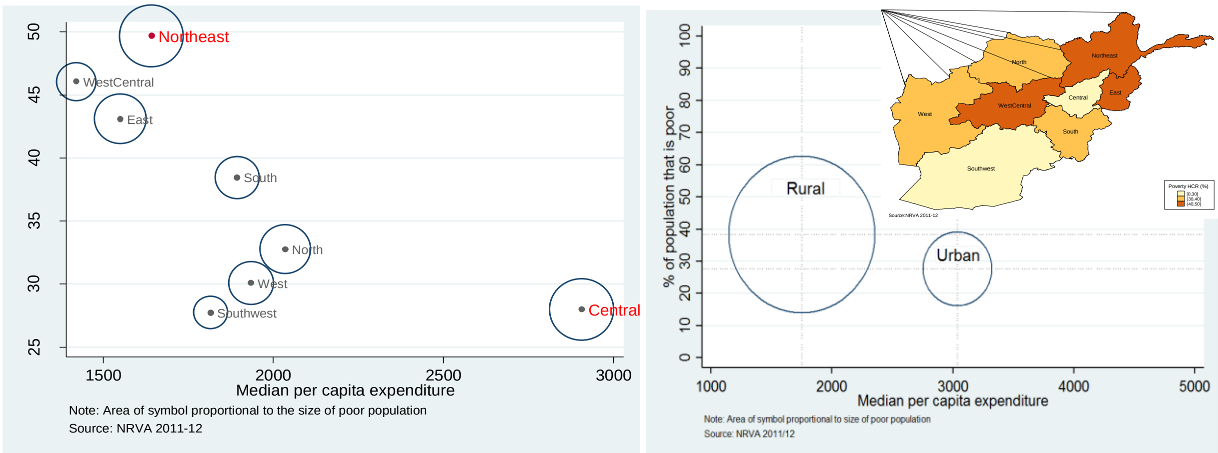


High levels of economic growth without corresponding declines in poverty levels indicate that the growth elasticity of poverty reduction (GEPR) in Afghanistan is very low. International evidence suggests that a country with the same level of development as Afghanistan should have a GEPR of about 1 percent. This means that, on average, for every percentage change in per capita consumption there should be a corresponding 1 percent decrease in the poverty rate. In Afghanistan, the GEPR is close to zero percent, meaning that the percentage decline in poverty is zero despite the country's rapid economic growth.

Disparities between urban and rural areas do not appear to be contributing to growing inequality. Afghanistan is largely a rural country with four out of five people living in these areas. Rural inhabitants tend to be poorer, with these areas having much higher poverty rates and lower levels of wellbeing than urban areas. Despite this, per capita consumption in rural areas is actually increasing faster than in urban areas—by 1 percent annually compared to only 0.3 percent annually, respectively. This suggests that economic growth is not exacerbating these inequalities. While urban-rural differences accounted for 23 percent of total inequality in 2008, they accounted for only 20 percent in 2012. In other words, living standards in urban and rural areas are converging, possibly as a result of the increased provision of health, education, and infrastructure to rural areas through aid.

Increased disparities in living standards between regions have contributed the most to growing inequality. As can be seen in Figure 2, poverty rates are highest and levels of wellbeing lowest in the Northeastern, West-Central, and Eastern regions. Furthermore, while regional disparities accounted for 15 percent of inequality in 2008, they accounted for 19 percent in 2012. One region in particular, the Northeast, seems to be hindering the impact of growth on the nation's average poverty reduction. Had the Northeast's economic growth and poverty reduction behaved as the rest of the country, national poverty levels would have fallen by 8 percent since 2008 and the GEPR would have been 0.7, in line with other countries with similar levels of development. Still, while it is true that lagging regions, like the Northeast, are falling further and further behind other regions, the inequality within regions has not dramatically changed. This suggests that regional disparities and not demographic disparities are contributing the most to the country's growing levels of inequality.

FIGURE 2: Urban vs Rural and Regional Disparities of Poverty, NRVA 2012



Gender and nutrition are two aspects of poverty that are particularly problematic as they affect the most vulnerable segments of the population—women and children. These two issues are therefore addressed as cross-cutting themes in the ARTF portfolio. Please refer to Boxes 1 and 2 for more details.

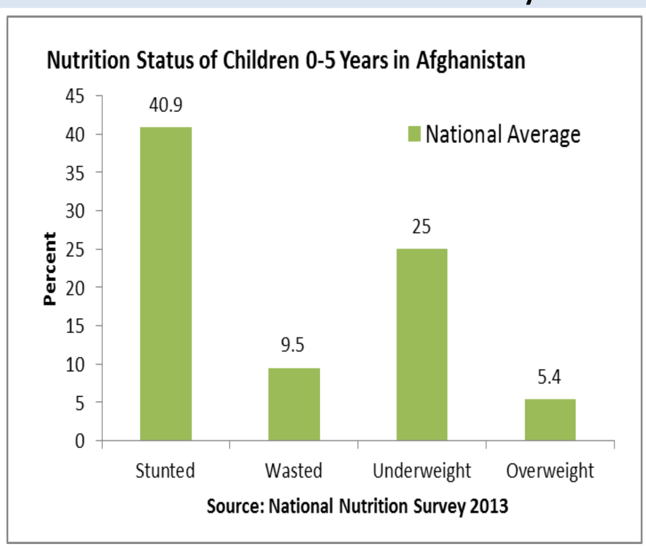
Findings from the Agriculture Sector Review of 2014 make this sector the most likely vehicle of poverty reduction in Afghanistan. With over 80 percent of the population and nearly 90 percent of the poor living in rural areas, the agriculture sector has the potential to foster job creation and economic growth and have a direct effect on income and consumption levels of the rural poor. Over the past decade, the ARTF Investment Window has channeled funds to large national programs such as the NSP, Education Quality Improvement Program (EQUIP), and SEHAT. While these projects have shown significant results, the link to poverty alleviation is long term. Further analytical work is needed to understand the drivers of poverty and inequality as well as to inform policies that are pro poor. The ARTF will continue aligning with findings from analytical work on poverty to ensure its impact on poverty levels is maximized.

BOX 1: Nutrition Status of Afghanistan

The latest National Nutrition Survey reports that at the national level, 40.9 percent children were stunted (low height-for-age) in 2013 (see Figure 3). Across the country, 9.5 percent children were wasted (low weight-for-height). Overall 25.0 percent children were underweight; 9.7 percent were severely underweight and 15.2 percent were moderately underweight. These statistics are among the worst in the world in child nutrition.

Stunting—an indicator of chronic malnutrition—levels in Afghanistan are among the highest in the world. This situation is of grave concern given that malnutrition between conception

FIGURE 3: Nutrition Status of Children 0-5 years



and 24 months of age can cause irreversible damage to health, growth, and cognitive development, leading to higher child mortality, lower IQ, lower school achievement, reduced adult productivity, and lower earnings. A key analysis by the International Food Policy Research Institute identified the following four determinants of nutritional status as the most critical in Afghanistan: (i) food security and the availability and accessibility of a diet of adequate nutritional quantity and quality; (ii) the mother's education level; (iii) women's status relative to men; and (iii) the health and water and sanitation environment.

The multidimensional nature of the causes of malnutrition in Afghanistan therefore underscores the diversity of actions that are needed across different sectors, ministries, and actors to address the problem. Multi-sectoral actions can strengthen nutritional outcomes in three main ways: (i) by accelerating action on determinants of under-nutrition; (ii) by integrating nutrition considerations into programs in other sectors, which may be substantially larger in scale; and (iii) by increasing 'policy coherence' through government-wide attention to policies or strategies and trade-offs, which may have positive or unintended negative consequences on nutrition.

These cross-sectoral actions are implemented through ARTF projects via a multi-sectoral nutrition engagement involving various projects and ministries. A new indicator on nutrition will be introduced in next year's ARTF Scorecard.

iv. Restoring Fiscal Sustainability and Economic Growth

The *Realizing Self-Reliance* paper highlights the need for sustained economic growth and fiscal sustainability, and, in particular, securing sustainable revenue generating sources and making efficient use of available aid. Afghanistan is still facing the effects of the fiscal crisis of 2014. Domestic revenues fell to 8.7 percent of GDP (projected) in 2014 from 9.7 percent in 2013, itself down from a peak of 11.6 percent in 2011. In 2014, despite austerity measures, the government ran down its cash balances and incurred arrears on operations and maintenance (O&M) and discretionary development spending, resulting in a fiscal deficit of over $500 million.

Extraordinary expenditure needs, weak revenues, and a decline in donor aid also present a daunting medium-term challenge for fiscal sustainability. Afghanistan faces extraordinary expenditure needs in the areas of security, service delivery, infrastructure development, and O&M. Furthermore, economic activity and jobs are still highly reliant on government spending and off-budget donor assistance. On the other hand, domestic revenue mobilization has weakened in recent years and total foreign aid is projected to decline as a share of GDP over time. Going forward, total government spending and off-budget donor spending is projected to decline from 55 percent of GDP in 2013 to 40 percent in 2018.

In order to confront these challenges, Afghanistan will need to pursue a three-pronged strategy to restore fiscal stability going forward: (i) improve revenue mobilization; (ii) secure a predictable flow of donor assistance; and (iii) prioritize, safeguard, and enhance efficiency of civilian operating and development spending.

The ARTF supports revenue mobilization through the Incentive Program, an incentive-based policy reform program, where key benchmarks in the past have focused on areas such as reforms of public financial management, governance, investment climate and trade facilitation. To support a predictable flow of financing, the ARTF plays a direct role in helping secure predictable and on-budget aid. Since the ARTF was first established in 2002 it has provided critical financing for government's civilian recurrent expenditures through the Recurrent Cost Window. This financing has in recent years been scaled up to include the Incentive Program and the Operations & Maintenance Facility, which encourages increased funding for operations and maintenance. However, it would be critical to prioritize and safeguard civilian operating and development spending. To this end the ARTF is financing the Public Financial Management Reforms project (PFMR II) and will finance a third phase of this under the new FS. Also, the Capacity Building for Results program is key to continue developing strong institutions to enhance efficiency of on-budget expenditures.

Going forward, it would be critical to carefully balance the financing available under the ARTF between recurrent costs and government's development priorities. While recognizing the severity and continuity of the government's fiscal gap, the ARTF should continue its support for development financing in support of service delivery, economic growth, and capacity building.

BOX 2: Progress towards Gender Equality in Afghanistan

The ARTF Gender Approach: The ARTF gender approach is fully aligned with the government's strategy as outlined in the *Realizing Self-Reliance* paper. The World Bank strategy, reconfirmed in the 2013 *Gender Stock-Taking Report*, is to ensure **gender mainstreaming** across all relevant projects. The ARTF has a clear focus on achieving significant gender outcomes through diagnostics, implementation, and monitoring and evaluation (M&E). All relevant projects have gender assessment/gender strategy, gender indicators, and gender benchmarks. In addition, the ARTF is looking to allocate dedicated funds to increase gender relevant data collection and analysis, e.g., with a focus on the Central Statistics Organization.

A Snapshot of Challenges Affecting Women's Welfare in Afghanistan: The status and lives of women have improved considerably over the past 12 years in Afghanistan. Progress, in terms of increased access to resources, participation in economic and income generating activities, and decision making from household to national political level, however, remains mixed. Mobility constraints worsened by insecurity; inadequate female human resources (i.e., female teachers, female health workers); and geographic disparities between urban and rural areas and within regions are some of the main constraints inhibiting further improvements in the welfare of women.

Table 2: Overview of Some Constraints in Improving Gender Equity in Key Services Sectors

Challenges in Health and Education	Challenges in Economic Participation	Challenges in Access to Justice and Political Voice

- Lack of qualified human resources (4.8 professionals/10,000 people, of which even fewer are women) - Low nutritional status - High maternal mortality - High fertility rates - Low female literacy and low gender parity - High drop-out rates in secondary school - Inadequate access to schools - Shortage of female teachers (41% of districts have no certified female teachers) - Low female participation in tertiary education	- Widespread unpaid and vulnerable employment (about 25% of working women are paid) - Urban underemployment (19% of urban female workforce are employed, compared to 79% of male) - Lack of women in government jobs, particularly in managerial roles) - Challenges of workplace harassment/power dynamics	- High levels of violence against women (an estimated 87% experience some kind of abuse, 62% at home) and widespread hesitancy to report - Lack of female personnel in the legal system and general lack of representation - Pluralistic legal system (including informal systems) providing uneven protections - Security and threats toward women voters and candidates; fraudulent use of female votes - Few women in appointed posts - Lack of mobility, time and active participation for women in community-based bodies.

Addressing Challenges through Programmatic Support: Safeguarding and improving gender outcomes are crucial to the development objectives of ARTF and critical to Afghanistan's overall development. The ARTF will continue to prioritize, through its projects and policy discussions with government and donors, gender parity in human capital, reduction of gender gaps in earning and economic productivity, and most importantly it will help shrink gender differences in voice within Afghan society.

New Gender Commitments across the World Bank Group: The World Bank Group has incorporated new gender indicators and targets to its 2014 WBG Corporate Scorecard. These new commitments at the corporate level, which will also apply to ARTF projects, will deepen integration of gender considerations into country strategies and improve accountability, monitoring, and quality of delivery of gender outcomes. Gender integration will be done through analysis of gender issues at various levels, targeted actions to bring about improvements, and monitoring and evaluations of interventions.

The new gender commitments, and the ARTF's overall focus on gender across its portfolio, will further strengthen government's reform priority to ensure citizen development and empowering women as outlined in the *Realizing Self-Reliance* reform paper.

The ARTF Administrator will continue working with the Gender Working Group to discuss constraints and opportunities to gender equality in Afghanistan and ensure donors can share best practices and experiences with Government and the World Bank to inform ongoing and future ARTF activities.

III. STRATEGIC AND OPERATIONAL RISKS

Overall, the risks to the ARTF, the projects and operations funded by the ARTF and their expected outcomes are considered high. This section outlines the key principles of ARTF Risk Management and the most important risk areas and mitigation measures. Recognizing that Afghanistan presents a high risk and continuously evolving context, risks are being monitored on a continuous basis. While the broad parameters are outlined, mitigation measures continue to evolve in response to a changing context and in consultation with government and donors.

The ARTF's approach to risk management builds on the World Bank's Framework for Operations Risk Management (FORM) and is organized along similar lines to the ARTF monitoring framework where risk mitigation and monitoring is structured in accordance with key risks. The ARTF Risk Management Framework is organized on two levels: (i) trust fund level; and (ii) project level.

i. The World Bank's Operations Risk Management

In the World Bank risk framework, risks are defined as "*risks to the client's achieving the expected results of the project, program, or strategy; and the risks of unintended impacts.*" The World Bank's Framework for Operations Risk Management rests on three pillars: (i) standardized systems and tools; (ii) an institutional structure and policies that support proactive risk management; and (iii) a culture of informed risk-taking.

The standardized systems and tools establish a unified and standardized risk rating tool that integrates information systems and links results to risks—the Standardized Operations Risk-Rating Tool (SORT). SORT contains a risk category matrix, rates risks at the country and project levels, and assesses risk throughout the life of project. Annex III has a detailed SORT risk framework for the ARTF.

SORT helps the Bank as the ARTF Administrator assess and monitor risks consistently both at the trust fund and project levels. At the portfolio level, the data collected through SORT are used to create portfolio reports that help the Bank define its tolerance and appetite for various risks. Thus, SORT provides the project-level foundation for portfolio-level risk management.

ii. Risk Management at the Trust Fund Level

While Annex III outlines the ARTF SORT, including specific risks and risk management approaches, at the trust fund level, the following describes some main principles for how the World Bank, as the ARTF Administrator, manages risks:

- **Partnership and communication:** ARTF risk management is primarily carried out by the World Bank as the ARTF Administrator but is done in close collaboration with government and donors through the ARTF governance structure. The institutional mechanisms provided by the ARTF governance structure allows for candid and open dialogue on risks to the ARTF and on mitigation measures.
- **Flexible approach:** Due to the relative volatility of the context in which the ARTF operates, the risk mitigation framework cannot be overly prescriptive. It outlines instead through SORT the broad

principles and the main measures to mitigate risk along a number of critical parameters while leaving room for adaptation in response to a changing environment.

- **Continuous monitoring:** Continuous monitoring of risks includes collecting information, assessment, and judgment regarding both new and ongoing risks. The ARTF Administrator works with its technical teams, government, and its development partners to understand the risks of the environment.

iii. Risk Management at the Project Level

ARTF risk management at the project level is based on the World Bank's FORM and makes use of SORT to carry out risk analysis linked to results management. Also, it is organized around the ARTF monitoring framework to ensure weaknesses, highlighted in the risk assessment, are addressed and mitigated to the extent possible in the monitoring framework. SORT looks at the following areas and rates the risk for each of those, after which an overall project risk rating is then generated: Political and Governance; Macroeconomics; Sector strategies and policies; Technical design of project/program; Institutional capacity for implementation and sustainability; Fiduciary; Environment and Social; Stakeholders; and Others.

SORT is initiated during the design process of each individual ARTF project and updated throughout the implementation process. Risk ratings of individual ARTF projects are made available to government and donors in the biannual Implementation Status and Results reports that are published for each project in the portfolio.

Fiduciary risks are monitored and carefully managed for all ARTF projects. The World Bank employs a systematic approach, based on its public financial management system, to minimize a project's fiduciary risk. This is done in two stages—project preparation and supervision phases:

- During the preparation stage, the focus is on assessment of the implementing agency to identify/evaluate risks and to mitigate them through design of appropriate fiduciary and oversight arrangements to reduce opportunity for loss and enhanced transparency.
- During the implementation stage, continuous assessment of fiduciary assessments by the World Bank is done to ensure they are operating effectively as originally designed and to identify any need for change.

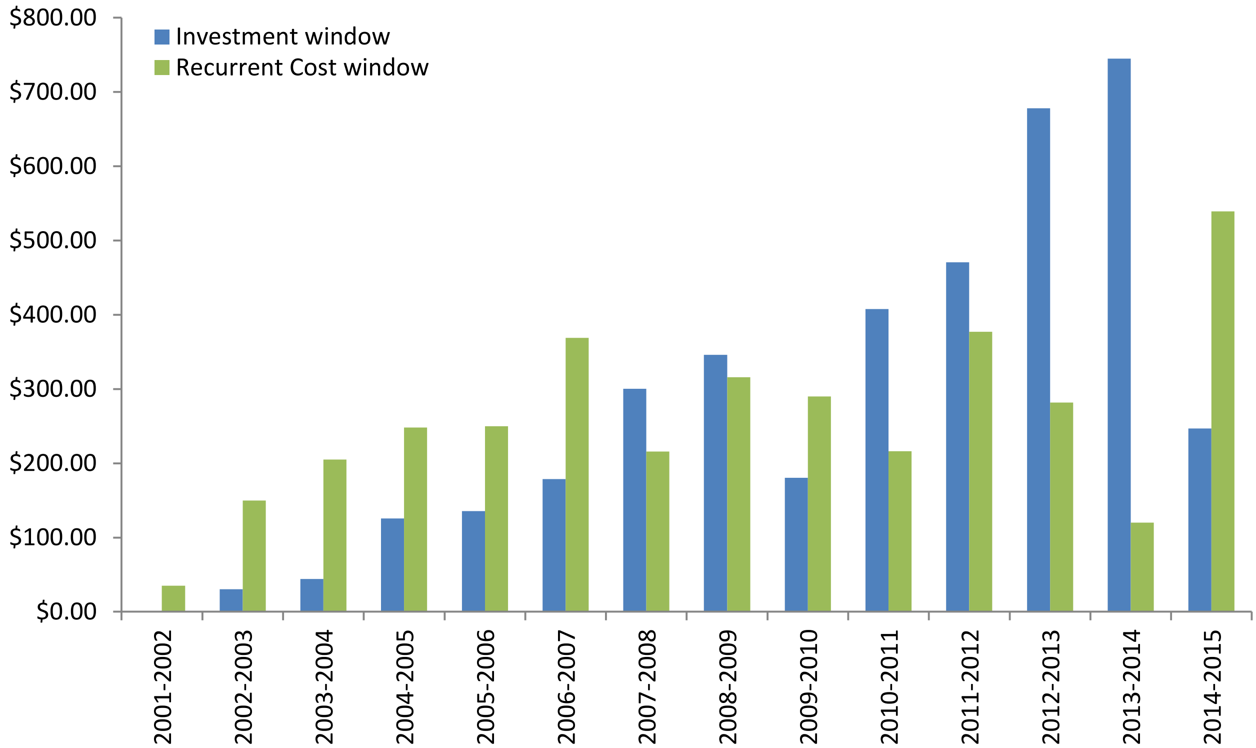
IV. FINANCIAL FRAMEWORK AND PRIORITIZATION OF FUNDING FOR THE FINANCING STRATEGY FY1394-1396

The following section outlines the financial status of the ARTF, providing an overview of the funds available and funds anticipated over the coming three years. The financial framework provides critical information to inform the prioritization of financing and thus helps government, donors, and the ARTF Administrator agree on a pipeline for the coming three years, FY1394-1396. The financial framework ensures full transparency on the available ARTF funding envelope and allows government strong ownership in the planning and prioritization of ARTF resources.

i. Historical Funding for Recurrent Cost Window and Investment Window

In the first years after the ARTF was established in 2002 it focused mainly on recurrent cost support to ensure predictable and transparent operating budget support, funding the non-security wage bill, and operations and maintenance. This is the Recurrent Cost Window. The financing for development projects through the Investment Window scaled up slowly over time as donors increased their support for the ARTF. Only in 2007 did the IW overtake the RCW in new commitments made. At the time, it was expected that government's need for recurrent cost support would diminsh over time as its revenue increased. However, this expected trajectory did not materialize as the government's expenditures increased in parallel. Figure 4 shows annual ARTF commitments for the RCW and IW since 2002.

FIGURE 4: ARTF Recurrent and Investment Financing, 2002-2014 (million $)

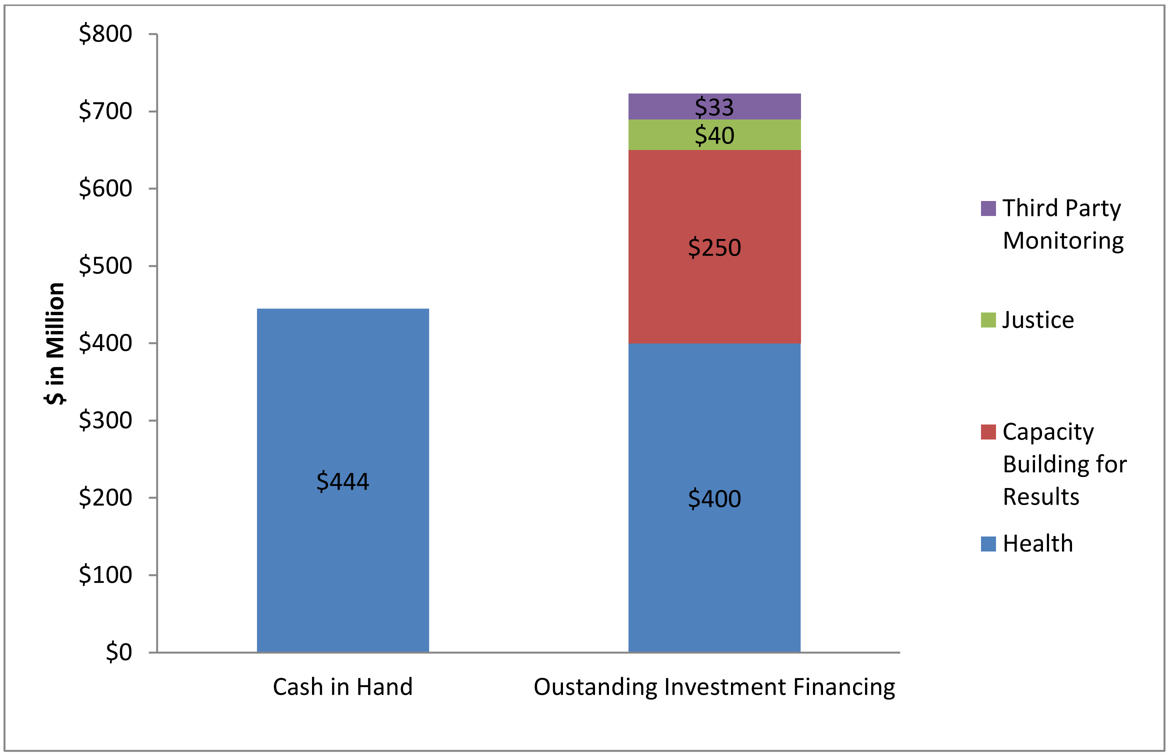


ii. Current Cash Balance and Commitments

Currently, $928 million is committed under legal agreements between the ARTF and government to ensure active investment projects continue implementing, including in agriculture, infrastructure, rural roads, health, and education sectors. These ongoing projects have been assessed and the potential for freeing up funds has been analyzed. Moreover, the Administrator carried out a detailed portfolio review and identified projects with potential for cancellation of funds in 2014. Funds were cancelled under two projects (Rural Enterprise Development and On Farm Water Management) while a third project (Justice Service Delivery Project II) will be discussed with the new government.

The ARTF currently has $444 million in cash against total outstanding commitments amounting to $723 million under the Investment Window. Committing more funds for ongoing projects than what is available in ready cash is standard practice for prudent cash management under the ARTF. This approach has been used since the ARTF was established to ensure funds are used efficiently for projects in immediate need rather than being tied up in large projects for 4+ years before disbursement to the end beneficiaries. Figure 5 shows the size of current ARTF cash in hand relative to outstanding hard commitments.

FIGURE 5: Cash Balance vs. Outstanding Financing Commitments (million $)

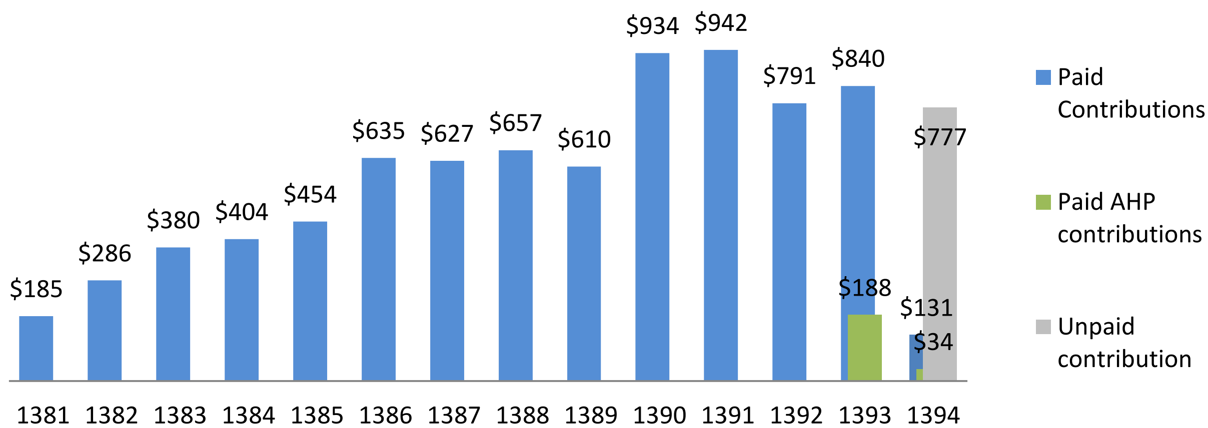


This leaves, in fact, an ARTF financing need of $723 million in outstanding *legal* commitments for the Investment Window carried over from previous years. This has to be covered by the ARTF available cash in hand ($444 million) and expected incoming donor contribution. These commitments will have to be financed during the coming three-year period alongside new projects.

iii. Donor Financing

ARTF donor contributions increased from $184 million when the ARTF was established in 2002 to approximately $1.03 billion (including AHP of $188.17 million) per year during 2013-2014. Following the Tokyo Conference of July 2012, donors committed to contribute $4 billion annually for development with 50 percent on-budget and 80 percent aligned with government priorities. Several donors indicated that their ARTF contributions were expected to increase as part of their Tokyo commitments. Donor contributions have, however, not increased. Instead we have seen a small reduction in donor contributions to approximately $800 million per year.[5] Figure 6 shows donor contributions from FY1381-1394 (2002-2015).

FIGURE 6: ARTF Donor Contributions 1381-1394 (million $)



Note: The Tokyo Conference took place in 1391 (July 2012). Donor contributions for FY1394 are projected based on donor pledges and discussions with donors.

Few donors have so far expressed their pledges for FY1394-1396—so far, only $1,245 million have been pledged, including multi-year signed/unsigned pledges. The Administrator strongly encourages donors to provide this essential information to ensure predictability in financing to inform the planning process and the FS. The risk of lack of information on donor contributions is not new and has been managed carefully by the government and ARTF Administrator to ensure supply and demand are balanced. Please see more details in Annex III on ARTF risk mitigation.

In the absence of information on pledges, the Administrator has to make assumptions. Based on discussions with donors and an expectation that donors will provide funding at 1393 levels for FY1394-1396, the Administrator is expecting levels of financing around $800 million per year. This would provide approximately $2.4 billion to finance recurrent cost and new pipeline investment programs over this period. Adding to this the cash in hand of $444 million carried over from 1393, the expected envelop for FY1394-1396 is estimated at approximately $2.8 billion. As explained above, the ARTF has outstanding commitments for ongoing projects for a total of $723 million. This therefore means that the **ARTF has a total available cash balance of approximately $2 billion for the proposed FS FY1394-1396** to cover both recurrent cost financing and new investment projects.

[5] This excludes AHP financing, which is not considered to support the core program outlined in the ARTF Financing Strategy.

TABLE 5: Projected Cash Flow FY1394-1396 (million $)

Sources/Uses of Funds	1394-1396 cash flow (m $)
Sources of Funds:	
Cash as of April 15, 2015	444
Total additional donor funds expected	2269[6]
Total:	**2713**
Uses of Funds:	
IW Outstanding Commitments	723
Total:	**723**
Total available financing	**1990**

KEY POINT: Assuming donor pledges hold steady at $800 million a year, approximately $2 billion are available for recurrent cost financing and new projects in the FY1394-1396 Financing Strategy.

While the reduction in donor financing does not seem enormous, from previous levels of around $950 million in 2012 to current expectations for the coming years of around $800 million, two factors greatly impact how much funding is available for new investment priorities in the coming FS period:

1. The RCW was scaled up from approximately $300 million annually to $400 million annually with the introduction of the O&M Facility. Since donor financing did not increase to absorb this upsurge, in effect, this means that $100 million per year is reduced from the available envelope for investment projects.
2. At the same time, more ARTF financing is tied to large-scale core service delivery than previously the case. One example is basic health—while the ARTF provided a total of $46 million to the previous phase of basic health, it is providing a total of $518 million for the current phase as the whole program (covering all 34 provinces) has been consolidated under the ARTF. This means that significant ARTF funding is absorbed and less financing is available for other projects in the pipeline.

V. ARTF FINANCING PRIORITIES AND PIPELINE FY1394-1396

i. Recurrent Cost Window

The ARTF Board paper of 2002 established the intention to continue scaling down recurrent cost support over time to ensure a sustainable trajectory and a strong incentive for government to increase its revenues. As can be seen in Figure 7, the ARTF's recurrent cost support has not been scaled down or

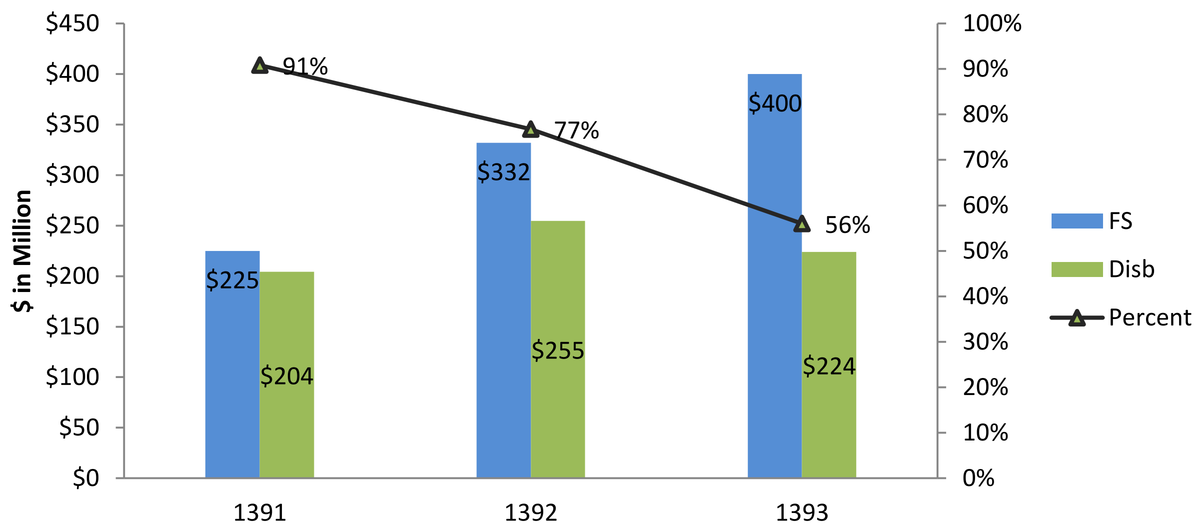
[6] $2,400 million were expected for the full FY1394-1396 period. However, as of April 15, 2015, $131 million had already been received, leaving the remaining donor funds to be received at $2,269 million.

phased out. Rather, an increasing share of the funds channeled through the RCW has been made available to government through incentive-based mechanisms including the Incentive Program and the O&M Facility.

The increase in the overall size of the RCW by scaling up the Incentive Program and introducing the new O&M Facility to support government's O&M spending was made on request of the government and donors as donor-financed infrastructure came on budget. Given the expectation that donors would continue financing around the 2012-level of $950 million annually, as well as the country's continued high financing needs, difficulties in mobilizing revenue and the benefits of direct budget support for aid effectiveness, the anticipated scale down of the RCW was therefore postponed.

As a consequence, the size of the recurrent cost support made available to government increased to an annual level of $400 million in FY1393. As shown in Figure 7, there is a difference in the funds made available to government under the RCW and what is finally disbursed. This is a result of the Incentive Program design that, while making funds available to government, only disburses what is earned, based on progress on agreed policy reform benchmarks.

FIGURE 7: ARTF RCW Incentive Program—Funds Made Available in FS vs Disbursements to Government, 2012-2014



In FY 1393, the government faced a significant fiscal crisis. The ARTF supported the fiscal gap through the planned recurrent cost financing as well as special funds paid by donors through the Ad Hoc Payments mechanism. Fiscal pressures will continue in 1394. **The Administrator proposes to continue recurrent cost support of $400 million per year** in order not to exacerbate this crisis, during a vulnerable time for a new government, and to allow the O&M Facility to continue**.** This will require revisiting previous agreements on ARTF principles (i.e., downward trajectory for recurrent cost financing).

ii. Investment Window

In response to the challenging fiscal situation, government is expected to put in place austerity measures including a reduction in discretionary development spending. This could have significant impact on long-term development and critical service delivery in Afghanistan. Reducing the ARTF's investment financing, tied to core development priorities, could seriously compromise development outcomes in Afghanistan, a key risk to combating fragility and conflict. If insufficient funding is available for investment financing, Afghanistan will lack:

- Economic growth and poverty reduction (infrastructure, agriculture, energy, mining, education, etc.);
- Service delivery (health, education, etc.);
- Capacity and institution building (civil service reform, public financial management, etc.).

The Pipeline: Based on the previous Financing Strategy and ongoing discussions with government, the ARTF has a number of new projects already in the pipeline. Some of the projects in the pipeline are carried over from the previous Financing Strategy. These were delayed as a result of the prolonged election process. **The current pipeline of new projects totals $1.6 billion**. Please refer to Annex I for a full overview of potential projects for the pipeline.

Since insufficient funds are available to cover this pipeline in full, projects will have to be significantly reduced and it will be difficult for the ARTF to engage in new sectors without new funding. The pipeline projects are projects planned under the IW at government's request. Projects in the pipeline are currently under preparation or have been requested/prioritized by government, but not yet committed in legal agreements between government and the World Bank as the ARTF Administrator. There is therefore flexibility on the pipeline and it will be up for discussion as part of the FS discussions and the broader prioritization discussion with government.

Some projects were already agreed in the Interim Arrangement for a total of $269 million for FY1394: (i) Higher Education ($50 million); (ii) On Farm Water Management Additional Financing ($45 million); (iii) Irrigation Rehabilitation and Development Additional Financing ($70 million); (iv) Public Financial Management Reform III ($75 million); and (v) Third Party Monitoring ($29 million). Please refer to Annex VII for more details.

It is critical to note that, as in previous years, donor preferencing is not allowed to drive fund allocations. Prioritization of funds is instead based entirely on discussions with government to ensure alignment with their core priorities and overall strategy.

iii. Balancing the RCW and IW

The proposed balance between the IW and RCW ($400 million/$400 million) is rooted in the ARTF's history and has evolved in response to the circumstances and government and donor demand. In the early years, RCW funding dominated the ARTF. This was required at the time as government had very little revenue of its own and ARTF contributions to the budget assumed a large share of government's overall civilian operational cost. As government revenue increased[7] and its ability to cover its operational costs improved, donors and government expressed a desire to balance ARTF funds more strongly towards investments. This structural shift in balance was supported by an overall increase in ARTF contributions. Moreover, donors and government agreed that RCW funds should be increasingly shifted from baseline financing into the IP to support structural policy reforms in support of fiscal sustainability.

The ARTF no longer sees an increase in contributions. Given the temporary nature and the fluctuations of the government's annual fiscal deficit and the limited amount which the ARTF could potentially contribute towards meeting the fiscal gap, the question of balance within the FS is more one of determining the potential benefits towards meeting the ARTF's medium- and long-term objectives within both the RCW and IW. While the ARTF should support government's operating budget, it is also critical that sufficient funding remains to support and safeguard investments in sustainable development.

In 1393, the redirecting of funds from core donor pledges towards the Ad Hoc Payments mechanism undermined the Administrator's ability to support the priorities as outlined in the FS. This new FS therefore agrees that only new money should go towards the AHP. However, the Administrator wants to emphasize that this is dependent on the cooperation of individual donors as they decide if/how to use the AHP.

iv. Summary and Proposal

Considering a reduction in the available donor financing envelope from around $950 million in 2011-2012, when the IP was scaled up and the O&M Facility introduced, to current estimations for the coming three years of approximately $800 million per year, the new ARTF FS 1394-1396 will have to be rebalanced. The FS will have to ensure sufficient recurrent cost support for the new government in support of its current fiscal crisis, while at the same time ensuring critical support for core development results through investment projects.

To ensure the ARTF continues substantial recurrent cost support in the coming year (1394), the Administrator proposes to continue the current level of recurrent cost financing of $400 million per year. Keeping the level of recurrent financing stable this first year would allow the new government time to reform and increase its own revenues in support of fiscal sustainability, while also safeguarding funds for core development activities.

With an overall financing envelope of approximately $2.8 billion (see Table 5 on page 21 and Table 6), outstanding commitments of $723 million, and recurrent cost support of $1.2 billion, **the ARTF will have only $765 million for the three years, or some $255 million per year, for new investment projects under the new FS 1394-1396**.

[7] Even though RCW funds increased consistently over the past decade, they only covered between 6.5 percent and 9.5 percent of the government's operational budget in the past three years.

TABLE 6: ARTF Financing 1394-1396

ARTF Window	1394 (m$)	1395 (m$)	1396 (m$)	Total
Investment Window: existing commitments, including Third Party Monitoring	225	229	269	723
Investment Window: new pipeline projects (prioritization TBD for outer years 1395 and 1396)	285	429	204	918[8]
Recurrent Cost, including baseline, IP and O&M	400	400	400	1200
Research and Analysis Program	1	2	3	6
AHP	TBD	TBD	TBD	TBD
Total	**$911 million**	**$1060 million**	**$876 million**	**$2.9billion**

KEY POINT: Once funds are allocated for existing commitments and recurrent costs, there is a total of $765 million available to finance new pipeline projects over the next three years. The $918 million for the new IW pipeline includes the $765 million available for the IW over the three-year period plus 30 percent overprogramming for the outer years 1395-1396.

Projecting $400 million per year in the RWC and some $255 million per year for the Investment Window, the proposed allocations are as follows:

For the Recurrent Cost Window, the Administrator proposes the structure outlined in Table 7. Some key points:

1. Baseline financing in 1394 starts out at the 1393 level of $125 million and then continues its downward trajectory in the following two years, 1395 and 1396.
2. A new Incentive Program is required to be in place by June/July 2015.
3. The O&M Facility will be rolled into the IP and remain at previous levels of $100 million, hence the increased size of the IP.

[8] The $918 million includes the $765 million available for IW financing plus 30 percent overprogramming for the outer years FY1395-1396.

TABLE 7: Recurrent Cost Window Structure 1394-1396

	1394 (m $)	1395 (m $)	1396 (m $)	Total (m $)
Baseline	125	100	75	300
Incentive Program	275	300	325	900
Total	400	400	400	1200

For the Investment Window, the Administrator proposes a pipeline of investment projects as outlined in Table 8 to prioritize the allocation of the estimated $765 million over the three years. The proposed prioritized pipeline totals $918 million, which is more than the available $765 million. The $918 million, however, includes overprogramming of about 30 percent for the outer years (1395-1396).[9] Considering the risk of delay or cancellation in fragile and conflict-affected situations, the 30 percent overprogramming has proven to be a prudent measure of portfolio and results planning.

To allow government time to develop its strategy and assess core development priorities for the coming years, it has been agreed that the new FS will provide certainty on the pipeline for FY1394, while the list of funding priorities for the outer years, FY1395-1396, will remain indicative. The pipeline for the outer years will be agreed and documented, including review of the overprogramming, in the FY1395 and FY1396 Update to the FS respectively, the former to be finalized by December 2015.

TABLE 8: ARTF Proposed Pipeline

Sector	Project in Pipeline	1394	1395 *(indicative)*	1396 *(indicative)*	Alignment w. ***Realizing Self-Reliance*** Paper
Governance	PFM	***75***			• Building Better Governance • Restoring Fiscal Sustainability • Tackling Underlying Drivers of Corruption
Human Development	Basic Education*		100		• Ensuring Citizen Development Rights
	Higher Education	***50***			• Ensuring Citizen Development Rights • Bolstering Private Sector Confidence, Ensuring Growth, and Creating Jobs
Agriculture	Irrigation Rehabilitation	***70***			• Bolstering Private Sector Confidence, Ensuring

[9] The available financing envelope of $765 million is split into three portions ($255 million), one for each of the fiscal years, and 30 percent ($153 million) is taken off the total of 1395 and 1396 and added to the $765 million. This equals a total envelope of $918 million available for programming.

	and Development				Growth, and Creating Jobs
	On Farm Water Management AF	***45***			• Bolstering Private Sector Confidence, Ensuring Growth, and Creating Jobs
	New agriculture program incl. grain reserves			100	• Bolstering Private Sector Confidence, Ensuring Growth, and Creating Jobs
Rural Development	NSP IV**		200		• Ensuring Citizen Development Rights • Bolstering Private Sector Confidence, Ensuring Growth, and Creating Jobs
	Rural Access Roads AF***			100	• Ensuring Citizen Development Rights • Bolstering Private Sector Confidence, Ensuring Growth, and Creating Jobs
	Rural Livelihoods Project		50		• Ensuring Citizen Development Rights • Bolstering Private Sector Confidence, Ensuring Growth, and Creating Jobs
Social Development	Land Management Support	30			• Ensuring Citizen Development Rights • Bolstering Private Sector Confidence, Ensuring Growth, and Creating Jobs
Infrastructure	DABS TA		5		• Bolstering Private Sector Confidence, Ensuring Growth, and Creating Jobs
	Power System Development AF	13			• Bolstering Private Sector Confidence, Ensuring Growth, and Creating Jobs

	Naghlu Hydropower Rehabilitation		70		• Bolstering Private Sector Confidence, Ensuring Growth, and Creating Jobs
Technical Assistance	TA Project	2	4	4	• Building Better Governance
Total		**285**	**429**	**204**	**918**[10]

*Note: (i) Figures marked in bold italics have been outlined and approved in the ARTF Interim Arrangement; (ii) *The full value of the next phase of primary education is tentatively set at $200 million with a first tranche of $200 million to be released in 1396; (iii)**The full value of the next phase of NSP (title TBD) is tentatively set at $400 million with a first tranche of $200 million to be released in 1395; (iv) ***AF is acronym for Additional Financing.*

v. Programmatic Approaches

Going forward the ARTF will endeavor to support programmatic approaches in line with a government-led strategy. The ARTF is already funding some programmatic approaches, including health and primary education, but will make a push to explore, with government in the lead, how to move further in this direction. As proposed by President Ghani, agriculture lends itself as a pilot area—a thorough review has already taken place to inform a programmatic approach and donors agree that agriculture is fundamental to Afghanistan's economic development and are keen to pool resources in support of an aligned approach.

In many respects ARTF project mechanisms have already evolved to align well with programmatic approaches, including, for instance, full alignment with government priorities (laid out in the National Priority Programs and in the presently emerging priorities from the *Realizing Self-Reliance* paper), the use of government budget structures, results monitoring and reporting systems. Table 9 outlines main funding areas of the ARTF and their respective progress and envisioned next steps on the way towards programmatic approaches.

TABLE 9: Programmatic Approaches

Sector	Current ARTF Support	Planned Projects	Status
Governance Reform	PFMR II, CBR and IP	PFMR III	Programmatic approach established within ARTF: Governance, already a programmatic approach as a strategy, has been formed around a multi-faceted approach supported by programs pooling donor funds. PFMR II and CBR are both based on NPPs.

[10] The $918 million reflects the $765 million available for IW financing plus 30 percent overprogramming for the outer years FY1395-1396.

Education	EQUIP II, NATEJA (skills development)	Higher Education	Programmatic approach established within ARTF: EQUIP II constitutes a programmatic approach to education; it is nationwide and covers a wide spectrum of activities all critical to primary education. EQUIP is supporting the majority of activities outlined in the government's NPP for primary education.
Health	SEHAT		Programmatic approach established within ARTF: SEHAT constitutes a programmatic approach to health; it is nationwide and covers a wide spectrum of activities all critical to primary health care and is centered on a sector-wide dialogue. SEHAT is supporting the majority of activities outlined in the government's NPP within the area of primary health care.
Agriculture	NHLP, AIP, IRDP, and OFWM	IRDP and OFWM AF, proposed new agriculture program	Potential area for programmatic approach: A government-led programmatic approach should be developed for agriculture and ensure donor alignment. A new programmatic approach can be informed by the recent Agriculture Sector Review. The ARTF will work with government to ensure alignment with this new approach.
Rural Development	NSP III, ARAP	NSP IV	Potential area for programmatic approach: A government-led programmatic approach should be developed for rural development and ensure donor alignment. The new government has already initiated discussions, led by MRRD, on a new programmatic approach for rural development projects, implemented by/centered on MRRD. The ARTF will work with government to ensure alignment with this new approach.

vi. Third Party Monitoring

The ARTF is contracting two third party monitoring agents to ensure an additional layer of oversight is in place for the large ARTF portfolio. The ARTF will continue contracting these monitoring agents in the next FS period:

a. **The ARTF Monitoring Agent (MA) for the Recurrent Cost Window:** The MA is an accounting firm that ensures the fiduciary integrity of the recurrent cost financing channeled to government under the ARTF. The MA:
   - Monitors the entire civilian operating budget for eligibility;
   - Performs automated desk review of 100 percent of recurrent cost expenditures;
   - Performs risk-based review of expenditures, including visits to provinces.

b. **The ARTF Supervisory Agent (SA) for the Investment Window:** The SA carries out asset verification, quality assurance, and data mapping of ARTF-financed national infrastructure projects (NSP, rural roads, education and irrigation). The SA:
   - Uses smart phones, satellite imagery and innovative technology to provide ministries and the ARTF with enhanced outreach to all 34 provinces of Afghanistan, including highly insecure areas, to obtain data from key national programs;
   - Helps build capacity within ministries by 'raising the bar' on monitoring and reporting standards;
   - Provides government, the ARTF and donors with a credible system of data collection and verification that contributes to effective policy making.

BOX 3: Monitoring Results

1. The ARTF Monitoring Agent has monitored 100 percent of the government civilian operating budget on an annual basis since 2002.
2. The ARTF Supervisory Agent has:
   a. Conducted a total of 11,239 site visits since the program start in 2011;
   b. Visited project sites in all 34 provinces of Afghanistan;
   c. Monitored four projects worth a total of $2.25 billion;
   d. Focused on infrastructure quality and safeguard issues in education, rural roads, irrigation, and community development;
   e. Trained and deployed 47 local monitors to monitor construction under school and irrigation projects ensuring community engagement and live feedback to ministries;
   f. Completed a two-year training program at the Ministry of Education developing skills for local and community monitors to be able to assess infrastructure quality and transmit information back to the ministry.

iv. The next ARTF Incentive Program

Uncertainty surrounding the political and security transition has had a greater than anticipated impact on the economy and the pace of reforms. Economic growth has fallen sharply and Afghanistan faces a deteriorating fiscal crisis, with declining revenues leading to an unfinanced fiscal gap, depleted cash reserves, and accumulating arrears. In this context, the new Government of Afghanistan has pledged to reinvigorate the pace of reforms. The government's *Realizing Self-Reliance* paper that was launched at the London Conference in December 2014 outlined its key priorities, which will be used to start discussions on the content of the next ARTF Incentive Program for FY1394-1396. The IP discussions were kick-started in March 2015, with a new Memorandum of Understanding expected to be signed by June 2015. As such, between April and June 2015, consultations with members of the IP Working Group will take place to agree on the design and content of the next IP.

vii. Ad Hoc Payments

The Ad Hoc Payments mechanism was introduced in the FY1393 Update to the ARTF Financing Strategy to allow donors to channel funds through the Recurrent Cost Window in support of bilateral agreements between the respective bilateral donor and the government, to which the ARTF Administrator is not privy. The bilateral agreement between the respective donor and Ministry of Finance is therefore not subject to oversight or due diligence of the World Bank as ARTF Administrator. However, funds channeled through the AHP are subject to the normal ARTF fiduciary framework for the RCW. Please refer to Annex V for more details on the AHP.

In the context of the fiscal crisis, a number of donors have come forward with contributions to the ARTF AHP to enable delivery of exceptional and emergency discretionary assistance within a short time frame in support of government's fiscal gap. While some donors have offered new funds for the AHP, other donors moved funds from their existing pledge. The latter poses challenges to the ARTF Administrator, and considerable risk to the ARTF program, as these funds had already been programmed under the previous FS 1391-1393 and the program was therefore suffering from a lack of funds towards the end of the FS period.

Considering the scale of the fiscal crisis, Afghanistan will likely require continued discretionary assistance in the medium term. However, it is important to ensure that this does not undermine the predictability of funds under the ARTF and that it does not come at the expense of scaling up contributions to the Investment Window, which would compromise critical service delivery and development outcomes in the medium term. Donors are therefore strongly encouraged to provide upfront information on their financial pledges, including plans to contribute to the AHP.

The AHP was introduced in the previous FS on a pilot basis with the caveat that it should be reviewed in the context of the new FS 1394-1396. Going forward, the Administrator proposes to continue the AHP while ensuring the least possible disruption to the general ARTF program as adopted under this FS. Should the AHP mechanism risk undermining the general integrity of the ARTF and its ability to meet the FS obligations, the Administrator will have to take necessary action to mitigate these risks, including potentially restricting the use of the AHP or, as a worst-case scenario, discontinuing the mechanism.

Please refer to Annex V for the full AHP concept note agreed with the ARTF Strategy Group.

viii. Research and Analysis Program

In April 2013, the ARTF Steering Committee endorsed the concept of the ARTF Research and Analysis Program (RAP) to facilitate and promote evidence-based policy research and knowledge consolidation through project-based and selected sector-wide/thematic research and impact evaluation. In March 2015, the Steering Committee endorsed adding the RAP to the ARTF structure and to include it in an amendment to the ARTF Standard Terms and Conditions. The RAP will therefore be budgeted for out of the ARTF (see Table 6).

The RAP provides an opportunity for introducing new and innovative ways of working with government, universities and other Afghan partners to undertake analysis and generate new knowledge. The World Bank will work to ensure that impact evaluations and analytical products include a focus on gender as a cross-cutting issue and provide gender disaggregated data.

The World Bank has previously financed priority analytical work through a combination of its own Bank budget as well as available funds from the ARTF fee income. So far, activities financed partly by the RAP include the following:

- Agriculture Sector Review: This study provides a comprehensive study on key agriculture sub-sectors and review of cross-cutting issues in the field. The report presents policy and strategic directions, which are necessary for revitalizing Afghanistan's agriculture for economic growth, job creation, and food security, and answers two key questions: (i) Will agriculture and natural resources be adequate to drive growth and job creation in Afghanistan?; and (ii) What are the most important sector-specific policy and investment priorities to support agricultural growth and job creation? The study and its recommendations are critical to a comprehensive sector strategy that will align the work of government and donors around a common set of goals and methodologies.
- Higher Education Sector Review: The review provides a wide-ranging and evidenced-based analysis of the Afghanistan Education Sector and surveys a variety of higher education systems, policies, and reforms observed in the modern world with an emphasis on areas where Afghanistan faces the greatest policy challenges;
- Subnational Constraints to Service Delivery: The report aims to identify the primary bottlenecks to service delivery in critical service delivery areas—primary education, basic health care, agricultural extension services, and community development. It also provides both operational and strategic guidance to sector teams implementing national programs and to the government on how to maximize the effectiveness and efficiency of its spending while responding to pressures to decentralize greater authority to subnational levels.

In line with RAP objectives, a number of sector-wide/thematic analytical work, project-based research, and impact evaluations are underway in the next Financing Strategy period, including:

- The **Public Sector Management Analytics** are a series of reports aiming to inform policy options for various Public Sector Management challenges, and to facilitate this policy dialogue;
- Another comprehensive upcoming sector study is the **Afghanistan Urbanization Review** which aims to generate knowledge on current patterns of urbanization at the national and subnational levels, analyze the key characteristics and challenges of Afghanistan's urban development, and provide policy and institutional recommendations during the country's transition;
- On the ARTF projects related research, the **NSP Future Directions** study will guide informed policy debate and facilitate decision making by government and key stakeholders regarding the future of the National Solidarity Program;
- In the extractives sector, a **comprehensive study of the energy sector** will be undertaken. The objective is to conduct a comprehensive assessment of the rural energy sector to inform investments that aim to increase accessibility to affordable and sustainable energy. The study will

therefore focus on a select number of key areas that will collectively provide the government, World Bank and other ARTF donors a complete understanding of opportunities, lessons learnt, constraints in the sector, capacity building needs in the sector, and recommendations.

- Similarly, a number of **impact evaluations** are planned in support of ARTF projects and work program. These include the Non-formal Approach to Training Education and Jobs in Afghanistan (NATEJA), Access to Finance Project, and the Targeting of the Ultra Poor Program.

While understanding that analytical needs are vast in Afghanistan, there is a need to be selective about activities chosen for ARTF RAP support. Government and the World Bank are currently working out a detailed prioritization of the top-most strategic analytical work over the short and medium term to underpin key government reform and policy priorities. As with the Investment Window pipeline, the RAP pipeline proposals outlined above are therefore only indicative and will be finalized as government's strategy evolves. The ARTF Strategy Group will consulted and updated as the pipeline develops to ensure coordination and collaboration.

i. Technical Assistance Project

The government's self-driven agenda to transform economic and social policy, undertake governance reforms, and establish citizen-centered service delivery requires not only sound technical support but also different ways to deliver that capacity given the vision specificity. To support this vision, a technical assistance facility, anchored in the Ministry of Finance, is proposed as a regular project. The project will provide government with a self-owned and self-paced mechanism to fund and to direct technical support to priorities founded on the president's vision and responsive to the context of a unity government navigating complex reform (e.g., development of an urban strategy or asset recovery).

There is agreement between government, donors and the World Bank that some reform areas might require greater government ownership in selecting the technical assistance preferred due to, for instance, political economy considerations (e.g. regional water policy analysis) or due to urgency. Others fall outside the legal or technical competence of the World Bank (e.g., cultural heritage or security sector expenditure rationalization). In this instance, technical assistance is understood as specific, short-term and highly technical consultancy and/or capacity-building – not continuous, across-board, advisory service or substitute for line positions. While the topics for the technical assistance project will be developed over time and outlined in the project document, the current priority areas include development of an urban strategy and cultural heritage management. All standard Bank fiduciary oversight and implementation support, including oversight of technical quality of outputs, will be in place for the TAF as for any other ARTF-funded project.

ANNEX I: Overview of ARTF/IDA Potential Projects

Sector	Project in pipeline	FY15 IDA	FY15 ARTF	FY16 IDA	FY16 ARTF	FY17 IDA	FY17 ARTF	Totals
Governance &	Development Policy Grant			$100				100
Capacity Building	PFM				**75**			75
Human Development	Basic Education				**100**[11]			100
	SHEP II (higher education)		50					50
Agriculture	Irrigation Rehabilitation and Development				**70**			70
	On Farm Water Management AF				**45**			45
	New agriculture program incl. grain reserves				**100**			100
Rural Development	NSP III AF				100			100
	NSP IV				**200**[12]			200
	Rural Water and Sanitation*				50			50
	Rural Livelihoods Project*				50			50
Social Development	Land Management Support				5[13]		25	30
Infrastructure	DABS TA				5			5
	Naghlu Rehabilitation				70			70
	Power Development Support Project AF				20			20
	Kunar (for regional funds) FY17-18 TBD							TBD
	Resource Corridors/Extractives			75				75
	Afghanistan Rural Access AF*						**100**	100
	Baghlan to Bamyan			250				250
	Customs AF	50						50
	Large Irrigation Dam (ex. Shahtoot or Gulbahar)							TBD
Urban	Urban Program TBD			**150**				150
	Total	**50**	**50**	**575**	**890**	**0**	**125**	**1,690**

Note: (i) The projects highlighted in light blue are those approved already in the ARTF Interim Arrangement; (ii) Projects marked by a * are projects that will be considered as part of a move towards a programmatic approach at MRRD as led by Government.

[11] The full value of the next phase of primary education is tentatively set at $200 million with a first tranche of $200 million to be released in 1396;

[12] NSP (title TBD) is tentatively set at $400 million with a first tranche of $200 million to be released in 1395.

[13] A first preparation grant of $5 million proposed.

ANNEX II - Portfolio Overview (ARTF and IDA)

(As of July 08, 2014)

								Overall			IDA			ARTF			Other TFs						
Proj ID.[1/2/]	IDA/TF #	Project Title	# Proj	Approval FY	Closing Date	TTL	Financing	Comm Amt	Cancelled	Net Commit	Commit	Disb.	Undisb Balance	Commit	Disb.	Undisb Balance	Commit	Disb.	Undisb Balance	Undisb Bal at Beg of FY	FY14 Disb.	Disb Ratio	Age yrs
ARTF																							
P091258	TF50577	ARTF - Recurrent and Capital Costs (TF050577)	1	FY02	06/30/2018	Sisk	ARTF	3,074.3		3,074				3,074.3	3,072.5	16.8				190.7	188.9	99.1	12.2
P120427	TF10024	AF: ARTF-Public Fin. Mgmt. Reform II (TF 10024)	1	FY12	12/31/2014	Sisk	ARTF	73.0		73				73.0	43.4	29.6				45.0	15.4	34.2	2.9
P111943	TF93513	AF: ATRF - Power System Development (TF 93513)	1	FY09	1/31/2015	Spencer	ARTF	60.0		60				60.0	48.6	11.4				26.3	14.9	56.7	5.6
P120397	TF15003	AF: ARTF-Agricultural Inputs Project (TF 15003)	1	FY13	6/30/2018	Soler	ARTF	74.8		75				74.8	6.3	68.5				-	6.3	-	0.8
P120398	TF99074	AF: ARTF-On-Farm Water Management (OFWM) (TF 99074)	1	FY11	06/30/2015	Matsumoto	ARTF	41.0	16.0	25				25.0	17.8	7.2				16.3	9.1	55.9	3.3
P143841	TF13820	ARTF-Natl Horticulture & Livestock Project (TF 13820)	1	FY13	12/31/2018	Soler	ARTF	50.0		50				50.0	19.0	31.0				44.1	13.1	29.7	1.4
P118028	TF12533	AF: ARTF-2nd Judicial Reform Project (TF 12533)	1	FY12	06/01/2017	Beardsley	ARTF	40.0		40				40.0	8.7	31.3				34.1	2.8	8.2	2.0
P121883	TF98001	AF Strengthening Natl.Statistical System (TF 98001)	1	FY11	02/29/2016	Kotikula	ARTF	14.0		14				14.0	4.1	9.9				10.5	0.6	5.7	3.6
P123845	TF11447	AF: ARTF - CB for Results Facility (TF 11447)	1	FY12	12/31/2017	Prasad	ARTF	100.0		100				100.0	35.3	68.7				74.5	9.7	13.1	2.4
P149410	TF17012	CASA-1000 Community Support Program	1	FY14	6/30/2017	Naila Ahmed	ARTF	40.0		40.0				40	-	40				40		0.0	
P146015	TF16354	Non-Formal Approach to Training Education and Jobs in Afghan	1	FY14	4/30/2018	Leopold Remi	ARTF	15.0		15.0				15	1	14				-	1		
P131864	TF17061	Kabul Urban Transport Efficiency Improvement Project	1	FY14	12/31/2019	Luquan Tian	ARTF	90.5		90.5				90.5	5	85				-	5		
P125597	TF17016	Kabul Municipal Development Program	1	FY14	04/31/2019	Deepali Tewa	ARTF	110.0		110.0				110	6	104				-	6		
P125597	TF14211	Kabul Municipality Development Project (PPG)	1	FY13	05/31/14	Deepali Tewa	ARTF	5.0		5.0				5.0	2.9	2.1				5.0	2.9	57.1	
P132944	TF14861	Naghlu Hydropower Rehabilitation Project(PPG)	1	FY13	12/31/14	Richard Jerem	ARTF	5.0		5.0				4.9	1.0	3.97				4.9	1.0	20.4	
P146184	TF 15577	Higher Education Development Project (PPG)	1	FY14	12/31/14	Harsha Aturu	ARTF	4.9		4.9				4.9	2.4	2.5				4.9	2.4	2.5	
P145443	TF 14845	Afghanistan Resource Corridor Project	1	FY13	12/31/14	Guillemette S	ARTF	2.7		2.7				2.7	0.9	1.76				2.4	1	39.3	1.4
TOTAL		17								3,784				3,784.1	3,274.9	527.8				498.7	280.0		
IDA																							
P118925	H6990	Afghanistan SDNRP II (H699)	1	FY11	06/30/2016	Stanley	IDA	52.0		52.0	52.0	10.3	40.3							46.1	5.0	10.9	3.0
P121755	H6650	Afghanistan ICT Sector Development Proje (H665)	1	FY11	06/30/2016	Tenzin	IDA	50.0		50.0	50.0	21.5	27.5							40.5	12.4	30.5	3.1
P087860	H2250	AF: Urban Water Sector (H225) - partially cancelled	1	FY06	06/30/2014	Tewari	IDA	40.0	24.2	16.9	16.9	15.1	3.79							13.1	9.3	70.9	7.9
P110644	H4840	AF: Financial Sector Strengthening Proj (H484)	1	FY09	06/30/2014	Jaffrin	IDA	8.0	6.2	8.0	8.0	2.3	0.01							6.8	0.6	9.3	5.1
P118053	H6800	AF: New Market Development (H680)	1	FY11	02/29/2016	Jaffrin	IDA	22.0		22.0	22.0	6.4	15.2							18.0	2.5	13.9	3.1
P119047	H7320	Financial Sector Rapid Response Project (H732)	1	FY12	06/30/2016	Jaffrin	IDA	19.0		19.0	19.0	5.8	12.6							13.2	0.7	5.0	2.8
P118027	H8740	AF: Development Policy Prog. Series (H874)	1	FY14	06/15/2015	Nassif	IDA	50.0		50.0	50.0		50.0							-	51.2	-	0.8
P113421	H5230	AF: Pension Admin and Safety Net (H523/H848)	1	FY09	06/30/2016	Al-Ahmadi	IDA	7.6		7.6	7.6	7.5	0.102							13.9	2.5	18.0	4.6
	H8480			FY13	6/30/2018	Al-Ahmadi	IDA	12.5		12.5	12.5	1.5	11.3							12.5	0.0	0.0	1.6
P132742	H8340	Second Skills Development Project (H8340)	1	FY13	06/30/2018	Sarr	IDA	55.0		55.0	55.0	8.5	46.6							55.1	8.4	15.3	1.0
P128048	H8940	Afghanistan Access to Finance (H8940)	1	FY14	12/31/2018	Jaffrin	IDA	50.0		50.0	50.0	2.0	48.3								2.0		0.3
P145054	IDA H9270	Central Asia South Asia Electricity Transmission and Trade Proje	1	FY14	6/30/2020	Sunil Kumar K	IDA	316.5		316.5	316.5		317							316.5	-	-	
P145054	IDA Q9010	Central Asia South Asia Electricity Transmission and Trade Project (CASA-1000) (PPF)	1	FY14	12/31/2014	Sunil Kumar K	IDA	3.0		3.0	3.0	1.0	2.0										
P145347	IDA Q8940	Baghlan (Dushi) Bamyan (PPF)	1	FY14	6/15/2015	Luquan Tian	IDA	5.0		5.0	5.0		5.0										
P112872	H5680	AF: Customs Reform & Trade Facilitation (H568)	1	FY10	06/30/2015	Zaidi	IDA	50.5		50	50.5	50.3	1.09							19.6	18.5	94.3	4.0
TOTAL		14								718	718.0	132.1	580.41							555.3	113.1		37.3
Co-Financed																							
P110407	H5310	AF: Rural Enterprise Devt Program (H531)	1	FY10	01/01/2015	Ladisy Komba	IDA	30.0		30.0	30.0	17.7	11.6							17.0	5.3	31.5	4.2
	TF98045	*ARTF Cofinancing TF98045*	0	FY11	01/01/15	Ladisy Komba	ARTF	16.0	9.8	6.2				6.2	6.2	0.0				11.14	1.4	12.7	3.6
P117103	H6030	AF: National Solidarity Program III (H603)	1	FY10	09/30/2015	Ladisy Komba	IDA	40.0		40.0	40.0	40.0	0.1							0.9	0.8	91.6	3.9
	TF98459	*ARTF Cofinancing TF 98459*	0	FY11	9/30/2015	Ladisy Komba	ARTF	950.0		950.0				950.0	773.4	174.6				62.81	301.5	480.1	3.3
P122235	H6810	AF: Irrigation Restoration &Development (H681)	1	FY11	12/31/2017	Matsumoto	IDA	97.8		97.8	97.8	44.8	55.3							66.9	37.6	56.1	3.1
	TF12029	*ARTF Cofinancing TF 12029*	0	FY12	12/31/2017	Matsumoto	ARTF	48.4		48.4				48.4	11.3	37.1				43.83	6.8	15.4	2.9
P125961	H7920	AF: Afghanistan Rural Access Project (H792)	1	FY12	03/31/2018	Luquan Tian	IDA	125.0		125.0	125.0	47.1	80.5							116.4	36.1	31.0	1.9
	TF13093	*ARTF Cofinancing TF13093*	0	FY13	3/31/2018	Luquan Tian	ARTF	107.0		107.0				107.0	14.5	92.5				107.0	14.5	13.6	1.8
P129663	TF15005	'System Enhancement for Health (SEHAT) TF15005	1	FY14	10/31/2018	Ghulam Dasta	ARTF	100.0		100.0				100.0	50.4	49.6				100.00	49.7	49.7	1.3
	H8290		0	FY13	30/06/2018	Ghulam Dasta	IDA	100.0		100.0	100.0	32.3	67.7							100.0	32.6	32.6	1.1
	TF95691			FY09	30/06/2018	Ghulam Dasta	HRBF	12.0		12.0							12.0	7.3	4.7	7.1	2.4	34.2	4.4
P106259	TF93962	Second Education Quality Improvement Project (EQUIP II)	1	FY08	8/15/2014	Samantha de	ARTF	408.0		408				408.0	245.0	353.8				123.10	82.4	66.9	6.5
TOTAL		5								2,024	392.8	181.9	215.2	1,619.6	1,100.8	353.8	12.0	7.3	4.7	756.1	571.2		
Sub total											2,024	1,290.1	734										
Total IDA +ARTF+CoF			36							6,527	6,527	4,697.1	1,842.5	7,733.1	5,678.9	2,100.1	24.0	14.7	9.3	1,810.1	964.4	53.3	3.8

ANNEX III
The ARTF Risk Matrix

The World Bank's Standardized Operations Risk-Rating Tool (SORT) is applied to the ARTF at the trust fund level. This includes an assessment of risks along eight different categories[14]. More detail is included in the matrix below.

1. **Political and Governance:**

Risk Area	Risk	Risk Rating[15]	Mitigation Measures
Political and Governance	Transition will result in major changes to the political economy, and contribute to potential challenges to the general governance environment. Potential increase in conflict and continued violence around the country impacts adversely on the ability to operate and implement projects.	S	The World Bank will as the ARTF Administrator continue monitoring the potential impact on ARTF financing of changes to the political economy. This risk is directly addressed by the strong ARTF fiduciary framework and will to the extent possible be mitigated through close cooperation with key government counterparts in Ministry of Finance. The ARTF-financed projects are implemented by government. While violence and conflict also affects government staff and is a constant challenge, line ministries and national staff have so far maintained the ability to reach the community level to ensure project implementation and service delivery. This is also helped by project designs that take into consideration the difficult operating environment and make use of design models that rely on community involvement for implementation.
	Uncertainty and volatility has followed the second round of the 2014 presidential elections. While a new President has been inaugurated, and a new Cabinet is	S	The ARTF Administrator will continue to monitor the situation closely and will remain engaged with our key counterparts in Ministry of Finance and the line ministries to mitigate to the extent possible impact on the ARTF program.

[14] 8 categories: 1. Political and governance; 2. Macroeconomics; 3. Technical design of a project; 4. Institutional capacity for implementation and sustainability; 5. Fiduciary; 6. Environment and social; 7. Stakeholders; and 8. Other. The 9th category that is part of the SORT, Sector Strategies and Policies, is not included at the program level.
[15] H=High, S=Substantial, M=Moderate, L=Low

	expected to be announced, volatility could continue should the legitimacy of a new government be in question. This could have a significant impact on the reform process as well as the implementation progress of ARTF funded development programs.		The Administrator has worked to ensure that financing has been allocated to all major service delivery programs in the portfolio so delivery of health, education and other critical services can continue without interruption. Work will continue at the technical and working levels to ensure basic service delivery continues. The Administrator is preparing for its engagement with a new government to ensure readiness of the ARTF. A new Financing Strategy will be developed in close cooperation with the incoming government and donors to support the government's key development priorities.

2. Macroeconomics:

Risk Area	Risk	Risk Rating[16]	Mitigation Measures
Economic risks	The transition process may pose continued challenges to macroeconomic stability over the coming few years, including further slow-down in economic growth and exchange rate depreciation. Moreover, the economy is susceptible to exogenous shocks such as changes in weather and international prices, especially for food and fuels. The Government has only few instruments, mainly	S	Funds through the Recurrent Cost Window will help mitigate the risk of a potentially increasing fiscal gap. It cannot, however, cover the growing expenditures of government and revenue increases will be required. Through the Incentive Program (IP) and the World Bank Development Policy Grant, work will continue to improve revenue and fiscal sustainability. A reform dialogue will be initiated with the new government to create momentum for revenue improvements etc. A new IP will be negotiated with the new government for FY1394-1396.

[16] H=High, S=Substantial, M=Moderate, L=Low

	in the monetary sphere, to respond to adverse macroeconomic developments.		
Fiscal sustainability	Increasing public expenditures and simultaneous reductions in government's revenues impacts negatively on fiscal sustainability. Government not meeting its basic operating expenditures, salary in particular, could have severe effects on the stability of the country.	H	The ARTF continues to support government's operating budget with annual contributions through the Recurrent Cost Window, including the Incentive Program and Operations & Maintenance Facility. This allows government to finance (civilian) salaries and operations and maintenance expenditures. Donors can provide financing directly to government, based on bilateral agreements between the respective donor and government, and channel the funds through the ARTF Ad-Hoc TMAF Payments window (ATP). The ATP ensures fiduciary oversight and allows donors to support government in addressing the fiscal gap. The Incentive Program and the World Bank's Development Policy Grant is working to strengthen government's revenue collection with a specific focus on customs.

3. **Technical design of a project:**

Risk Area	Risk	Risk Rating[17]	Mitigation Measures
Project design	Project performance is easily affected by the challenging context, which risks impacting on results.	M	Project design should take into consideration the low capacity and challenging operating environment. This requires use of flexible modalities and innovative project design – weighing long-term sustainability gains against short/medium term service delivery: • Outsourcing service delivery: Health using NGOs to deliver a basic health package across the country; contracts managed by ministry;

[17] H=High, S=Substantial, M=Moderate, L=Low

			• An in between model: NSP: Uses facilitating partners to work with communities in the field, but general operations maintained by ministry. • Using country systems: EQUIP: fully integrated into the ministry systems, no PIU.

Portfolio Performance	In a high risk, low capacity environment, the portfolio performance is easily affected.	M	Portfolio management requires an integrated approach with regular trouble shooting:
			• Careful and continuous monitoring: 2 levels:
			  • Operational through biweekly Senior Ops Meetings
			  • Strategic level through biweekly Sector Advisory Group
			• Annual PPRs focusing on identifying key bottlenecks to portfolio performance;
			• Proactive approach to restructurings – 6 last year alone.
			• Strong Bank-Client collaboration on portfolio issues to ensure ownership and proactive approach.
			
			Please see Annex II for a full outline of the mechanisms through which portfolio performance risks are mitigated.

4. Institutional capacity for implementation and sustainability:

Risk Area	Risk	Risk Rating[18]	Mitigation Measures
Implementation capacity	The absorbtive and implementation capacity of line ministries is a key factor in how projects perform and therefore how funds can be allocated and disbursed. While the ARTF	S	Implementation risks are mitigated through careful project design, capacity building and ongoing close supervision of project performance. The ARTF Administrator also carries out annual portfolio performance review to identify and address crosscutting issues. Identified issues are

[18] H=High, S=Substantial, M=Moderate, L=Low

	portfolio is generally performing well with high disbursement rates, implementation continues to face a number of challenges affected by the implementation capacity in line ministries and agencies.		discussed in detail with Government to ensure their involvement and ownership in solving problems and removing bottlenecks.
World Bank resources	The Bank's capacity to support line ministries in project preparation and implementation and to perform supervision is critical to the quality and effectiveness of the portfolio.	L	While the Bank has over the last year started aligning its working model with the World Bank's normal business model. An office has been established in Dubai to ensure staff has easy access to travel to Afghanistan and to make sure the Afghanistan is able to attract a wide range of skills needed to support the complex program. With some staff based in Dubai, more visiting missions can be accommodated which allows the Bank to move in skills as needed for the program. Also, local staff is being trained to ensure they can increasingly take on more responsibility for support to the client. In terms of *facetime*[19] the World Bank in Afghanistan continues to be at the forefront for the World Bank with around 12,000 days annually, compared to the average for fragile states (3000 days) or IDA countries (7500). Afghanistan is thereby number one within the World Bank for hands-on support to and engagement with the client. To continue supporting the large ARTF program the ARTF admin fee will be increased to 3 % from january 1, 2016, and to 4 % from january 1, 2017. The fee on AHP financing will continue at 2 %. The fee increase will allow the ARTF to align itself with the Bank's policy for full cost recovery from trust funds and continue supporting the large scale ARTF program in Afghanistan.

[19] Face-time is a new measure of the Bank's engagement with client countries that aggregates in a single scale multiple forms of engagement including Field staff (both national and international staff), and mission travel (from both HQ and nearby offices).

			The fee increase has been discussed with donors who are supportive and will be discussed with the new government.

5. **Fiduciary:**

Risk Area	Risk	Risk Rating[20]	Mitigation Measures
Fiduciary risks	Fiduciary risks are significant despite good progress. Investment operations (e.g., Public Financial Management Reform Project I and II) have helped to put in place adequate processes and practices for financial management, procurement and control. Afghanistan has a relatively strong public finance capacity track record as witnessed by the 2013 PEFA. However, fiduciary risks remain significant.	H	Safeguarding funds is a multifaceted approach taking place through four complementary modalities: 1. Technical assistance through individual investment projects; 2. Capacity building: CBR and PFM investment projects. The ARTF financed PFM II investment project focuses on technical assistance to further strengthen government control systems; 3. Policy reform work: Incentive Program and the IDA-financed Development Policy Grant. A new IP and DPG and a new PFM project will be negotiated with the new government to ensure reform momentum continues in a sustainable manner to address fiduciary risks by implementing reform and building systems and capacity in government: ➔ The ARTF Incentive Program focuses heavily on the timely implementation of PFM measures, including internal and external audits, procurement certifications, and budget transparency; ➔ Better internal and external budget controls, greater budget transparency, deep customs reforms aimed at improving efficiency, enhancing controls and reducing rent-seeking opportunities; and incentives for domestic revenue growth and improved budgetary spending 4. A strong and comprehensive fiduciary framework to safeguard ARTF funds channeled through the budget, along four lines: 1. strong community ownership and monitoring; 2. government wide controls;

[20] H=High, S=Substantial, M=Moderate, L=Low

			3. World Bank supervision; and 4. Additional controls: Monitoring and Supervisory Agents. The new Government has emphasized its strong disregard for corruption and highlighted its intention to root out such practices. In support of Government's strategy, the ARTF Administrator will work with Government and donors to assess potential additional anti-corruption measures.
Controls	Strong controls are needed to mitigate fiduciary risks, including independent verification, to ensure donor confidence in ARTF systems and fiduciary controls and allow donors to continue financing on budget.	**H**	**Third Party Monitoring agents address the specific weaknesses of the operating environment and adds a layer of control:** • **ARTF Monitoring Agent** (accounting firm): Monitors the entire civilian operating budget for eligibility: – MA performs automated desk review of 100 % of recurrent cost expenditures; – MA performs risk-based review of expenditures, incl. visits to provinces. • **ARTF Supervisory Agent**: Carries out asset verification, quality assurance, and data mapping of national infrastructure projects (NSP, rural roads, education and irrigation): – Provides the Bank with strengthened outreach to all 34 provinces of Afghanistan, including highly insecure areas, to get data from key national programs.

6. Environment and social:

Risk Area	Risk	Risk Rating[21]	Mitigation Measures
Environment	Lack of implementation and monitoring capacity of the national environmental law.	S	Environment risks are analyzed on a project-by-project basis. All projects and operations financed under the ARTF follow World Bank policies and procedures for environmental safeguards. Projects are required to develop environment and social management plans.
Social	Tenure insecurity and land conflicts plus multiple, inconsistent and overlapping legal framework.	S	Social risks are analyzed on a project-by-project basis. All projects and operations financed under the ARTF follow World Bank policies and procedures for social safeguards. Projects are required to develop environment and social management plans and resettlement action plans in case of land acquisition.
Implementation and Monitoring	Weak implementation and monitoring capacity in implementing ministries.	H	Assessed during design phased and identified weaknesses addressed through project design, implementation arrangements and ongoing World Bank supervision.
Disasters	Natural disaster risks including flooding, droughts, earth quakes, locusts etc.	H	The World Bank focuses on disaster risk management at the project level, where appropriate response mechanisms are incorporated into the project design to be activated in case of an emergency. Also, infrastructure quality specifications take into account potential disaster risks.
Gender	Marginalization of women in the economy and broader development.	H	The World Bank follows a mainstreaming approach to ensure gender issues are addressed as a cross cutting issue in the ARTF portfolio. This includes careful attention to gender issues at the project level, where project designs take into consideration the relevant challenges and opportunities. The World Bank gender specialist works closely with line ministries to provide input and guidance to ensure gender inclusion and equity. The

[21] H=High, S=Substantial, M=Moderate, L=Low

			World Bank is also piloting socially and culturally acceptable approaches for access and participation of women. Policy dialogue with line ministries as well as Ministry of Finance to emphasize the importance of increased gender equity.

7. Stakeholders:

Risk Area	Risk	Risk Rating[22]	Mitigation Measures
Stakeholder risks	In light of Afghanistan's aid dependency, continued donor support will be crucial for balancing the budget. At the Tokyo and Chicago Conference in 2012, international partners committed to providing military and civilian support to Afghanistan through 2016. In return, the Afghan Government committed to key deliverables outlined in the Tokyo Mutual Accountability Framework. Predictability of donor contributions is therefore highly dependent on developments that are outside the immediate control of the ARTF.	S	The performance of the portfolio and the delivery of the ARTF Financing Strategy is likely to influence donors' willingness to continue high levels of contributions to the ARTF. The ARTF therefore needs to ensure a continued focus on effectiveness and delivering results. To allow substantive discussions on effectiveness, the Administrator has strengthened the focus on results reporting. The ARTF Scorecard is published annually and feed into a dialogue with Government and donors on results, effectiveness and funding priorities. The Administrator manages the cash balance as well as supply and demand of funds very carefully, structured in the ARTF Financing Strategy which is updated annually. This helps mitigate the risk of a deficit of funds. Donors are strongly encouraged to provide information on planned estimated contributions on a three year rolling basis to allow for more accuracy in the Administrator's planning.

[22] H=High, S=Substantial, M=Moderate, L=Low

	Donor pledges, single-or multi-year, are often lacking. This creates a challenge to the cash balance management of the Administrator in trying to meet the agreements outlined in the Financing Strategy. While donor financing has remained stable around US8-900 million over the last years, it not yet clear if donor contributions to the ARTF will remain at this high level.		
Security	The general security levels will impact on the ARTF's ability to support the government and people of Afghanistan.	H	Due to the World Bank mandate the ARTF does not have any dealings on security and rely entirely on the Afghan authorities and the international community and their mitigation measures. NATO just concluded a summit in Wales. The summit concluded that the ISAF mission will conclude at the end of 2014. NATO remains committed though and will continue supporting Afghansitan through (i) training, advising and supporting ANSF as well as supporting financial needs of ANSF sustainment to the end of 2017 and through 2024 when the Afghan government needs to assume full financial responsibility for its security forces.
Beneficiaries	Increased tension between different social and/or regional groups. Balancing the different regions of the country as there is some overlap between ethnic groups and regions and the tension between centralization and	M	The World Bank social safeguards policies apply to ARTF projects which ensures social inclusion irrespective of gender, ethnic and religious affiliation in ARTF-financed projects. The ARTF adhers to the policies of the Afghan government but within the ARTF-financed projects the World Bank strives to ensure a balanced regional spread of resources.

	devolution to the regional and provincial levels.		
Managing expectations	There is growing pressure on the ARTF to take on an increasingly larger share of the development assistance for Afghanistan, i.e. accept responsibility for the funding of still more National Priority Programs etc. The demand for ARTF resources has to match the supply of funding from donors as well as the available implementation capacity and Bank resources to ensure the program is realistic and can meet expectations.	S	It is critical that expectations are managed in terms of the ARTF's capacity to continue scaling up its program. This requires careful and ongoing dialogue with Government and donors on ARTF capacity. The ARTF Administrator manages this by ensuring frank and transparent information and continuous updates to Government and donors.

8. **Other:**

Risk Area	Risk	Risk Rating[23]	Mitigation Measures
Supervision/Access to field	The Administrator's ability to supervise the portfolio, and particularly the project sites located in high risk and/or remote areas, is affected by the general security situation in the 34 provinces of the country.	H	Access to the field happens along three parallel tracks: 1. Implementing agencies: ▪ Working through government ensures access to the field, using community monitoring, grievance mechanisms, ICT and partners; ▪ Projects have been able to adapt to changing operating environment and government staff are so far still able to access projects. 2. The World Bank as ARTF Administrator:

[23] H=High, S=Substantial, M=Moderate, L=Low

	Access to project sites in the provinces is crucial to provide monitoring by line ministries and implementation support and supervision by the World Bank. Previously the World Bank team could rely on logistical support from donors and Provincial Reconstruction Teams located in the provinces. This option is now diminishing and logistical support in the field is getting scarce.		▪ Continues to use the UN facilities in the field; ▪ The World Bank has established a guesthouse in Mazar-e-Sharif in Balkh province. This will allow the Bank teams easy access to the northern provinces and enable field visits in this part of the country; ▪ 19 out of 32 Bank projects with ~15,000 project sites within 200 KM radius of Mazar, allowing for day trips; 3. Making use of ICT and third party monitoring agents to get data; ▪ The ARTF Supervisory Agent ensures constant monitoring of ARTF projects, even in conflict-affected areas, and a steady flow of verified data to feed into and enhance the ongoing dialogue with the implementing line ministries; ▪ Individualized innovative approaches to use ICT in project supervision is being developed and built into the project design to ensure access to data and establish beneficiary feedback mechanisms in communities.

ANNEX IV – ARTF Results Snapshot

The ARTF is currently serving 8.1 million people in all of Afghanistan's 34 provinces, 38 percent of whom are female. When counting the National Solidarity Program, the number of beneficiaries swells to 22.4 million people, 48.5 of whom are female. The ARTF Investment Window is currently financing 23 projects in 5 sectors aligned with the ANDS: Agriculture, Rural Development, Human Development, Infrastructure, and Governance. A snapshot of results achieved in the 5 sectors is outlined below.

A snapshot of aggregate results under the ARTF Investment Window	
Agriculture	- **9,815 ha** have been provided with irrigation and drainage services; - **67 percent** of target famers have adequate improved technology; - **a 2.23 ton per hector** increase in agricultural productivity; - **178,000 people** have access to agricultural and irrigation services (**52 percent** of which are female).
Rural Development	- **31,000 CDCs** have been elected through a democratic process where 36 percent of CDC members are female; - **The Block Grants** provided to CDCs have totaled **$1.2 billion** and 77507 sub proposals have been financed; - Supporting sustainable economic growth through improved employment and income opportunities: **54.2 million labor days** were created and a 31 percent increase in direct employment through supported Enterprise Groups (with 35 percent are female members); - **48,676 beneficiaries** participating in Savings Groups and Enterprise Groups (42 percent of which are female) and AFs 107 million in savings collected by Savings Groups and Village and Loans Association members; and - In rural transport, essential to promoting equitable economic growth, **6,497,000 million** people living within 2km of an all season road with 15,000km or rural roads have been rehabilitated and maintained
Human Development	- **7.8 million** children have been enrolled in school (**38 percent** of whom are female); - **6805 classrooms** have been constructed or rehabilitated, and **160,515** teachers have been trained; - **18,980 beneficiaries** have received skills development training (30) percent are female, and of those graduated, women see an average monthly increase in earning of AFN 3428 while youth receive AFN 8158. - Where Afghanistan previously had the highest maternal mortality rate in the world, today prenatal care coverage is now 39 percent up from 6 percent in 2003; - **39 percent** of births are now attended by a skilled attendant and institutional deliveries are now at 43 percent, up from 7 percent in 2004; - The number of health facilities nationwide increased to **2,000 (496 in 2003)** with **38.6** percent providing complete services outlined in the BPHS while 20,000 community health workers—half of them women—were trained and deployed throughout the country, increasing access to family planning and boosting childhood vaccinations.
Infrastructure	- Through several power supply projects, including also sub-projects under the NSP, **3,219,000 beneficiaries** have been provided with new or rehabilitated metered connections to the grid in the target areas with 316 km distribution lines transmission lines constructed or rehabilitated under the project.
Governance	- **4 World Bank** financed projects audits have been verified to have been done to international standards;

	- **23 procurement units** in line ministries and provincial offices have been restructured for stand-alone procurement; - **21 ministries** have completed pay grading and 92 percent of management positions have been filled; - Government **revenues** have increased by **28.3 billion AFs** since 2012 and the previous **open budget index** score target has been surpassed with a solid score of **59**.

To ensure that development results are tracked and reported to diverse audiences including donors, government officials, civil society groups and beneficiaries, the ARTF has taken steps to strengthen result tracking and reporting mechanisms to leverage transparency and accountability by creating a series of complementary tools such as: ARTF Scorecard; ARTF Results Matrix; ARTF at Work Series; The ARTF Biannual Report; ARTF multimedia productions; and, ARTF Open Data System.

These tools have not only been an operational innovation in the area of results tracking and reporting but also instrumental in strengthening donor coordination as well as government counterparts. All tools are available on the ARTF website: www.artf.af

Annex V
ARTF Ad Hoc Payments
Concept Note, September 2014

Under the FY1393 Update to the ARTF Financing Strategy the "Ad hoc Bilateral TMAF Payments (ATP)" was introduced. The ARTF Strategy Group in September 2014 agreed to change the name of the new scheme to allow donors to channel funds through the ARTF without necessarily linking those funds to the TMAF and its progress. This line of ad hoc donor contributions is instead denoted as "ARTF Ad Hoc Payments" (AHP)" and take the place of the previous ATP in the Financing Strategy.

<u>The content of the AHP:</u>

In FY1393 individual donors[24], may decide to make contributions on a pilot basis, in addition to their annual pledge already made for the ARTF. These additional ad hoc contributions arise from agreements between the respective bilateral donor and Ministry of Finance, to which the Administrator is not privy. The bilateral agreement between the respective donor and Ministry of Finance is therefore not subject to oversight or due diligence of the World Bank as ARTF Administrator.

Pledges already made by donors in the Financing Strategy cannot be switched to AHP. Should a donor none the less, considering the current fiscal deficit, preference funds from an existing pledge for the AHP, this will count towards the overall preferencing of the contribution, i.e. maximum 50% of the annual contribution can be preferenced.

The Administrator, Government and Donors agreed that AHP is entirely separate from the ARTF Incentive Program, which will continue uninterrupted regardless of the status of the AHP.

AHP contributions will be subject to the same fiduciary controls and monitoring arrangements as the ARTF Recurrent Cost Window.

The new arrangement will run on a pilot-basis starting with a first disbursement of US$15 million in December 2013. It will be reviewed and discussed in advance of the new FY1394-1396 Financing Strategy.

[24] The Ministry of Finance and US Government requested the ARTF Administrator to consider an ad hoc arrangement that will enable the latter to transfer funds to the former in recognition of TMAF achievements.

ANNEX VI: Monitoring and Mitigation Mechanisms

Monitoring and risks mitigation occur at several levels:

1. **Internal Bank risk monitoring and mitigation**:
    - Portfolio level by sectors and the Country Management Unit – bi-weekly discussions at Senior Operations Group (operational, fiduciary);
    - Country Management Unit reviews and follows up on SAR monthly reports (operational);
    - Annual Portfolio Performance Review exercise (operational, security, fiduciary);
    - The bi-weekly Sector Advisory Group focus on strategic level risks (security, political, fiduciary);
    - Annual internal World Bank budget discussions (operational, fiduciary);
    - Management dialogue on country program risks (security, political, operational, reputational)
2. **World Bank-Client dialogue on risks and mitigation:**
    - Regular discussions with Ministry of Finance and relevant line ministries on projects/programs (operational, security, fiduciary);
    - Annual dialogue based on Portfolio Performance Review (operational, security, fiduciary);
    - Annual dialogue focusing on ARTF financing priorities (ARTF Financing Strategy) (political, operational, security, fiduciary, reputational).
3. **Through the ARTF risks are monitored and discussed:**
    - ARTF Strategy Group – discussions with donors (operational, political, security, fiduciary, reputational);
    - ARTF Financing Strategy – annual review of ARTF financing (political, security).
4. **Risk ratings and lessons learned are reported on in:**
    - Biannual Implementation Status and Results reports;
    - Implementation Completion Reports.

Annex VII

ARTF Interim Arrangement

Key message: The Ministry of Finance does not find that the timing is currently right to engage in a detailed discussion of future priorities for ARTF funding. Instead they have requested that an interim solution is found to allow the new government the necessary time to define its key priorities and thereafter agree with the ARTF Administrator and donors on ARTF financing for the coming three years. Ministry of Finance has therefore proposed a bridging arrangement be devised to continue core priorities, while leaving time for reflection and dialogue.

This note outlines a proposal that addresses Government's concerns, including a medium term proposal. The proposal has been discussed with and endorsed by the ARTF Strategy Group.

How each ARTF component would proceed without a new Financing Strategy or under an interim arrangement?

ARTF Windows	ARTF Components	How would it proceed without an FS or under an interim arrangement?
Recurrent Cost Window	Baseline financing	Baseline financing will require a new FS or interim arrangement to be in place for new funds to be committed
	The Ongoing Incentive Program	The current IP runs till June 30, 2015. Payments under this phase of the IP do not require a new FS in order to disburse financing earned by Government.
	New Incentive Program, including O&M	The plan is to have a new IP in place to start July 1, 2015 to allow Government to earn funds during the second half of the fiscal year. A new IP will, however, require that a Financing Strategy to be in place as the IP will have to align with government's overall reform priorities and the financing framework of the ARTF. This will ensure the IP is focused on key reforms.
Investment Window	Tranches of funding for ongoing projects (i.e. SEHAT, CBR, ARAP etc.)	Tranches do not require a new FS to be in place. These projects have been approved by the Management Committee in full under the previous Financing Strategy and as such financing is transferred independent of a new FS.
	New pipeline projects (e.g., next phase of primary education or of NSP)	Financing of new projects would require that a new FS or an interim arrangement be in place.

Proposal: In the absence of a new FS a medium-term interim solution is outlined below. This would allow the ARTF to continue financing key priorities, while leaving sufficient time and space for the Government to define its priorities and agree with donors and the Administrator on a robust three-year framework and financing strategy.

1. **Key principles of the interim arrangement:**
    - This interim arrangement will cover at its maximum the period up and until June 21, 2015, i.e. half way through the Afghan fiscal year 1394. It will at any time during this period be superseded by a new FS endorsed by the ARTF Steering Committee;
    - A new Incentive Program (IP) cannot be agreed or activated without a new Financing Strategy as its guiding framework. The Administrator urges Government and donors to approve a new FS by June 21, 2015, to allow the new IP to start as the current IP expires June 30, 2015;
    - The interim arrangement will be reviewed on a regular basis by the ARTF Administrator and the Strategy Group will be updated regularly and included in discussions and key decisions.

2. **Proposed Financing under the Interim Arrangement:**
    - **RCW Baseline:** The baseline financing would provide financing continuing at the 1393 level of US$125 million or US$31.25 million per quarter;
        - The baseline financing would be disbursed on a quarterly basis in line with previous practice;
        - The amount available per quarter for disbursement would be equivalent of one quarter amount of the baseline amount as outlined in the draft Financing Strategy – US$125 million of which a quarter is US$31.25 million. Should this overall amount change in the finalized version of the Financing Strategy, the remainder of the available baseline financing would be split in two parts to be disbursed in Q3 and Q4.
    - **Incentive Program:** The current IP continues to disburse funds as earned by Government until June 30, 2015;
    - **Tranches for ongoing projects:** Tranches for ongoing projects would continue to be transferred as projects are in need of new financing[25]:
        - **Outstanding tranches** total US$790M for ongoing projects to be covered by the current available cash balance and incoming donor contributions;
        - **The ARTF Monitoring and Supervisory Agents:** These two programs are a core part of the ARTF Administrator's fiduciary and quality monitoring framework and as such will have to have sufficient financing to continue.
    - **New projects:**
        - Projects must meet the following conditions:
            - MoF must have already requested financing for these projects/covered under the previous FS;
            - The project objectives must be aligned with the *Realizing Self -Reliance* paper;

[25] This includes Rural Roads, Capacity Building for Results, SEHAT and Justice Services Delivery.

- The project must be in preparation or be ready to immediately start preparation to move towards approval;
- This results in three projects that would move forward under the interim arrangement to be delivered before or immediately after June 21, 2015:
    - Additional financing: The ongoing On Farm Water Management (US$45 million);
    - Additional financing: The ongoing Irrigation Rehabilitation and Development (US$70 million);
    - New project: Higher Education (US$50 million).
- The Administrator would reconfirm MoF's support for this select set of projects and ask, as per normal procedures, that the ARTF Management Committee, where MoF is represented, approves all technical project proposals.
- **Public Financial Management:** The next phase of the Public Financial Management Reform project (PFMR III) -- this serves as a backbone to the ARTF program and the ARTF program cannot run with integrity and accountability in the absence of this critical technical assistance project. Under the interim arrangement, <u>the Administrator would proceed with preparing the new PFM III project with the understanding that this project would be prioritized for financing under the new Financing Strategy</u>. The project would have to be approved by November 2015 at the latest to take over from the current PFMR II that ends December 31, 2015.

ANNEX VIII
REVIEW OF FY1391-1393 USE OF FUNDS

This annex provides an overview of the use of funds under the previous ARTF Financing Strategy FY1391 to 1393. The following outlines commitments and disbursements for each of the ARTF financing modalities and gives a short overview of new initiatives introduced over the last three years.

i. ALLOCATIONS

As outlined in table 9 the ARTF allocated[26] a total of US$2.33 billion to investments and recurrent costs from FY1391 to 1393. This includes **a total of US$1.5 billion for new investment projects**, including health, education, infrastructure, agriculture, capacity building and reforms, urban and rural development. A full outline of allocations for new and ongoing investment projects can be found on page xx.

Under the Recurrent Cost Window a total of US$786 million was allocated to government in support of its civilian operating budget during the same period. This includes US$450 million for baseline financing, US$235 million for the Incentive Program and US$101 million for the new Operations & Maintenance Facility.

While the FY1391-1393 had originally outlined allocations around US$3.3 billion in total, the actual total of US$2.2 billion comes in at about 33 % lower than projected three years ago. As noted in the earlier Financing Strategy, there is always an element of over-programming in the Financing Strategy to ensure room for delays and cancellations, consequently approximately 30% over programming is planned for. Differences between projections and actuals are therefore to be expected. This is a normal approach adopted within the World Bank, where overprogramming usually averages 25-35 %.

Two reasons in particular affected the allocation levels: (i) A Portfolio Performance Review was carried out in early 2013 by the World Bank and Ministry of Finance. A clear lesson coming out of this review was the need for enhanced project readiness at the time of approval as projects otherwise risk facing significant delays in the implementation phase. The delivery of several projects was therefore postponed from FY1392 to FY1393; and (ii) The FY1393 allocations were greatly affected by the prolonged election period. Government and line ministries were focused on the impact of the election process and World Bank staff had difficulties operating on the ground due to heightened security risks. The majority of the ARTF's planned investment pipeline for FY1393 was therefore postponed till FY1394.

It is important to note that the Financing Strategy is not a fixed allocation but rather a tool to provide better predictability in sector allocations and amounts. The actual implementation of the Financing Strategy depends entirely on the capacity within ministries to absorb and implement projects, readiness of projects, donor contributions, as well as other externalities outside the control of Government.

TABLE 9: ARTF Allocations FY1391-1393

[26] An allocation refers to funding that is legally committed for a project or activity in a legal agreement between the Government of Afghanistan and the World Bank as the ARTF Administrator.

Allocations	1391	1392	1393	Total
Investment Window:	467,500,000.00	492,320,000.00	580,500,000.00	1,540,320,000.00
Recurrent Costs Components:				
Baseline	175,000,000.00	150,000,000.00	125,000,000.00	450,000,000.00
IP	50,000,000.00	24,100,000.00	160,800,000.00	234,900,000.00
O & M		32,000,000.00	69,100,000.00	101,100,000.00
Total RC	**225,000,000.00**	**206,100,000.00**	**354,900,000.00**	**786,000,000.00**
	.			
Total	**692,500,000.00**	**698,420,000.00**	**935,400,000.00**	**2,326,320,000.00**

ii. DISBURSEMENTS

A total of US$1.78 billion was disbursed from FY1391 to 1393. This includes US$1.09 billion from the Investment Window. Table x in annex 1 outlines disbursements by project in the investment portfolio. Project disbursements happen at the project level, independently of new allocations. While an ongoing project might not receive an allocation during a given fiscal year, it continues to disburse.[27]

Under the Recurrent Cost Window a total of US$690 million was disbursed, including US$500 million in baseline financing, US$115 million under the IP and US$45 million under the O&M Facility.

TABLE 10: ARTF Disbursements FY1391-1393

Disbursed	1391	1392	1393	Total
Investment Window	256,140,479.16	424,390,775.92	409,442,758.51	1,089,974,013.59
Recurrent Costs Components:				
Baseline	225,000,000.00	150,000,000.00	125,000,000.00	500,000,000.00
IP	-	74,100,000.00	41,200,000.00	115,300,000.00
O & M		32,000,000.00	12,900,000.00	44,900,000.00
TMAF			30,000,000.00	30,000,000.00
Total RC	**225,000,000.00**	**256,100,000.00**	**209,100,000.00**	**690,200,000.00**
Total	**481,140,479.16**	**680,490,775.92**	**618,542,758.51**	**1,780,174,013.59**

iii. Donor Contributions

[27] The term “allocation” refers to the transfer of new funds from the ARTF to ongoing or new projects committed in legal agreements between the World Bank and the Government. The term differs from disbursements, which happen at the project level, independently of new allocations. While an ongoing project therefore might not receive an allocation during a given fiscal year, it can still continue disbursing from allocations made during previous fiscal year(s).

Donors pledged a total of US$2.9 billion for the ARTF Financing Strategy FY1391-1393. As of September 30, 2014, US$2.1 billion had been paid in by 19 different donors. This constitutes 72 % of the pledged funds. The large majority of the outstanding pledges are expected to be paid in during the coming three months, i.e. by the end of FY1393, December 21, 2014. October to December is traditional the peak season for donor contributions to be paid in to the ARTF.

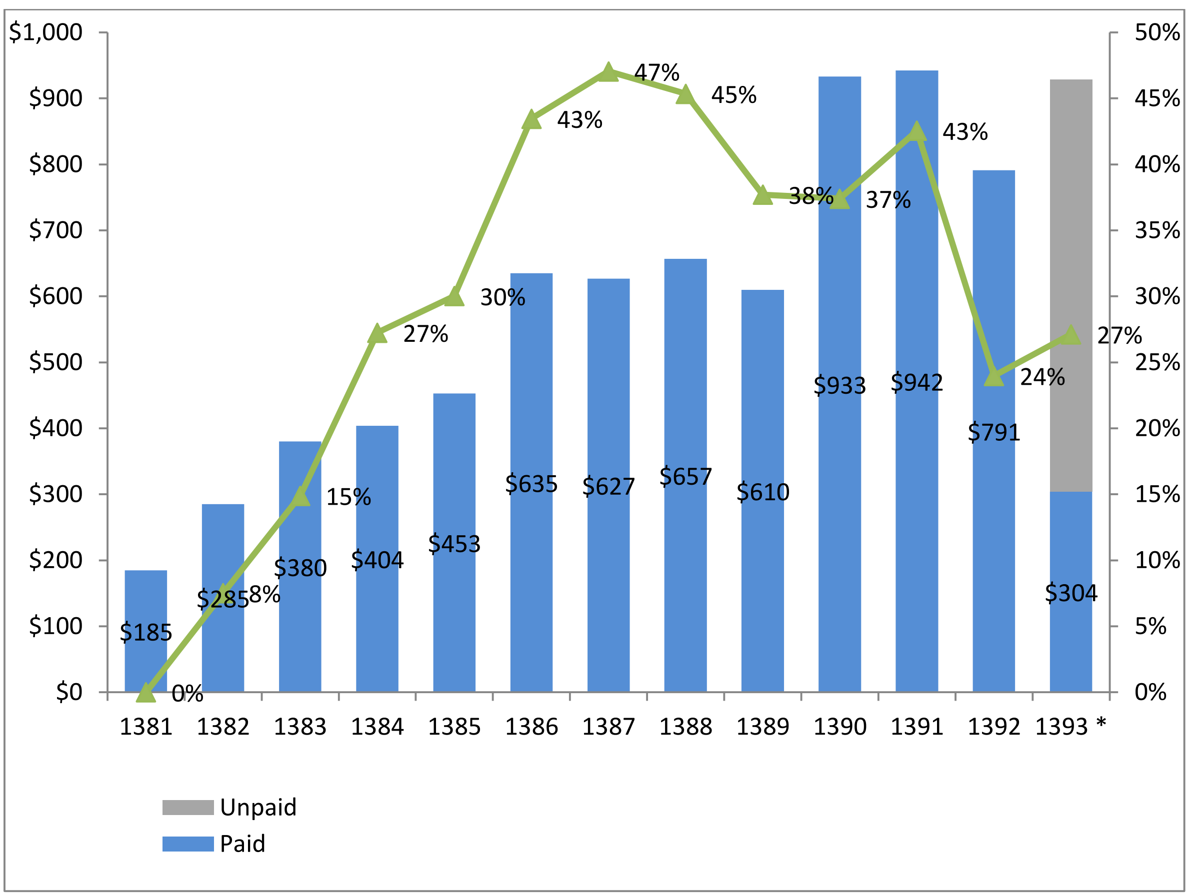
The ARTF Administrator is, however, expecting a difference between pledged funds and total paid in funds by the end of FY1393 as a result of some donors reallocating part of their pledge from the "core ARTF pledge" towards the Ad Hoc Payments mechanism in support of the government's fiscal gap.

TABLE 11: Donor Pledges and Paid-In Funds FY1391-1393

1391		1392		1393		1391-1393	
Total Pledges	Paid-in	Total Pledges	Paid-in	Total Pledges	Paid-in	Total Pledges	Paid-in
1005.01	942.20	916.69	791.00	1011.49	354.70	2933.19	2087.89

Table x below outlines total donor contributions per year since the establishment of the ARTF in SY1381. As can be seen, donor contributions have increased significantly since SY1389, while donor preferencing has gone down to around 27 % expected for FY1393.

TABLE 12: Donor Contributions 1381-1393



iv. Cash Flow

The ARTF cash flow budget in Table x outlines the cash balance in actuals as it has developed by year during the FY1391-1393 Financing Strategy. It provides an overview of sources of funds, i.e. donor contributions, as well as the use of funds, i.e. the allocations made for each of the ARTF windows (Recurrent Cost and Investment Windows) and modalities (Incentive Program and Operations and Maintenance Facility).

The FY1393 Q4 is tentative but allows a projection of the closing FY1393 balance and the potential carry-over into FY1394 and the new Financing Stratey.

TABLE 13: ARTF Cash Flow Budget

Sources/Uses of Funds	1391 (Actuals-in million)	1392 (Actuals-in million)	FY1393 (Actual as of June 30, 2014)	End of FY1393 (Projected in million)
Sources of funds:				
Carry-over from previous year	$500.00	$656.00	$641.17	$641.17
Donor Contributions	942.00	790.99	354.69	881.15
Total Sources of funds	**$1,442.00**	**$1,446.99**	**$995.86**	**$1,522.32**
Uses of Funds (Allocations):				
Recurrent Cost Window (Base)	$175.00	$150.00	$125.00	$125.00
Recurrent Cost Window (Incentive Program)	$22.50	$177.50	$150.00	$150.00
O & M	$0.00	$32.00	$69.10	$88.00
Recurrent Cost Window Total	**$197.50**	**$359.50**	**$344.10**	**$363.00**
Investment Window Allocations	$565.50	$442.32	$630.50	$975.00
Monitoring Agent	$23.00	$4.00	$12.00	$12.00
Total allocations out of parent account	**$786.00**	**$805.82**	**$986.60**	**$1,350.00**
Surplus / (Deficit) balance :	**$656.00**	**$641.17**	**$9.26**	**172.32**

PROJECT COMMITMENTS/DISBURSEMENTS FY1391-1393

Project Name	1391		1392		1393	
	Committed	Disbursed	Committed	Disbursed	Committed	Disbursed
Second Public Financial Management Reform Project	13,000,000.00	8,888,091.49		17,844,365.43		11,733,788.07
Justice Service Delivery Project - PPG		1,447,610.12		(848,368.93)		-
Afghanistan Justice Service Delivery Project	40,000,000.00	5,742,996.82		2,148,248.85		1,122,907.10
Afghanistan Rural Access Project	107,000,000.00					21,972,113.47
Afghanistan Second Skills Development Project (PPG)	500,000.00			436,440.71		57,081.95
National Horticulture and Livestock Productivity Project			50,000,000.00	11,586,366.89		12,178,472.10
Kabul Municipal Development Program			5,000,000.00	2,856,136.15		-
Afghanistan Resource Corridor Project			2,700,000.00	600,000.00		717,328.06
Naghlu Hydropower Rehabilitation Project PPG			4,970,000.00			1,000,000.00
Afghanistan Agricultural Inputs Project			74,750,000.00	5,126,344.17		1,412,791.75
System Enhancement for Health in Transition Project (SEHAT)			100,000,000.00	15,000,000.00		35,374,013.28
Higher Education System Improvement Project (PPG)			4,900,000.00	1,000,000.00		1,762,138.35
Non Formal Approach to Training, Education and Jobs in Afghanistan (NATEJA)					15,000,000.00	1,000,000.00
CASA-1000 Community Support Program					40,000,000.00	-
Kabul Municipal Development Program (KMDP)					110,000,000.00	6,000,000.00
Kabul Urban Transport Efficiency Improvement Project					90,500,000.00	5,000,000.00
Rehabilitation of Naghlu Hydropower Plant				2,818,574.75		
Management Capacity Program		522,746.46				
National Solidarity Program		(1,247,310.56)				
Kabul-Aybak/Mazar-e-Sharif Power Project		3,746,598.99		7,449,879.84		
Horticulture and Livestock Program		9,536,470.50		4,615,862.70		
Kabul Urban Reconstruction Project		819,103.22		(1,853.96)		
Justice Sector Reform Project		1,287,788.93				
Strengthening Higher Education Project		769,478.78		(173,154.42)		
Kabul Urban Roads Improvement Project		961,656.23				
Water Resources Development Technical Assistance Project		720,441.77		1,226,903.05		
Skills Development Project	9,000,000.00	932,011.83		5,099,053.69		1,392,340.40
Second Education Quality Improvement Program	148,000,000.00	26,685,738.61		60,712,405.13	125,000,000.00	51,693,831.18
Afghanistan Rural Enterprise Development Project (AREDP)		686,244.80		3,541,489.93		
Third Emergency National Solidarity Project	150,000,000.00	153,364,251.96	250,000,000.00	229,303,800.35	200,000,000.00	198,595,905.47
On Farm Water Management project		1,600,267.67		6,815,446.11		6,674,573.52
Improving Agricultural Inputs Delivery		728,767.97		748,482.88		(15,085.11)
Capacity Building for Results Facility		38,269.25		6,167,664.62		4,565,243.92
Irrigation Restoration and Development		2,500,000.00		4,540,906.66		5,021,380.41
Power System Development Project		16,921,877.11		13,406,087.43		11,419,260.78
National Emergency Rural Access Project		13,917,581.75		8,412,494.72		
Strengthening Health Activities for the Rural Poor (SHARP)		5,569,795.46		13,957,199.17		(42,788.06)
Total investment window	**467,500,000.00**	**256,140,479.16**	**492,320,000.00**	**424,390,775.92**	**580,500,000.00**	**378,635,296.64**
Recurrent & Capital Costs Component	**225,000,000.00**	**225,000,000.00**	**322,000,000.00**	**256,100,000.00**	**129,000,000.00**	**174,100,000.00**
Grant total	**692,500,000.00**	**481,140,479.16**	**814,320,000.00**	**680,490,775.92**	**709,500,000.00**	**552,735,296.64**