Briefing note

Towards an agenda for MDB reform in FCV

Kathryn Nwajiaku-Dahou, Fiona Davies, Hans Peter Lankes, Alastair McKechnie and Matthew Foley

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About the authors

Kathryn Nwajiaku-Dahou

Kathryn Nwajiaku-Dahou is Director, Politics and Governance, ODI.

Fiona Davies

Fiona Davies is Senior Research Associate, Development and Public Finance, ODI.

Hans Peter Lankes

Hans Peter Lankes is the Managing Director and Deputy Chief Executive at ODI, and is a visiting professor in practice at the LSE Grantham Research Institute and a senior fellow at the LSE/Oxford International Growth Centre.

Alastair McKechnie

Alastair McKechnie is Senior Research Associate, Development and Public Finance, ODI.

Matthew Foley

Matthew Foley is Managing Editor and a Research Fellow, Humanitarian Policy Group, ODI.

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Acronyms

CMU	Country Management Unit
DFI	Development Finance Institution
FCV	Fragility, Conflict and Violence
IDA	International Development Association
IBRD	International Bank for Reconstruction and Development
IFC	International Finance Corporation
INGO	International Non-governmental Organisation
MDB	Multilateral Development Banks
MIGA	Multilateral Investment Guarantee Agency
ODA	Official Development Assistance
OP 7.30	Policy on Operating under De Facto regimes
PRA	The Prevention and Resilience Allocation
RECA	Remaining Engaged during Conflict Allocation
TAA	The Turn Around Allocation
WBG	World Bank Group

Introduction

‘Fragility’ is not a uniform condition. It can encompass a wide range of different vulnerabilities. When, how and to what degree a country might be considered fragile is often unclear. Even in apparently ‘fragile’ states there can be pockets of stability, effective governance and a functioning private sector, as is the case, for example, in Haiti and across much of the Sahel. States that appear to be on a development trajectory may contain marginalised regions prone to violence and insurrection, and repression amidst institutional functionality, may conceal underlying fragilities.

As an organising principle for policy making ‘fragility’ is an all-encompassing and blunt analytical tool that can be particularly discriminatory towards low-income countries. Nevertheless the rising number of countries and regions affected by fragility, conflict and violence warrants increased and focused attention by policymakers. We expect that by 2030 between half and two-thirds of the world’s poor will be living in countries affected by different forms of fragility, conflict and violence. By which we mean chronic institutional weaknesses, unstable or contested political settlements, economic and fiscal weaknesses and the compounding risks of climate change all combine to create a complex and diverse set of development challenges.

In addition, today some 49 per cent of states experiencing forms of fragility, conflict or violence have de-facto (Tindall, 2023) or politically estranged regimes (Cliffe et al., 2023). The absence of international recognition, access to international banking and finance, and sanctions regimes, not only compounds the drivers and forms of fragility facing the increasing number of people living under de facto regimes, but creates new types of operational challenges for international actors, including Multilateral Development Banks (MDB), in these contexts.

Even if more than half of the world’s extreme poor are likely to be living in fragile and conflict-affected states by 2030, they receive only a quarter of all international development assistance. Much of that assistance is channelled through MDBs, who as the largest source of institutional financing, enjoy considerable leverage (particularly in contexts where bilaterals are increasingly channelling their development assistance through multilateral sources). They dispose of significant analytical capacity, and the scale of their financing gives them privileged access to institutional channels for sustaining dialogue. Against this backdrop, how can MDBs fully capitalise on

these strengths and ensure they are fit for the purpose of preventing the continued proliferation of fragility, conflict and violence or responding to and addressing their drivers once unleashed?

Being fit for purpose requires MDBs to answer 3 key questions: How is MDB engagement in Fragility Conflict and Violence (FCV) (financing, analysis and dialogue) making a difference to the drivers of fragility and what needs to be improved; with whom should they be working (partnerships) in order to increase delivery and impact in FCV in ways that 'Do No Harm', and what needs to change in the MDB authorising environment to enable them to be more effective in FCV.

This short note outlines considerations to guide discussions on how MDB reform processes can contribute to effective engagement and better outcomes in FCV contexts.

How authorising environments need to change

The World Bank Group (WBG) published a five-year Strategy for FCV[1] in 2020 which recognised addressing FCV as a strategic priority essential to its goals of ending extreme poverty and boosting shared prosperity. This was reiterated in the Mid-Term Review released in 2023.

The FCV Envelope that accompanied the FCV strategy provides additional resources to International Development Association (IDA) countries facing FCV risks (the **Prevention and Resilience Allocation** (PRA)), to enable IDA to stay engaged in countries in conflict (the **Remaining Engaged during Conflict Allocation** (RECA)) and to support countries emerging from conflict or crisis (the **Turn Around Allocation** (TAA)). The WBG Evolution Roadmap explicitly recognises the need for increased support for FCV countries.

This analytical and operational work speaks to the WBG's increased interest in, and financing for, fragile and conflict-affected states. But more needs to be done. In particular, while the development of an FCV Strategy is welcome and there is liberal reference to FCV in the Evolution Roadmap, fragility is still not visible enough in the Bank's overall strategic approach and there are as yet no Bank-wide mechanisms to drive the kind of change the problem requires. Without such a focus, existing business cultures and modes of operation which do not maximise effective engagement in FCV will be extremely difficult to shift.

The progress made over the past three years, needs to be consolidated to ensure that IDA 21 replenishment lays the foundations to scale up the visibility and relevance of the FCV agenda across the WBG. **A Global Challenge Programme around FCV to mainstream fragility as a core operational priority in MDB reform debates, and pull together capabilities from across the Group, could be one way of doing this.** This would ensure that the operational reform agenda keeps the focus on financing for fragility

[1] See: https://documents.worldbank.org/en/publication/documents-reports/documentdetail/844591582815510521/world-bank-group-strategy-for-fragility-conflict-and-violence-2020-2025

as a global challenge and a necessary target for addressing extreme poverty.

The WBG can do more to leverage its finance (public and private), its analysis and its capacity for dialogue to create opportunities for peacebuilding and to engage more proactively in international efforts to prevent conflict and consolidate peace.

More broadly, efforts to simplify IDA as part of a larger overhaul of policies and procedures tailored to FCV are welcome, but this has to be a concerted effort by shareholders. WBG management flags that each country has attached specific rules or conditions to their aid over time, to the point where the Bank now has to reckon with more than 1,000 conditions, against 50 years ago.

Simplifying and addressing this procedural heaviness and increasing the flexibility of financing is in everyone's interest. One possibility might be to use the principles of the crisis response windows for FCV financing more flexibly and apply them beyond crisis to speed up processes, especially in lending and the application of safeguards, procurement and other risk-management policies.

Decisions on disbursements in FCV must be made less subject to the risk aversion of particular shareholders. Whilst the WB has an policy on Operating under De Facto regimes (OP 7.30), questions have been raised about whether it is being effectively used, and the extent to which it provides sufficient and adequate guidance to inform decision making about whether or how to continue operating in de facto environments. **The rules on remaining engaged should be aligned with new guidance frameworks. In particular, G7 countries could be more nuanced in their decision-making on when to withdraw support from countries,** and MDBs and DFIs could consider working with a range of partners (see below). This will require greater investment in third-party monitoring and accountability, and probably a higher share of grant funding.

There is a greater commitment to prevention in the World Bank Group strategy and prevention is referred to in the MTR – this is a welcome step forward. The WBG Strategy defines prevention as incorporating inclusion, access to social services and access to justice. **But the instruments for prevention are limited to a prevention window (Prevention and Resilience Allocation), which requires the existence of client governments' prevention plans, in cases where some violent outbreaks have already been documented.** This is far beneath the ambitions outlined in the WB's own Pathways for Peace Report – 2018 (jointly with UN)[2]. The Bank knows what needs to be done, however what is required is clearer operational guidance and financial tools fit for operationalising

2 See: https://www.worldbank.org/en/topic/fragilityconflictviolence/publication/pathways-for-peace-inclusive-approaches-to-preventing-violent-conflict

commitments. **At the moment there are inadequate financial and analytical tools for seriously tackling prevention and inadequate provision for monitoring.**

What kind of MDB is needed in FCV?

Structural institutional weaknesses, poor absorptive capacity and weak political settlements, mean that the risks of doing harm are greater in FCVs if MDBs operate in the same ways they do elsewhere. Whilst the focus on financing fragility is welcome (just a few months away from IDA 21 replenishment) the focus also needs to be on how MDBs, with an increased financial envelope for FCV, can operate differently in order to address the drivers of fragility in ways that 'Do No Harm'.

The World Bank Group cannot use the same tools and roll out the same systems in fragile and conflict-affected states as it does elsewhere because the absence of a political settlement is at the heart of the problem in these situations. Policies, systems and institutional support need to be tailored to the needs of an FCV context, rather than replicating practice from non-FCV countries. Greater investment is needed in strengthening capacity of institutions likely to consolidate political settlements. This should be considered as investments in prevention, going beyond investments in social protection, and should include the strengthening of inclusive institutions (e.g. security and justice infrastructure and economic foundations for peace as outlined over a decade ago in the New Deal for Engagement in Fragile and Conflict Affected states (IDPS, 2011)).

Developing in-country governance capacity and systems is key. **Technical assistance should not focus narrowly on the systems and procedures that matter for Bank programming and the management of fiduciary and reputational risks. Rather, the focus should be overall state-building requirements and how Bank finance for the country can strengthen them.** In particular, this means strengthening national procurement capacity, systems and processes, even where these systems are not used for the implementation of Bank programmes.

The Bank's engagement in West Bank and Gaza is an instructive lesson on mismatch and stasis in analysis, dialogue, and operational engagement that had been foreseen by staff and managers. Addressing the drivers of fragility also means integrating more robust diagnostics and, political economy and security analysis into the Bank's own financing and project decisions, as highlighted in the MTR. **The Bank's experience in West Bank and Gaza**

underscores the importance of more rigorous and regular analysis of drivers and risks of conflict or crisis. This includes candidly addressing (rather than airbrushing) controversial political and security considerations, and providing for communicating more frankly with shareholders. More just-in-time analytical work is needed, coupled with faster quality assurance processes, to ensure that this analysis is relevant and can be used to facilitate timely outcomes.

The Bank should consider increasing investment in monitoring, evaluation and learning in relation to fragile and conflict-affected contexts. This will require more robust project-level understanding of the Bank's impact and footprint. Conflict sensitivity and context-specific analysis of the local political economy need to be integrated into the design, evaluation and monitoring of project impact. Given the diversity of contexts at issue here, **systematic learning and sharing of country and regional experience is called for. It will be important to better understand the perceived gaps and shortcomings in the Bank's engagement in FCV environments at project level.** This data is difficult to gather and aggregate, although thanks to IEG evaluation reports some useful country-specific narratives are beginning to emerge.

Among other things, this will mean **incentivising staff to stay, transfer and consolidate knowledge, strengthening the role of the Country Management Unit (CMU) in FCV, investing in career paths** and managing staff profiles to ensure that staff on the ground and in Washington understand the requirements of working in fragile and conflict-affected states. This understanding needs to be threaded through all operations in fragile contexts. This will require creating career path incentives for MDB staff working on fragility and integrating them in operations and performance management, where otherwise financial criteria ('securing a deal') tend to be prioritised. Anything less would run the risk of doing harm, rather than contributing to peace in ways that ultimately also weaken the economic viability of investments.

MDBs should build their presence on the ground with far greater ambition than has been the case thus far – there will be a need for significant changes to internal incentives for staff, especially at IFC/MIGA. This could include simplifying and consolidating expertise across MDB groups for impact and sustained engagement and combining strategies and country programme management and operations across the World Bank Group. It should also include the more systematic, integrated deployment of IBRD/IDA, IFC and MIGA instruments as well as diagnostics, technical assistance, finance, and grants/concessional loans bearing in mind the uniqueness and complexity of each FCV situation.

Partnership

To be able to deliver increased finance in fragile and conflict-affected states will require diverse financing tools and instruments, and partnerships. Partnerships and agreement at political level, on the application of existing policies to enable effective delivery including with non-sovereign, private and non-governmental entities will be important. There may also be trade-offs in terms of managing priorities set by sovereign borrowers, that need to be addressed and managed.

Partnership innovations particularly for de facto situations are key but definitions of partnership need to be broadened – to include sub national governments, regional institutions, domestic private sector, civil society, as well as UN and international non-governmental organisations. **Partnerships with different entities will require different approaches**.

Fostering partnership at sub national level, with local governments may have to be via grants rather than loans and via third parties. This will also **require continued and stepped up investment in third party monitoring, accountability in ways that create space for community / civil societ**y voices to be heard, particularly in situations where authority is deeply contested.

The private sector could be a critical partner for both prevention and engagement in fragile and conflict-affected contexts more broadly. Leveraging the private sector should be a more important plank of FCV engagement. Even in the most difficult environments there will be functioning businesses, financial and trade networks and rudimentary supply chains. While it would be a mistake, in the absence of strong political economy analysis, to presume a distinction between political and economic elites, it may be the case that a strong private sector can serve as a counterweight to difficult or abusive governments in fragile states, or where engagement with governments is not possible.

Greater sustained on-the-ground presence in FCV would put MDBs and DFIs in a better position to know and understand local players and the local political context within which they operate. Since the underlying political economy drives both private sector development as well as development more generally, and also the role of public finance in political risk mitigation, there is a case for reexamining the relation among IDA/IBRD, IFC, MIGA and possibly synergies with

ICSID, particularly in country programme management in FCV countries.

In these contexts, financial intermediaries – local banks, money transfer organisations (which in Somalia and Yemen for example have greater reach than the formal banking network), regional institutions or public development banks – are able to reach the most vulnerable and provide a service MDBs and DFIs cannot. The value of that service should be recognised through at-cost or below-market loans, guarantees, grants, and/or technical assistance. Greater use of the private sector arms of MDBs and DFIs would offer an opportunity to keep finance flowing into the economies of fragility and conflict-affected states, helping to cushion vulnerable populations from the full effects of conflict and instability.

Financing through UN bodies and INGOs particularly in contexts of protracted crises, requires careful management and planning. As ICRC points out, currently very few countries meet the threshold criteria for accessing the Remaining Engaged during Conflict Allocation (RECA)[3] window or other innovative solutions, developed before the COVID-19 pandemic, which exclude high-intensity and medium-intensity contexts. For programmes to be supported by the RECA, they must also "preserve institutional capacity and human capital that will be critical for the country's future recovery". Whilst this is important, scope for gap filling when government plans are not in place, should be assessed.

MDB reform discussions should include reforming FCV financing allocation windows and facilities to enable them to adopt more flexible criteria for direct financing. This could also involve giving country teams greater freedom to develop direct partnerships in order to improve the responsiveness, agility and reach of the World Bank Group. But preserving human capacity and human capital should remain the priority, as indicated by client borrowers as situations allow.[4]

3 The RECA eligibility criteria in IDA 20 for the RECA will be based on three criteria: (a) a quantified indicator that identifies countries in high-intensity conflict; 6 (b) a Country Policy and Institutional Assessment (CPIA) of 2.5 or below; and (c) a proposed program that is consistent with the RECA. World Bank Document

4 The model of partnership used in Somalia when IDA financing to Government, was then channelled through UN institutions and onwards to INGOs for humanitarian assistance, could be replicated)

Towards an MDB reform agenda: A new approach in fragile and conflict affected states?

The need for innovative ways to address the drivers of conflict and fragility is becoming ever more urgent – and needs to be part of the reform agenda of the MDBs.

Increased ODA for IDA is required, not least because it has been stuck at $24 billion for two decades, meaning that its value today is far less than it was twenty years ago. But better financing is also needed, more tailored to the particular needs of fragile and conflict-affected states, and more aligned with borrowers' priorities for how the finance is spent, and where the gaps are.

This paper has highlighted some core innovations required in the authorising environment; the way MDBs invest in partnerships; and rethinking what MDBs should focus on in FCV. These are critical:

1 Fragility must become an institution wide priority through the equivalent of a WBG Global Challenge Programme on FCV and similar programmes in other MDBs. This can help disrupt established business cultures and disjointed modes of operations, for example by adjusting Operating Policies with guidance to facilitate greater risk taking, investment in prevention and insulation from political considerations, in ways that ensure FCV are considered as global public challenges and are financially accounted as such;

2 Flexibility and simplicity to enable more diverse partnerships through grants and concessional finance with a range of structures, particularly in de-facto contexts, with an increased focus on local banks and financial service providers as well as partnerships with INGOs, where necessary;

3 MDBs should rethink their approaches, adopting ways of working in FCV that focus on less standard governance modalities and more on investment in capacity for inclusive prevention, and ensure robust, regular, joint analysis that feeds into country diagnostics. Monitoring, evaluation and learning should also drive

more agile operational decision making. This should include leveraging partnerships with local organisations and international NGOs to better address gaps in understanding and tackle political economy and implementation hurdles, especially in de facto and displacement situations.

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