

LESSONS FROM ENVIRONMENTAL POLICY LENDING

Messages for Bank Management



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The Independent Evaluation Group has produced a Learning Product on the Bank's experience with environmental policy lending. The report does not evaluate the instrument or portfolio, but rather offers lessons based on experience. Though the primary audience of the report is Bank operational teams working on environmental policy lending, the report also offers a number of findings relevant to Bank management, including in the Environment and Natural Resources Global Practice and in Country Management Units.

The Development Policy Financing Instrument and Sectoral Policy Lending

Environmental policy lending offers a mechanism for supporting a wide range of policy reforms. Environment DPOs are frequently multi-sectoral in nature, including policy actions in energy, water, agriculture, transport, industry, and others, especially in climate change and green growth operations. Such operations can serve as an entry point for policy reform in these sectors, and can serve as a platform for inter-sectoral cooperation. The multi-sectoral nature requires a certain degree of complexity in design and counterparts, but there can also be disadvantages from program designs that are too broad, with higher coordination challenges and implementation risks.

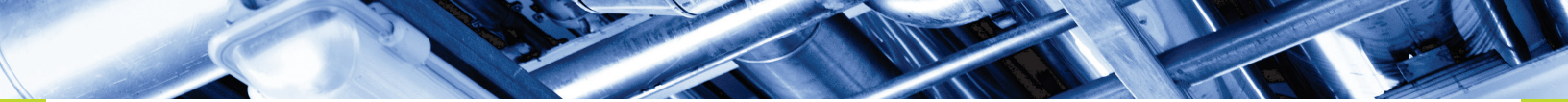
There are particular circumstances where the DPF instrument is most effective.

- DPF is a policy lending instrument; it is most effective when policy issues are the main barrier.

If policy issues are not the main barrier to improving environmental outcomes, then other instruments are likely to be more effective.

- Effective policy lending requires a significant degree of country and sector knowledge, especially institutional knowledge, as well as strong and positive existing relationships with policymakers.
- Policy lending can be more effective when used in combination with other instruments – for example analytical work can perform diagnostics and identify policy reforms, prior investment lending can help to build relationships and capacity, technical assistance and parallel or subsequent investment lending can help with implementation.
- There are risks in using policy lending as emergency response – while client governments may well seek rapid budget support, it is difficult to prepare significant reforms under emergency circumstances, and any prior actions selected may be either minor in impact or ones in which the Bank adds little new value.

Environmental DPF can be different from other sectoral policy lending. As noted above, environmental policy reforms often involve reforms across multiple sectors. The DPF instrument can be particularly advantageous for environmental issues, because environmental ministries and agencies are often relatively weak, so raising issues to senior decision-makers especially in finance and planning agencies can be critical.



The Bank should be clear that sector DPF is still general budget support. Though policy dialog may lead client governments to shift spending priorities towards needed areas including environmental agencies, problems can be created if budget support financing is earmarked directly to line ministries or agencies. Earmarking can disrupt the relationship between the finance ministry and line ministry by placing the Bank in between the two, and earmarking of Bank financing can also undermine the Bank's approach to environmental and social risk management for policy lending, which focuses on the supported policies rather than on the financial support. Instead, the benefit to line ministries comes not from additional funding, but rather from the ability to use the Bank to help promote important policy priorities.

Designing policy lending operations

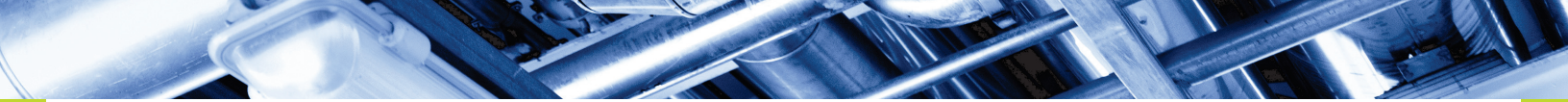
Task teams and managers should have a clear political theory of change. Attention is usually paid to the technical theory of change—how particular policy reforms will lead logically to desired policy outcomes. But there should also be a clear underlying political theory of change—how the presence of a Bank DPO will help influence which policy reforms are implemented or how, or when they will occur. That is, the additionality of the Bank DPO should always be sought and determined in internal review meetings.

Results frameworks could be improved. IEG informally uses criteria for assessing the quality of prior actions that considers *relevance* (will the policy action achieve the desired result?), *criticality* (will the precise policy action achieve significant results or will many subsequent steps be required?), *additionality* (how is the Bank adding value?) and *measurability* (how do we tell if the action was completed or not?). Monitoring and evaluation systems for environmental DPOs have often been weak. Objectives are sometimes imprecise or unclear, and indicators often did not provide a direct or adequate reflection of the objectives or sub-objectives with which they were associated. Results frameworks sometimes end up measuring processes rather than results or

impacts. Effective utilization of monitoring and evaluation is rare; systems are used largely for reporting purposes and tracking progress on triggers rather than for identifying problems and assessing the need for course correction. Results frameworks by necessity focus on the outcomes that can be observed by the time of evaluation, but this means that monitoring and evaluation systems generally fail to assess longer term impacts. Management could consider developing an additional mechanism to assess such impacts.

Analytical work and technical assistance play a key role in the effectiveness of policy lending. There is universal agreement that relevant analytical work is critical in developing policy strategy, and that technical assistance is often needed to support development and implementation – yet there are cases where staff believe the level has been inadequate. The absence of technical assistance is a common cause behind unsuccessful policy lending operations. Key constraints have been: limited budget resources, especially as trust funds have been exhausted and not replaced; challenges in timing so that analytical work is not available in advance of policy development; unwillingness of governments to borrow for technical assistance; and a perceived lack of incentives for staff to focus on analytic work in an institution driven by loans and disbursements.

Working with other development partners on DPOs has pros and cons. Many policy lending operations have been co-financed by other partners, especially bilateral donors. This has tradeoffs: harmonization and donor coordination is valuable, other partners can offer things that the Bank cannot, especially grant funding for technical assistance, and reducing client transaction costs is desirable. But harmonization can also add complications, especially when other agencies have different views about the underlying instrument, for example in terms of what types of conditionalities should be included, and on how hands-off the development partners should be. In some cases the Bank has been initially valued by other partners for its convening role, but then seen as more of a burden



during implementation, in particular because of the Bank's requirement to go back to the Board for each new stage in a programmatic series.

Institutional issues

Staffing composition and expertise would benefit from management attention. Several staff raised the issue of mismatches in expertise between Bank staff with “traditional” environment backgrounds and the skillsets needed for environmental policy lending (e.g., environmental economists, experience in environmental policy, regulation, etc.). Some operations have had TTLs

or other staff with no prior experience in DPF, which adversely affected implementation. This may be relevant for GP training and staffing strategies.

Documentation quality is often poor. Program documents are often vague in describing the underlying theory of change, and often do not describe the contents of the reforms being supported—for example they might report a new energy law, but not indicate the contents of the law or what is changed. ICRs often report only on the completion of particular outputs, and may not address even the initial results and impacts that have occurred by the time of evaluation.

The full report is available at <http://ieg.worldbankgroup.org/learning-envidpo>