

## ARTF Donor Committee Meeting 19 March 2008

### Administrator's Discussion Note: Preferences & the investment window

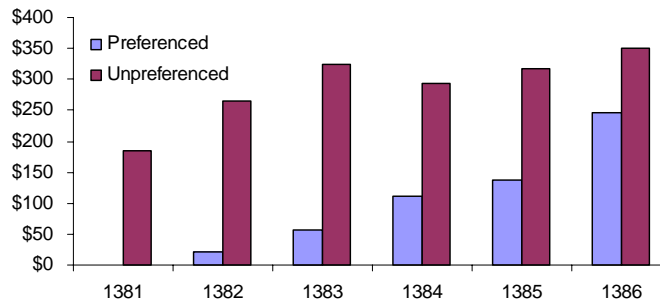
**Background:** In response to concerns raised by both Government and donors, this brief background note aims to set out some of the facts and figures around the system of 'preferencing' in the ARTF. It is intended to stimulate discussion at the Donor Committee Meeting, 19 March 2008.

1. Preferences make up the bulk of financing that has flowed to the ARTF's investment portfolio. In total, eleven donors have made preferenced contributions to ARTF worth \$571 million, accounting for 95% of all investment commitments made since SY1381. Preferences have increased year on year in absolute terms and also as a percentage of the total. Thus, the target set by the Performance Assessment Matrix for a reducing share of preferenced contributions – in order to meet the needs of the Government for greater flexibility and ownership of the budget process - is not being met.

2. Preferences are consistent with the ARTF investment strategy pursued by the Management Committee: to allocate funds to existing Government National Priority Programs, such as the National Solidarity Program (NSP) and the new program for National Justice Reform.

3. Preferences are *additional*. In other words they do not replace un-preferenced contributions. As indicated in table i, both preferenced and un-preferenced contributions are increasing year on year (although preferences at a faster rate). Preferences facilitate donor accountability towards domestic constituencies which mobilizes greater resources for Afghanistan.<sup>1</sup>

**Table i. Donor contributions (\$m)**

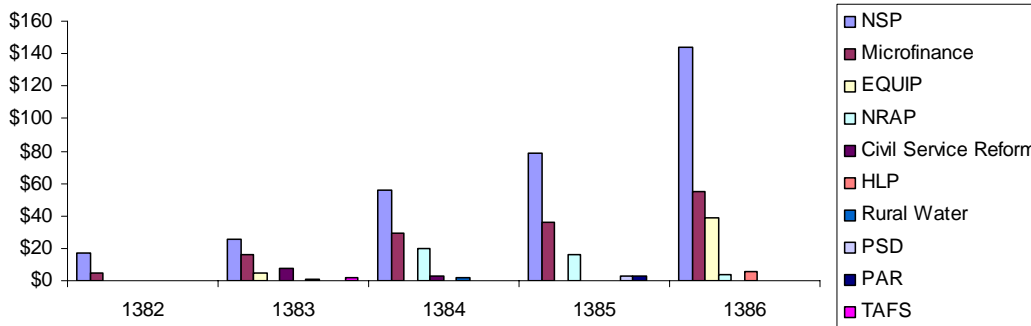


4. Table ii illustrates the allocation of preferences across the investment portfolio. 95% of total preferences received have been for four national programs: NSP, Microfinance for Poverty Support, EQUIP and National Emergency Rural Access Program (NRAP). The ARTF investment portfolio is therefore oriented towards poverty reduction.

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<sup>1</sup> It should also be recognized that all funds are fungible. Therefore preferencing does not impact fiscal space. Rather it impacts prioritization and flexibility for expenditure planning.

**Table ii. Preferences by project (\$m)**

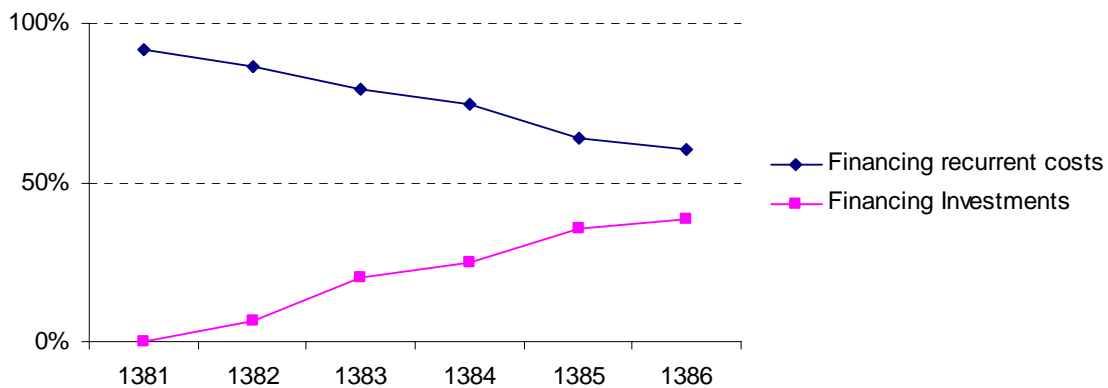


5. NSP and microfinance have been the two national programs that have received preferred contributions consistently since SY1382. In fact the national microfinance program was initiated through the ARTF and has now been able to scale up significantly, also with the support of the International Development Association (IDA). Preferences have enabled NSP to scale up significantly, with major year-on-year increases in the contributions. Both NSP and microfinance are rapidly disbursing national programs that are able to demonstrate impact and effective utilization of funds.

6. The government’s budget sets the level for ARTF investment allocations. Preferences do not set the level of allocations by ARTF program. While the Administrator may accept preferences over and above budget levels for a program, the Management Committee will not allocate all of those in one year – preferences will be rolled over to cover that program’s budget in the following year.

7. The Administrator monitors the levels of preferences by donor and puts forward suggestions for changes in the framework if necessary. The ARTF framework does not allow for a donor to make preferences greater than half of its total contribution for any one fiscal year. However, in the past two years, once un-preferenced contributions have been received sufficient to fund the recurrent window, donors have been allowed to contribute more preferred funds. This has both increased the total level of contributions and the proportion of preferred funds in the ARTF.

**Table iii: Share of Recurrent & Investment Windows as % of total disbursements**



8. Given increasing overall contributions and (almost) static recurrent window levels the investment window has grown as a percentage of the overall use of funds. In SY 1386, overall investment allocations to the investment portfolio are estimated at around \$450 million<sup>2</sup> driving portfolio disbursements to around the same level.

9. At the same time, in SY 1386 ARTF donors have contributed significantly more unpreferenced funds that were needed to cover the recurrent window. This has allowed the Government to utilize un-preferenced funds for its other priority needs. Provided total contributions remain at current levels with constant or declining share of preferences, the Government will be able to exercise a greater degree of discretion over its prioritization in the future. This sets the stage for a greater degree of policy & strategy discussion between donors and government around investment portfolio priorities. This is also in line with the ANDS policy towards aid effectiveness which argues for greater government discretion over the allocation of funds.

### **Looking ahead**

10. With the completion of the ANDS this year, donors and government have an opportunity to agree a common set of development priorities. Looking ahead, the ARTF strategy should align with the priorities set out in the ANDS and provide donors a mechanism to support these priorities through the core budget.

11. Arguably, this understanding, if translated through the investment portfolio, reduces the need for donor preferences. If donors can “buy into” the ARTF strategy, unpreferenced funds will line up behind it, with the Administrator and Management Committee ensuring the strategy is pursued and monitoring its outcomes. This could fulfill both donors’ needs for visibility and accountability as well as government need for flexibility in managing the ARTF cash through the annual budget cycle thereby increasing its ownership of the policy-making.

12. ARTF Donor Committee meetings are a possible forum for agreement around the future ANDS priorities for ARTF financing.

### **Possible points for discussion**

- What are the main reasons donors make preferences? Is it a concern over fiduciary or public finance management or is it for greater accountability for the funds?
- How can preferencing be reduced in time? What can government do to provide donors assurances over distribution of funds?
- Does the ANDS offer an opportunity to align investment allocations with the national development strategy?

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<sup>2</sup> The GoA 1387 budget as it pertains to the ARTF will be discussed with MoF and the MC.