

LESSONS FROM ENVIRONMENTAL POLICY LENDING

When to choose policy lending



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The Independent Evaluation Group has produced a Learning Product on the Bank's experience with environmental policy lending. Among other topics, the report looks at the context in which policy lending can be most effective.

Policy lending can be a powerful instrument for influencing reform efforts

When policy issues are the main barrier to improving environmental outcomes. Many environmental challenges include governance, public good, and externality issues where policy interventions are needed to achieve efficient outcomes. But if the main barriers are those of institutional capacity or enforcement, or the need for direct financing, then policy lending may not be the best instrument.

For achieving multi-sectoral or sector-wide goals.

Most environmental management issues are multi-sectoral, crossing energy, water, agriculture, urban, industry, and transport sectors in addition to environmental management. The policy lending instrument offers advantages in its ability to offer a platform for influencing outcomes in these sectors through an environmental lens.

When the Bank has prior knowledge of the country and sector and strong institutional relationships.

Policy lending requires a substantial degree of technical knowledge in the country and sector, of political and institutional dynamics, and of institutional and personal trust. Policy lending can work better as part of a sequence where sectoral knowledge and engagement

with counterparts has been built up by prior activities. It is more difficult to start an environmental engagement with policy lending.

For issues that need attention from high-level decision makers, especially in finance and planning ministries.

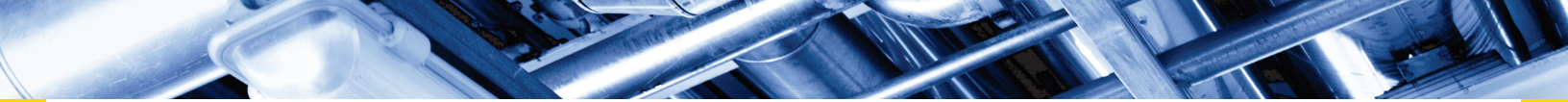
Environmental ministries are often politically or institutionally weak or have limited ability to implement large-scale reforms. The substantial budget support financing associated with policy lending helps to elevate critical environmental development issues to senior decision makers in finance and planning ministries.

An opportunistic approach to policy lending can pose risks

It is difficult to support significant environmental policy reforms under emergency circumstances.

Bank teams may favor policy lending operations in order to offer fast-disbursing budget support in the face of natural disasters or other shocks. But it is often not possible to prepare new substantial reforms in such circumstances; operations prepared rapidly have sometimes selected prior actions that are either relatively minor, or that have already been completed or otherwise offer little ability for the Bank to influence. In such cases the impact of the operation on policy reform is modest, and the benefit largely limited to the fiscal transfer.

Policy lending is often most effective when used in parallel or coordination with other instruments. Prior investment lending can help to build the relationships, trust, political and technical knowledge of the country and sector, and institutional capacity that are needed to



support a policy dialog and reforms. Parallel or subsequent investment lending can help to support implementation of policies.

Champions with an appetite for reform can provide an opportunity for policy lending, even when the existing base is weak. But this approach can be risky, and vulnerable to the loss of particular champions.

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