



## Twenty years since the GEF Council incorporated nongrant instruments into the strategy, the IEO's first comprehensive study of the nongrant portfolio finds encouraging returns.

Nongrant projects in the GEF refer to projects in which GEF financing is used in products and mechanisms that have the potential to generate financial returns. Concerns of crowding out commercial finance, and donor reluctance to provide “free” money to the private sector through traditional grant-based financing, led to support of nongrant instruments to augment the GEF's offerings. Moreover, the nongrant instruments lend themselves to tailored structuring, allowing better alignment of mitigation measures to the risk being covered—not only helping to ensure the principle of minimum concession but also minimizing market distortions.

### KEY FINDINGS

**1. High-leverage ratio of cofinancing to GEF grant.** On average, every dollar of GEF grant spent for nongrant projects leverages \$10 in cofinancing. Not only is the overall leverage ratio the highest among the private sector portfolio, it is also the

highest across the general GEF portfolio.

**2. Increasing trend in global nongrant projects.** In GEF-6, seven of the eight projects are multicountry efforts, representing a significant increase over previous cycles.

**3. Diversification over time.** The vast majority of nongrant projects are in the climate change area. The GEF-6 projects in particular show greater diversity in the sectors covered, with an increased focus on biodiversity and land degradation.

**4. New implementing partners.** Of the eight projects approved in GEF-6, two are being implemented by Agencies that have not previously led GEF projects: the Development Bank of Southern Africa (DBSA) and Conservation International.

**5. Role of technical assistance.** Nongrant projects have made use of a large range of instruments, often with

**PURPOSE AND METHODS:** The purpose of this study is to assess the Global Environment Facility's (GEF's) nongrant instrument activities in order to provide insights and lessons for GEF-7. A mixed-methods approach was used, based on evidence from a nongrant instrument portfolio analysis, review of terminal evaluations of completed projects, interviews with relevant stakeholders, and desktop research of pertinent project documents. The study's recommendations aim to enhance the design and use of nongrant instruments going forward.

**WEB PAGE:** [www.gefio.org/evaluations/study-non-grant-instrument-gef](http://www.gefio.org/evaluations/study-non-grant-instrument-gef)

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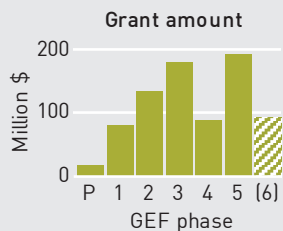
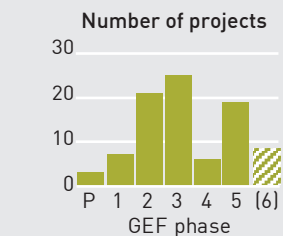
**ABOUT US:** The Independent Evaluation Office (IEO) of the GEF has a central role in ensuring the independent evaluation function within the GEF. [www.gefio.org](http://www.gefio.org)

## PORTFOLIO HIGHLIGHTS

**89**  
projects

**\$0.7 billion**  
in grant funding

**\$7.2 billion**  
in cofinancing

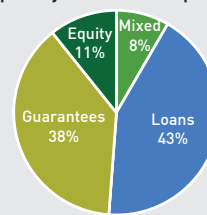


**Project modality**  
91% full-size projects  
9% medium-size projects

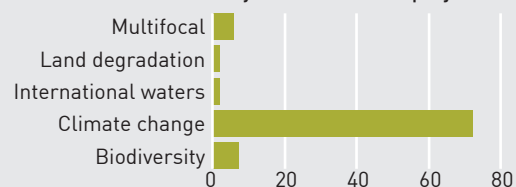
**Top 3 Agencies**  
34% UN Development Programme  
31% World Bank Group  
9% Inter-American Development Bank

**Regional distribution**  
28% Europe and Central Asia  
20% Asia  
18% Africa  
18% Latin American and Caribbean  
9% Global  
7% Regional

Frequency of use (% of projects)



Distribution by focal area (% of projects)



technical assistance—almost invariably financed by the GEF—integrated into nongrant financing mechanisms.

**6. Reflows.** Reflows are the financial returns transferred to the GEF Trust Fund. To date, \$8.2 million in reflows has been received.

## BACKGROUND

Nongrant instruments were first mentioned formally in GEF-2; in GEF-4, the 2006 [GEF Strategy to Enhance Engagement with the Private Sector](#) envisioned “strategic use of nongrant/risk mitigation instruments” as one of the main instruments to achieve the goal. In GEF-5, the private sector set-aside amounted to a total of \$80 million, focusing entirely on the use of nongrant instruments. In GEF-6, the GEF launched a \$115 million pilot program to apply nongrant financial instruments to combat global environmental degradation.

## RESULTS

**Performance.** Overall, the outcomes of 37 (78 percent) of the 41 nongrant projects were rated as moderately satisfactory or higher, comparable to the most recent performance report across the entire GEF portfolio. Sixty-six percent of projects (35) have sustainability ratings

of moderately likely or higher—again comparable to the broader GEF project portfolio. Sixty-one percent of projects have efficiency ratings in the satisfactory range. Sixty-two percent of projects have satisfactory ratings on monitoring and evaluation, and 74 percent have satisfactory design ratings.

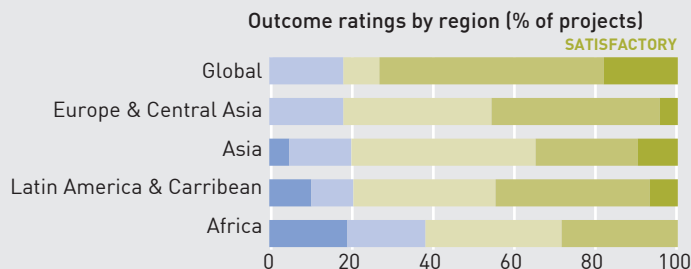
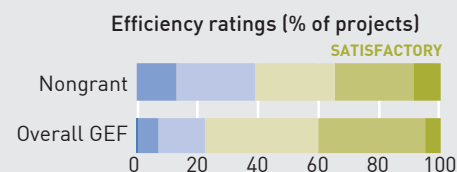
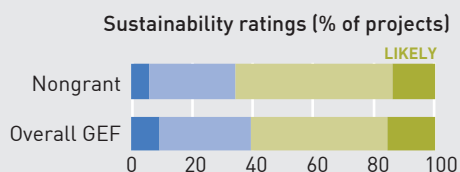
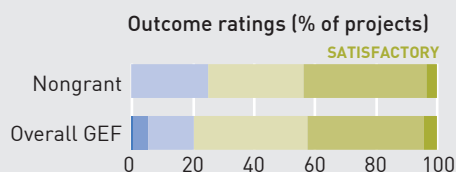
**Reflows.** In all cases reviewed in this study, project-level reflows remain in the country and continue to be used as originally intended or deployed to other agreed-upon uses.

The terminal evaluation for the Hungary Energy Efficiency Project indicates that the project was highly successful, with remaining balances rolled into the second Hungary Energy Efficiency Co-Financing Project. The Environmental Business Finance Program was funded in part from reflows emanating from the Small and Medium Enterprise Project and is still generating reflows for the GEF. Reflows on the International Finance Corporation (IFC) [Earth Fund](#) are also beginning. Notably, starting with GEF-5, project appraisal documents presented for Chief Executive Officer (CEO) endorsement contain an annex where reflows are to be explicitly addressed. There has been a clear evolution in reporting practice, with better descriptions of the reflow and quantification of returns to the GEF.

**Instruments.** The GEF classifies nongrant instruments into three broad types: loans, guarantees, and equity.

- **Loans.** Debt instruments are the most popular financing structures in the portfolio (42 percent). These are used either on their own or in a blended manner. The concessionality could be a lower interest rate, a longer maturity, or a subordinated position. They are also often provided in conjunction with a multilateral development bank facility, which takes a more senior position.
- **Guarantees.** These instruments are the second most used financing vehicle (37 percent), often used in conjunction with loans; they are typically structured to cover first loss tranches in financial intermediaries. The rationale for a guarantee is to overcome the reticence of financial intermediaries in lending to the activity in question by providing a risk-sharing mechanism. Evidence on the effectiveness of the guarantee instrument is mixed. The Poland Energy Efficiency Project included a partial credit guarantee to cover 50–70 percent of the loan principal on first loss. The terminal evaluation states that the project was restructured in 2011, because of very limited demand from banks for the

## PERFORMANCE HIGHLIGHTS



guarantee. In other cases, the guarantee appears to have been highly successful in expanding energy efficiency lending. In at least five cases, a guarantee was used with minimal or no losses, proving the soundness of the business case and the underlying premise.

The study also brought to light a few cases where other climate finance providers were involved in GEF projects. One such project is the World Bank's India Partial Risk Sharing Facility for Energy Efficiency. This project involves GEF financing of \$18 million, Clean Technology Fund (CTF) financing of \$25 million, and other cofinancing of \$127 million; \$12 million of the GEF financing is used to fund a risk-sharing facility, which is "backstopped" by \$25 million of CTF contingent financing.

- **Equity.** Equity investment has recently become more prevalent. Four of the eight projects in GEF-6 involve some sort of equity structure. GEF-6

also marks the first appearance of a *pari passu* risk/return-sharing feature. Equity is the riskiest form of capital in the stack, and it stands to reason that a mission investor such as the GEF take this position. Another reason for the greater use of equity could be the potential for returns.

From GEF-5, one such investment as part of the GEF Public-Private Partnership platform occurred with the Inter-American Development Bank's Multilateral Investment Fund (MIF), which requested \$15 million in reimbursable resources from the GEF for this program to invest in three venture capital funds: The MGM Sustainable Energy Fund, Ecoenterprises II, and the Honduras Renewable Energy Financing Facility. The MIF is administering GEF investments of \$7 million, \$5 million, and \$3 million, respectively. In addition to the investments, the MIF will provide a total of \$1.95 million in nonreimbursable

resources for technical assistance in the three funds.

Another interesting use of equity can be seen in the GEF-6 nongrant investment in the Meloy Fund with Conservation International. The Meloy Fund is an \$18 million impact investment fund devoted to providing debt and equity capital to scalable enterprises that can play a key role in incentivizing sustainably managed community small-scale fisheries, contributing to the maintained integrity and functioning of coral reef ecosystems in Indonesia and the Philippines. No grants will be provided through the fund. Funds will be deployed to finance the scaling-up of enterprises to move them toward environmentally responsible product lines, with a significant portion of invested capital to be used for the acquisition or upgrading of fixed assets. Borrowing entities are expected to include fisher cooperatives, aggregators and processors, and early stage enterprises. As with other nongrant projects, the Meloy Fund will provide need-based technical assistance in the form of mentoring, operations and product technical support, financial management, corporate governance, etc., to its investees to support their

“With nongrant projects, project developers and GEF Agencies are increasingly able to offer innovative financing solutions for both climate change and natural resources management.”

—Baljit Wadwha,

IEO Senior Evaluation Officer

development, as well as to maximize positive social and environmental impacts.

Based on the terminal evaluations reviewed, equity instruments are experienced as challenging. The need for high returns and a secure exit further complicate sourcing of deals in “difficult” sectors such as climate change and biodiversity, as evidenced by the terminal evaluations for completed equity deals such as the Solar Development Capital and the Renewable Energy and Energy Efficiency Fund projects. The equity transactions in GEF-6 appear to be more complex and consist of several moving parts. It is too early to gauge performance, as none of the GEF-5 or GEF-6 projects have been evaluated, and thus the effect of this complexity on project performance is yet to be determined.

## RECOMMENDATIONS

**1. Diversify.** The market has changed, with blended finance becoming a more mainstream activity and amenable to a wider range of providers and financial instruments. The GEF is operating

in a crowded climate finance landscape, but can distinguish itself and continue to support private markets in biodiversity and prevention of land degradation where external financing is a viable growth option for private firms and where the GEF remains one of the few financiers of other convention areas.

### **2. Simplify financial structures.**

Blended funds and programs focused on small and medium enterprises (SMEs) are generally successful, but more resource intensive to deliver. A number of terminal evaluations point to the challenges involved in implementing innovative structures, and advocate for simplicity in design. Moreover, even using similar financial instruments, success in one country is not necessarily replicable in another and depends on a variety of factors that cannot be addressed by structuring alone.

### **3. Scale back overly ambitious targets.**

Terminal evaluation reviews revealed that many nongrant projects set overly ambitious targets for implementation results which require midcourse correction, resulting in implementation delays and additional transaction costs. Projected reflows

in GEF-5 and GEF-6 seem overly optimistic.

### **4. Simplify project design and delivery.**

The GEF should avoid overly complicated structures. Multiple Agency involvement and/or multiple partners for implementation can be difficult to manage, entail greater transaction costs, and lead to delays.

### **5. Integrate technical assistance.**

The GEF should consider integrating technical assistance into nongrant projects, particularly when GEF financing is mixed with other nongrant funds. Technical assistance is a necessary adjunct to investment support, and a clear niche for the GEF when acting in conjunction with other financiers.

### **6. Systematically tag projects.**

The GEF Secretariat’s Project Management Information System does not adequately provide information on type of nongrant instruments used, investment allocations, and projected reflows. Moreover, classification of instruments in project documents can lead to confusion and create inconsistencies. There is a need to standardize formats and reporting requirements. ■

