

CENTRE FOR DISASTER PROTECTION

POLICY BRIEF

IDA19: A VITAL TOOL FOR MANAGING CRISIS RISK



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The Centre for Disaster Protection works with developing countries to find better ways to manage the risks of disasters and to deliver earlier, more cost-effective support for people when disasters occur. One element of the Centre's work is influencing global policy on financing responses to disasters. This series of papers was commissioned to provide analysis, ideas and recommendations for the 19th replenishment of the International Development Association. The series comprises Discussion Papers and Policy Briefs, all available at disasterprotection.org.

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● SUMMARY

Countries are increasingly vulnerable to natural hazards, and when disasters strike millions of people are driven deeper into poverty. Between 1998 and 2017, climate-related and geophysical disasters killed 1.3 million people and affected 4.4 billion more. Those living in the poorest countries are on average six times more likely than those in rich nations to be injured, lose their home, be displaced, or require emergency assistance. Climate change threatens to push an additional 100 million people into extreme poverty by 2030, and 720 million more by 2050 unless something is done. Half of those most affected by natural hazards live in fragile and conflict-affected states.

The International Development Association (IDA) is playing a vital role in helping low-income countries manage the risk of crises. The forthcoming IDA replenishment (IDA19) is an opportunity to increase the impact and efficiency of IDA's contribution to crisis risk financing and management. It could do this by taking the following steps:

1. Reset the incentives for client governments to invest in prevention and preparedness. Specifically:

- Require IDA to report formally on how analysis of crisis risk informs its investment strategy and to account for its contribution to risk reduction and preparedness.
- Make finance for crisis prevention and preparedness available on the same terms or better as finance for crisis response.
- Scale investment in preparedness, focusing on building the delivery systems needed for a response when a crisis strikes. Meanwhile, increase the coverage of shock-responsive social protection systems and accelerate testing of shock-responsive basic services.

2. Work with development insurers to deliver early and predictable finance to drive an early response. This would enable IDA to move away from its current approach, which relies largely on post-crisis budget reallocations, and towards one that finances risk more efficiently. IDA should focus on brokering 'development insurance'—that is, institutions that are based on insurance principles, but are used to deliver specific development objectives and financed on a concessional basis. It should also seek to connect financing to prevention and preparedness measures and monitor risk financing arrangements to ensure they deliver the maximum development impact at the lowest cost.

3. Reform the Crisis Response Window (CRW).

The CRW is an important innovation, but it suffers from limitations in design and operation. Specifically:

- Increasingly reserve the CRW for responses to large crises and those that are inherently difficult to predict and use other instruments to finance more predictable crises.
- Improve transparency and operational performance.
- Review eligibility criteria to allow earlier responses to slow-onset crises such as drought and famine.

4. Commission a review of IDA's existing risk financing tools, drawing on independent expertise.

Such a review should examine the coherence and cost-effectiveness of IDA's approach to crisis risk management and financing. Particular attention should be paid to how existing approaches deliver for the poorest, and how the IDA risk financing architecture relates to the wider global architecture.

SECTION 1



Building a new maternity unit at Magunga Health Centre, Kenya, 2009. Image: DFID/Caroline Irby

● INTRODUCTION

Disaster risk management is fundamental to reducing poverty. Between 1998 and 2017, climate-related and geophysical disasters killed 1.3 million people and affected a further 4.4 billion. People in the poorest countries are on average six times more likely than those in rich nations to be injured, lose their home, be displaced, or require emergency assistance (CRED and UNISDR 2018). Vulnerability to natural hazards is increasing: climate change alone threatens to push a further 100 million people into extreme poverty by 2030 (Hallegatte et al. 2016). Fragility, conflict, and violence exacerbate these risks—in fact, more than half of people affected by natural hazards live in fragile and conflict-affected states (Ghesquiere 2016). After a crisis, the social and institutional capacities needed in those states to mitigate risks and respond are reduced.

This policy brief aims to inform the forthcoming replenishment of IDA, the World Bank’s main source of finance for grants and loans to low-income countries. In doing so, it draws on a series of five commissioned papers—Allan and Paterson (2019), Clarke and Dercon (2019),

Paterson (2019), Spearing (2019), and Vaughan and Hillier (2019) — and it asks how IDA could be strengthened to deliver better results for those living in extreme poverty.

IDA is replenished every three years. The last replenishment (IDA18), covering the period 2017-20, was the largest in IDA’s 56-year history, mobilising US\$75 billion. IDA18 placed risk management at its core, recognising the importance of increasing the resilience of the poorest people at a time of growing environmental, economic, and political risks.

This policy brief argues that the focus on crisis management and financing should be maintained and deepened in IDA19. It commends the pioneering role that IDA has played in scaling investment in building resilience and in supporting low-income countries when crises strike. However, it identifies a number of strategic and operational challenges that should be addressed if IDA is to fulfil its potential as a major financier of crisis risk.

● CRISIS FINANCING: WHY IS IT IMPORTANT FOR IDA19?

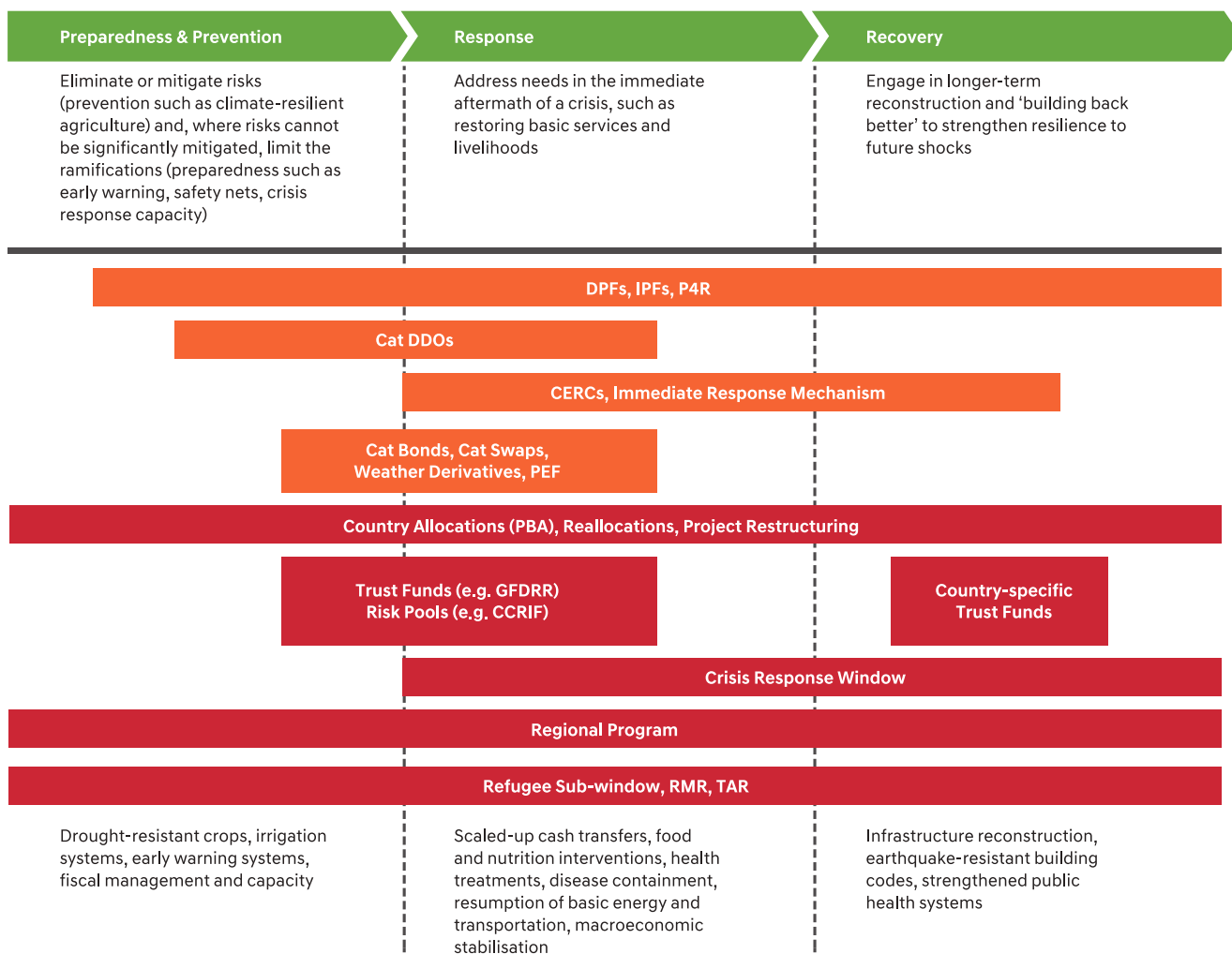
Crises deepen poverty and threaten development investments. For that reason, crisis prevention and preparedness are a crucial part of poverty eradication. Estimates for 89 countries find that if all natural disasters could have been prevented in 2017, the number of people in extreme poverty—that is, those living on less than US\$1.90 a day—would have fallen by 26 million (Hallegatte et al. 2017). In the same year, climate shocks were one of the leading causes of acute food crises and malnutrition, affecting 59 million people in 24 countries in Africa alone (FAO et al. 2018).

Securing value from investments in international development means protecting them from the effects of natural hazards. Millions of dollars of investment in schools, hospitals, and roads can be wiped out in hours by

floods and earthquakes if development planning does not take disaster risk into account. The impact of extreme natural disasters is equivalent to a global US\$520 billion loss in annual consumption.

The growing recognition of the intersection between poverty and crisis risk has been reflected in the evolution of IDA, which has developed a sophisticated set of instruments to finance and manage crisis risk (see Table 1). IDA18 was particularly ambitious in this regard, with a significant increase in the volume of funds allocated to key risk financing solutions, such as the Crisis Response Window (CRW), leaving the World Bank with a wide range of funding sources and delivery mechanisms to address crisis across a spectrum, from preparedness and prevention through response and recovery.

Table 1: CRW within the broader World Bank toolkit for addressing crisis



- Instruments / Tools
- Sources of Financing

Sources: Spearing (2019), adapted from IDA (2018)

Note: CAT-DDO = Catastrophe Deferred Drawdown option; CCRIF = Caribbean Catastrophe Risk Insurance Facility; CERC = Contingent Emergency Response Component; DPF = Development Policy Financing; GFDRR = Global Facility for Disaster Reduction and Recovery; IDF = Institutional Development Fund; P4R = Program-for-Results; PBA = Performance Based Allocation; PEF = Pandemic Emergency Facility; TAR = Turn-Around Regime

Particularly notable in IDA18 was the significant uplift in the allocation to the CRW, to US\$3 billion from US\$1 billion in IDA16. Also notable was the launch of the Pandemic Emergency Facility (PEF) and the introduction of the refugee sub-window.

The growing breadth and diversity of crisis financing instruments present both challenges and opportunities. Typically, multiple instruments are used to finance the

response to specific events, 'blending' different sources of finance to meet needs. The growing number of instruments can make it difficult for stakeholders, including within the World Bank, to navigate the options. Growing awareness of this challenge resulted in the creation of the Global Crisis Response Platform (World Bank 2018), a mechanism intended to enhance the capacity of the World Bank to anticipate crises and ensure effective coordination across the institution as a whole.

SECTION 2



Floating through flooded villages
in Benin, West Africa, 2010.
Image: CARE/Loetitia Raymond

● IDA19 AND CRISIS FINANCING: AN AGENDA FOR ACTION

It is no longer a question of *whether* IDA should play a major role in enabling low-income countries to manage and finance different types of crisis risk, but *how* it should do so. This policy brief sets out four recommendations for changing the way IDA is used to manage and finance crisis risk.

Recommendation 1: Reset the incentives for client governments to invest in prevention and preparedness.

IDA is already doing a lot to help clients understand, manage, and finance the risks they face, but there is scope for it to make a much sharper distinction between the ways in which risks are anticipated, managed, and financed. The current design of much of IDA’s crisis financing tends to reinforce the idea that it is not possible to know (and therefore plan for) crisis risk. However, many crises are not surprises. They are known unknowns—that is, the likelihood of a particular event (such as a climate shock, earthquake, or epidemic) occurring in a particular country is known, as are the likely consequences and what could be done about them. Unknown is when such events might happen. Other crises are more of a surprise. They are *unknown unknowns*—

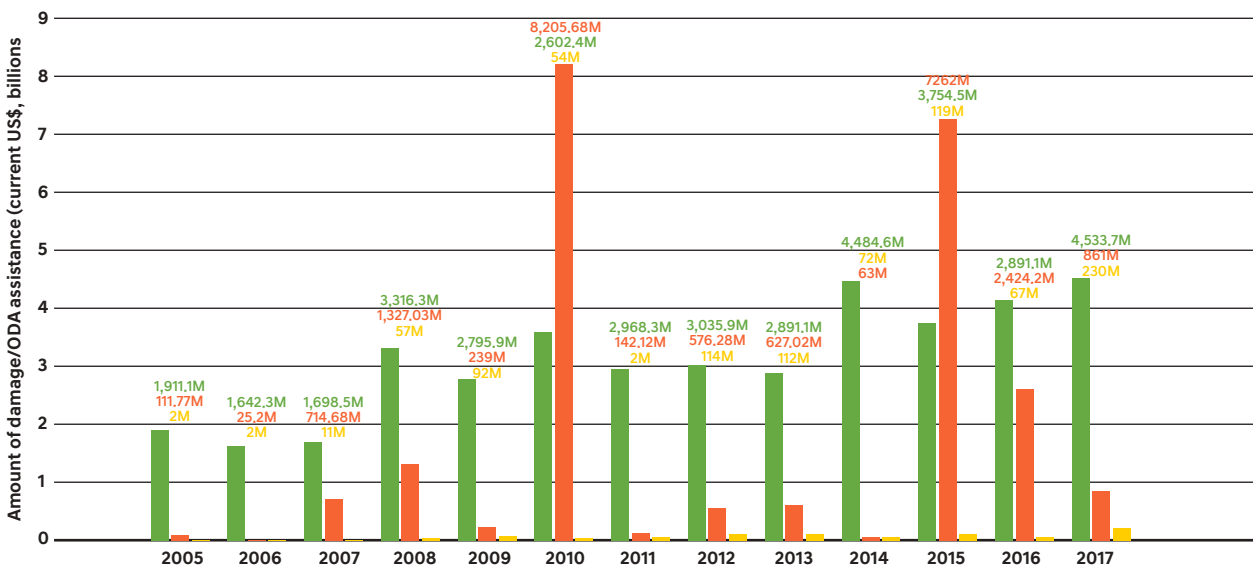
that is, the kind of crises that are very difficult to predict accurately. Examples are economic shocks, large-scale displacement, or ‘perfect storms’ of what should have been independent shocks previously thought impossible or remote.

Recommendation 1.1: Report formally on how analysis of crisis risk informs IDA’s investment strategy and account for its contribution to risk reduction and preparedness.

IDA has considerable capacity to support countries in analysing the risks they face from natural hazards and climate change, as well as their capacities to manage these risks. It has developed expertise as well in the design of projects to build resilience. It has also played a valuable role in brokering agreement on the ownership and governance of particular risks, such as pioneering the development of shock-responsive social protection systems.

IDA could and should do more of this work. Figure 1 shows that current levels of aid investment in prevention and preparedness remain very low, compared with the damage caused by natural hazards.

Levels of damage from natural hazards and of official development assistance (ODA): low-income countries, 2005-17



- Total ODA Emergency response
- Total damage from natural hazards
- ODA commitment to prevention and preparedness

Data from Centre for Research on the Epidemiology of Disasters, www.emdat.be; OECD/DAC.

Because of the significance of IDA in supporting public financing in low-income countries, it is particularly well suited to driving a scale-up in preparedness and prevention and overcoming the political disincentives that constrain investment there. At present, the quality of risk analysis is variable, and it is not always clear how it is being used by clients to guide investments and to protect the poorest people. Hardwiring such analysis into approval and scrutiny processes will be crucial.

Recommendation 1.2: Make finance for crisis prevention and preparedness available on the same terms, or better, as finance for crisis response.

Investment in preparedness remains particularly low despite growing evidence of the high rates of return of this type of investment. A recent study suggested that for every US\$1 invested in preparedness, the average return was US\$2.10, with some projects yielding returns of US\$18.70 (UNICEF/WFP 2015).

A country's IDA envelope is essentially an extension of the country's balance sheet. Investment in preparing for an uncertain event is unlikely to seem an attractive option, compared with investing in delivering immediate development returns, particularly if governments think they will be able to access additional 'free' resources through humanitarian aid or through the CRW without any requirements to contribute their own budget. It is perhaps no surprise, then, that while the CRW alone has financing of US\$3 billion over three years, the total amount of protection bought from crisis risk pools was only US\$56 million (Vaughan and Hillier 2019).

IDA19 is an opportunity to reverse these incentives by aligning the degree of concessionality for crisis preparedness and insurance-like contingent finance with that for crisis response funding. Such a change would incentivise governments to turn unmanaged unknown unknowns into proactively managed known unknowns. The Asian Development Bank provides one model of how this could be done. Its Disaster Risk Reduction Financing Mechanism focuses mostly on prevention, but it can fund some elements of preparedness (Clarke and Dercon 2019). IDA has already been approved to provide matching funding to countries for the Development Policy Loan with the Catastrophe Deferred Drawdown Option (Cat-DDO), which combines policy preparedness with contingent finance. Extending this eligibility to other combinations of preparedness and contingent financing, or setting up a separate Crisis Protection Window, would be useful.

Recommendation 1.3: Scale investment in shock-responsive social protection and test the development of shock-responsive basic services in IDA countries at highest risk.

There is growing experience with using social protection systems to build the resilience of those living in extreme poverty and with using these mechanisms to respond to major shocks. IDA19 is an opportunity to further increase the coverage of these systems, to review how they are financed, and to explore the potential applications of this approach to the delivery of basic services such as education, health, nutrition, and water and sanitation services.

Recommendation 2: Work with development insurers to deliver early and predictable finance to drive early responses.

Many of the risk financing instruments within IDA rely on a process of reallocating existing country or global funds to respond to crises when they happen, which undermines incentives to prevent and prepare for crises beforehand. Broadly speaking, this is an appropriate approach to last-resort financing for unknown unknowns—but better approaches are possible for known unknowns.

A mature set of development insurance institutions would be much better placed than development banks to deliver protection against known unknowns. Although the World Bank has experience delivering insurance-like products, it does not operate as an insurer. Development insurers should be able to manage this risk more cost effectively, as well as help to deliver the kind of transparency, scrutiny, and participation that will lead to more inclusive and broad-based benefits. Just as development banks have evolved over time to ensure that concessional loans and grants provided to countries achieve specific development objectives, so too a new sphere of ‘development insurance’ is emerging. It has the potential to deliver concessional

insurance-like protection that protects people and economies against shocks. The World Bank has played an important role in fostering institutions that could deliver this kind of protection—for example, the Caribbean Catastrophe Risk Insurance Facility and its counterpart in the Pacific, the Pacific Catastrophe Risk Insurance Company. In IDA19, it should commit to do more.

In the private sector, banks and insurers have a way of working in partnership—bancassurance—which allows each to play to their respective strengths. Learning from this model, IDA could help to build similar systems that support low-income countries by encouraging and financing informed demand for such services. In this role, IDA would focus on helping governments (and the public) to better understand risk and how it should be financed. Similarly, it would work with development insurers to ensure that products that finance protection against known unknowns are well understood and deliver fair outcomes for poor people at the lowest sustainable cost.

Growing the supply of development insurance would reduce the need to hold large volumes of IDA in reserve, while also guaranteeing that, if and when pre-agreed risks materialise, support will be available quickly and easily.

Recommendation 3: Reform the Crisis Response Window to maximise its comparative advantage and operational performance.

The CRW was designed to provide a pot of money to respond to economic shocks, public health emergencies, and natural hazards. The allocation for CRW in IDA18 was US\$3 billion. Box 1 summarises how the CRW has been used since it was introduced in 2010.

Box 1 The Crisis Response Window: Allocations, 2010-18

- US\$3.1 billion allocated across 24 crisis episodes;
- Allocations to crisis affected countries range from US\$1.5 million to US\$508 million;
- Grants and loans used to respond to drought (26 percent), earthquakes (26 percent), floods and storms (21 percent), public health crises (20 percent), and economic crises (7 percent).

Source: Spearing (2019).

Recommendation 3.1: The CRW should increasingly focus on responding to unknown unknowns. In the meantime, ensure that the sizing of the CRW is based on robust analytics.

Almost half (47 percent) of the CRW caseload relates to drought and floods, which recur largely in the same countries. Almost a third of CRW funding has been used to finance the shock-responsive component of established safety net systems (see Box 1). Finding alternative ways of financing this significant known unknown risk and pre-planned responses would allow the CRW to focus its resources on the unknown unknowns. For example, in Uganda the shock-responsive component of the IDA-financed social protection system is supported by a funded project component. While still using a reallocation approach, this arrangement has the advantages of encouraging a higher level of discipline in terms of anticipating potential demand and increasing certainty that sufficient funds will be available. A series of plans are made in advance about how unspent funds will be disbursed at the end of the year, ensuring that they will be reallocated efficiently.

Accelerating the shift away from using the CRW to manage known unknowns is important because it would be a more efficient way of financing this risk. The CRW does not behave as a true risk pool, relying instead on an allocation from IDA: funds can be reallocated in and out of the window, and may not always be available even for anticipated needs. For example, during IDA17 the CRW was depleted by July 2015 and not replenished until the following summer. In the intervening period, allocations remained sluggish despite demand—including the demand for support to drive the additional finance required to flex social protection systems in response to impending drought. Despite pre-planning, and the early warning, CRW commitments were delayed because of uncertainty about available funds (see Spearing 2019).

Currently, the CRW has a limited ability to forecast potential demand, raising the risk that funds are reallocated out of the CRW (as happened at the IDA Mid-Term Review in November 2018) because they were not spent down in the first 18 months. It is not clear, however, whether the judgement to reallocate the funds underspent is informed by an analysis of future risk.

The Global Crisis Response Platform could increase the capacity of the World Bank to analyse trends in crisis risk, which could, in turn, be used to inform the sizing and allocation of the CRW. Similarly, development of the Famine Action Mechanism (FAM) could inform longer-term planning for the long-term risk of drought. If there were a commitment to replenishing the CRW if finance levels fall below a certain threshold, the uncertainty surrounding the availability of funds could be overcome.

Recommendation 3.2: Improve transparency and operational performance.

It will be difficult to agree on the right division of labour among the CRW, other IDA mechanisms, and a broader set of risk financing instruments within the timeframe of one IDA cycle, but some operational issues should be resolved as a matter of urgency during IDA19, including increasing transparency and improving operational performance.

CRW funds can be used to respond to a variety of natural hazards once a government declares an emergency. Although CRW eligibility criteria have been defined in relation to natural disasters, economic crises, and public health emergencies, decisions on the size of contributions are confidential. For example, there is no published guidance in terms of the CRW's approach to burden sharing or its role as the donor of last resort. Therefore, it is difficult to know whether particular events will qualify for support and by how much. It is also difficult to track

which projects are funded by the CRW because specific recovery projects often rely on a blend of finance from multiple windows within IDA. The requirement for multiple reallocation processes within CRW has implications for its operation.

The CRW self-reports that CRW operations disburse faster than regular IDA-funded operations, with the median time from approval to disbursement approximately 144 days, compared with 213 for other operations (IDA, 2018). Further analysis of the data suggests, however, that there is considerable variability in the average time between commitment and disbursement. For example, the average number of days from crisis to first disbursement ranges from 183 days for a health emergency (cholera) to 386 days for drought and 1,182 days for earthquakes (Spearing 2019). In many cases, this long turnaround is explained by the multiple approval processes and by the fact that a significant percentage of CRW funds are used to finance the rehabilitation of infrastructure, which—in the absence of suitable preparedness—requires extensive design and procurement. But, again, the question is whether the CRW and its reliance on a reallocation model is the most efficient way of financing known unknown risk.

Recommendation 3.3 Review eligibility criteria to allow an earlier response to slow-onset crises such as drought and famine.

Slow-onset crises account for a significant percentage of the CRW's allocation—for example, 26 percent of the funds that have been allocated since 2010 were to respond to drought (see Box 1). There is a growing understanding that a timelier response to slow-onset crises reduces their human and economic costs (Hill, Skoufias, and Maher, forthcoming; Venton 2012). The CRW clock effectively starts when governments declare emergencies, but for slow-onset crises such as drought early warning information could be used to drive earlier action. To date, the CRW has been relatively slow to commit resources in these contexts—although once those commitments were made, funds were disbursed relatively quickly (within a month). A number of factors explain this slow pace, including the need to amass larger pools of funding from multiple donors, the lack of CRW funds during IDA17, and the need for governments to declare an emergency before the CRW process can start.

IDA19 is an opportunity to innovate and reconsider how the CRW could help to drive an earlier response to slow-onset crises. The proposed FAM could provide one route to testing new approaches by, for example, linking the release of CRW funding to pre-agreed triggers to deliver a pre-agreed early action plan.

Recommendation 4: Commission a review of IDA's existing risk financing tools, drawing on independent expertise.

The replenishment process is an opportunity to review IDA's role in crisis risk financing, testing whether its existing approach is delivering the best value for crisis-affected communities and for shareholders and is fit for the future. The review should include two components:

- **Component 1 should examine the internal coherence and operational performance of IDA's crisis risk financing toolkit.** How does IDA as a whole set the right incentives for effective crisis risk management through budgetary and financial instruments? What are the implications of introducing new tools (such as PEF and FAM) for the purpose, design, and sizing of the CRW? How can different stakeholders, including

civil society organizations, work together to maximise the impact of IDA disaster risk financing for the poorest? How should crisis finance be delivered?

- **Component 2 should test the positioning of IDA financing instruments in relation to the wider crisis financing architecture.** Greater clarity is needed of the relative strengths of IDA and the humanitarian financing system, particularly in the most fragile states. The synergies between the CRW and the UN-led humanitarian financing architecture are growing, for example, and must remain complementary rather than duplicative. Donors will need to be reassured that IDA is not simply becoming 'one more humanitarian donor' among many, and that it has the requisite skills and capacity to allocate and manage funds in ways that are delivering value and impact.

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Scene of devastation in Haiti following the 2010 earthquake.
Image: UK Fire Service





Cover image: Nepal, Kathmandu city view,
Shutterstock.

