

GEF IEO – Concept Note
Assessing Portfolio-Level Risk at the GEF
January 16, 2024

Purpose and Objectives

At the request of the GEF Council, the GEF IEO is conducting an evaluation to better understand the risk profile of the GEF portfolio. The main objective is to analyze and categorize the risks that the GEF is taking in projects and programs; test the robustness of the framework on closed projects, and subsequently apply the framework to ongoing projects. The goal is to support decision-making (on a portfolio basis) to ensure that risks taken are in line with GEF's preferred risk profile.

One of the GEF's practices of managing risk is through the GEF's System for Transparent Allocation of Resources (STAR) formula, and through programming choices outside of STAR. The evaluation will acknowledge and describe contextual and upfront decision-making through STAR, as this system may already mitigate against country concentration risks, and risks associated with conflict and violence-affected states. Other contextual allocative preferences may be shown by the GEF Agencies and recipient countries in terms of the geographical areas and sectors covered.

The proposed analysis by itself does not lead to a normative outcome where one risk profile is better or worse than another. Rather, it is a tool for assessing whether (i) GEF takes on the right risks where they are necessary to advance strategic priorities, and (ii) avoids taking on risks that may add little to GEF's overall impact.

Finally, what constitutes the 'right' risk profile requires a deliberate consideration of the GEF's risk appetite. The strategic directions, as well as the ongoing scientific understanding of risks and benefits, are important components in agreeing on the desired risk appetite, and risk profile.

Background

The GEF Secretariat (GEFSEC) has developed a risk appetite statement set to be presented to the Council for endorsement in February 2024.

Back in 2018, the STAP's guidance on innovation¹ provided a framework for a strategic direction for innovation in GEF programming and underscored the importance of having a risk appetite statement. In OPS-7², the GEF Independent Evaluation Office urged a continued emphasis on innovation for transformational change, noting that the GEF should encourage innovation and clearly articulate an acceptable level of risk. In its management response, the GEF Secretariat agreed and asked STAP for guidance in establishing an acceptable appetite for risk that would guide the preparation, selection, and

¹ Toth, F., et al., 2019. Innovation and the GEF. Scientific and Technical Advisory Panel to the Global Environment Facility, Washington, D.C.

² GEF IEO, 2022. Working toward a Greener Global Recovery: Seventh Comprehensive Evaluation of the GEF. Global Environment Facility Independent Evaluation Office, Washington, D.C.

design of innovative projects. In support of that request, this evaluation intends to offer evaluative insights on the actual risk profile in GEF operations and aims to make recommendations to develop a robust risk appetite framework for the GEF.³

Important progress has already been made. The GEF developed a Monitoring Policy to monitor risk during implementation in 2029 that replaced an earlier monitoring policy from 2010.⁴ Building on the GEF-7 experience, the risk section in project templates for GEF-8 now includes a standard table allowing systematic reporting on, and rating of, key risk categories. These risk categories enable GEF to assess its overall risks, as well as portfolio risks along the detailed risk categories by focal area and region. They also allow GEF to assess the risk to achieving project outcomes by mapping the four risk ratings against outcome ratings.

In addition to project design and implementation, there are several upstream decisions that relate to risk appetite but are not necessarily reflected in project documentation. A key element is the allocative preference revealed in GEF's STAR allocation mechanism. Accordingly, this evaluation will discuss the implicit risk-mitigation measures, documented in the STAR formula, such as the country characteristics related to income, policy coherence, Country Policy, and Institutional Assessment (CPIA) indicators, and past project performance, to demonstrate how GEF is taking risks into account in the allocation process.

Approach

The GEF has embraced an agenda of transformative change, aiming to leverage its limited resources to shift the trajectory of major environmental trends. By definition, incremental progress is inadequate to achieve this ambition. Therefore, it is necessary to question and assess at the strategic level, what constitutes a desirable and acceptable level of risk in different areas of the investment portfolio.

This evaluation will work with generally accepted concepts of risk. Risk is generally defined as the uncertainty of outcomes. Risk management can be described as the systematic application of management policies, procedures, and practices to the tasks of communicating, consulting, establishing the context, identifying, analyzing, evaluating, treating, monitoring, and reviewing risk. Lastly, risk appetite can be defined as the total impact of risk an organization is prepared to accept in the pursuit of its strategic objectives.

The purpose of this evaluation is to contribute to an understanding of risk management and risk appetite in the GEF. This evaluation attempts to assess whether the risk management and appetite of agencies is coherent with the GEF's risk profile. It will also assess concentration risks among countries and agencies and the role GEF administration fees play for helping agencies monitor and oversee risks in their respective GEF portfolios. Furthermore, the evaluation attempts to gain greater insight into the concept of high-risk/high-reward projects in its closed and ongoing portfolios as a means to developing possible indicators for measuring risk taking and risk appetite.

The evaluation approach will involve the following steps:

³ GEF. 2022. Risk Appetite and the GEF. A STAP Advisory Document, May 2022. GEF/STAP/C.62/Inf.07. 62nd GEF Council Meeting June 21 – 23, 2022 Washington D.C.

⁴ The GEF. 2019. Policy on Monitoring. 56th GEF Council Meeting, June 11–13, 2019 Washington, D.C. EN_GEF.C.56.03.Rev._01_Policy_on_Monitoring.pdf.

First, the evaluation will review the wider risk management literature in general and then draw on the existing risk frameworks of selected GEF Agencies and compare their risk management frameworks with risk management practices and requirements in the GEF, identifying respective alignments and gaps. It will compare the agencies' different risk categories and risk appetite statements among each other and with the GEF. The evaluation will assess the agencies' inherent and residual risks, the failure culture, and the incentives around the administration fee intended to monitor risks. It will also assess other global partnerships, such as the Global Fund and the GCF, to compare the GEF's risk management practices with those of similar funds.

Most importantly, the evaluation will attempt to develop recommendations based on interviews with implementing agencies. Additionally, it will explore the potential for GEF to track concentration risk by country and agency. This would include potential recommendations for the GEF to develop guidance on risk and a response mechanism.

The evaluation will draw on risk management frameworks and guidance notes that have been prepared in recent years. For instance, governing bodies have asked MDBs and UN agencies to specify their risk management frameworks and develop risk appetite statements.

Second, the evaluation will include an assessment of the risks identified ex ante (at CEO approval level) against those that eventually materialized (at project completion). To do so, the evaluation will look at closed projects to determine the pattern of anticipated and actual risks. The end-result will be a qualitative and quantitative analysis of risks taken across the GEF portfolio, their contribution to achieving strategic priorities, and an analysis of deliberate risk taking as an explanatory variable in the overall outcome ratings of GEF projects. In addition, and to better understand the contextual risk landscape, it will also review ex ante risk according to the STAR allocation formula.

The evaluation will validate the current risk management practices and requirements for understanding the risks in GEF projects based on a portfolio of closed projects, identifying potential gaps, and comparing them against development outcome ratings. It will examine a set of similar projects and elicit whether they yield differential returns across different sets of countries and why. Here, the evaluation will especially focus on understanding high-risk-high-reward patterns, building on the IEO evaluation of Learning from Challenges scheduled to be presented to the Council in February 2024.

Third, the evaluation will apply emerging lessons from the risk profile to recently approved and new projects. The CEO project approval process will be examined to better understand risk-taking at the top of the organizational hierarchy and its translation into project approval decisions.

This three-pronged approach translates into the following evaluative questions.

Evaluative Questions

1) When comparing GEF's risk profile with those of other agencies, the evaluation will address several key questions:

- To what extent do the risk categories and risk appetite statements of selected GEF agencies align with GEF's risk profile?

- To what extent does the GEF Secretariat assess concentration risk by country and agency?
 - What guidance on risk does the GEF provide to its implementing agencies and how does it respond to red risk flags in the project portal, which indicate high-risk issues in ongoing projects?
 - To what extent does the comparison of the GEF with its implementing agencies give an indication of policy coherence regarding risk appetite?
 - How does the GEF's risk management practices compare with similar partnership agencies (such as the Global Fund, for example)?
- 2) Analyzing the GEF's risk profile in closed project:
- How do GEF's risk ratings at entry compare with its risk ratings at completion?
 - Comparing the GEF's risk data with its outcome data, to what extent is the pattern of high-risk-high-reward reflected in the portfolio of closed projects?
 - What are GEF's contextual risks related to STAR allocation preferences?
 - Is there a difference between innovative projects compared with the rest of the portfolio in terms of their risk profile?
- 3) Applying GEF's risk profile to ongoing project:
- To what extent is the relationship between high-risk-high-reward reflected in GEF's portfolio of current projects and its current appetite for risk.
 - What is the risk appetite communication at the top and how does it translate project approval/endorsement cycle decisions?

Limitations

There are several limitations and challenges that this evaluation will have to address. First and foremost, while several implementing agencies have their own risk appetite statements, the GEF has not yet completed the process for developing one. The STAP advised on dimension for a potential risk management framework and a working group is being set up to present a risk appetite statement to the GEF Council in January 2024.

As a partnership, where each implementing agency manages risks differently and has different governance structures to manage an acceptable level of risk, there are only a limited number of comparable risk frameworks or risk appetite statements available. As a result, while drawing on available examples, this evaluation will focus on the analysis of risks in the existing and on-going portfolio, while stopping short of coming up with a normative conclusion.

A further limitation is the scarcity of research and academic literature regarding risk frameworks and risk appetite statements in the non-financial sector. While risk management frameworks are standard practice within the financial sector, and guidance notes exist for several multilateral organizations on the development of risk management frameworks, the evidence regarding their effectiveness is limited.

Scope

The evaluation will involve a sample of ongoing GEF projects from the GEF 7 implementation periods, covering a span of three years. The risk management framework will be applied to closed projects from

the GEF 5 and GEF 6 implementation periods, also spanning three years. The specific parameters, including the selection criteria and project portfolio definition, will be further elaborated in the evaluation.

Key Stakeholders

Regular stakeholder interaction will be sought with the GEF Secretariat, selected GEF Agencies, and the Scientific and Technical Advisory Panel (STAP). This will include consultation and outreach while the evaluation is under way, and dissemination and outreach once the evaluation is complete. During evaluation preparation, the team will solicit feedback and comments from stakeholders to improve the evaluation's accuracy and relevance. In particular, the evaluation will benchmark the risk management framework of the GEF agencies against each other and against the GEF's risk management practices and requirements. This will be important to determine potential gaps. In addition, for projects using Non-Grant Instruments, private sector partners will be consulted.

Timeframe

The evaluation will be conducted between October 2023 and April 2024. It will be carried out in several phases and focus on desk reviews: 1) the elaboration of an approach paper and literature review; 2) a comparative assessment of risk management frameworks for selected GEF agencies, benchmarking them against each other and against the GEF's risk management practices, as well as against comparable funds; 2) description of GEF's risk management practices; 3) application of the risk management practices and outcomes variables to a sample of closed and ongoing projects; and 5) write-up and incorporation of feedback; (6) dissemination and discussion with the Council.

The Evaluation Team

Silke Heuser (Evaluation Officer and Team Lead), Hans Boehmer (Senior Consultant), Geeta Batra (Manager)