



Global Environment Facility

GEF/C.12/6
October 1, 1998

GEF Council
October 14 – 16, 1998
Agenda Item 7

MAINSTREAMING THE GLOBAL ENVIRONMENT IN WORLD BANK GROUP OPERATIONS

(Prepared by the World Bank Group)

DRAFT

**MAINSTREAMING
THE GLOBAL ENVIRONMENT
IN WORLD BANK GROUP OPERATIONS**

**World Bank Group Draft Paper prepared for
Presentation to the Executive Board, October 13, 1998 and
at the GEF Council Meeting, October 14-16, 1998**

TABLE OF CONTENTS

EXECUTIVE SUMMARY	1
Attachment, The World Bank and the global Environment (Progress to Date)	5
1. INTRODUCTION	10
2. THE CHALLENGE OF MAINSTREAMING THE GLOBAL ENVIRONMENT	11
The Bank Group's Commitment	11
The Client Country Perspective: Trade-offs and Constraints	11
Objectives and Role of the Bank Group	12
3. REVIEW OF PROGRESS MADE	14
Lending for the Global Environment	14
Country Assistance Strategies, Economic and Sector Work, Operational Tools and Training	16
(a) Country Assistance Strategies	16
(b) Country Economic and Sector Work	16
(c) Operational Tools and Training	17
Operational policies	19
Sector Policies	21
New Products and Strategic Partnerships	21
Mainstreaming GEF in Bank Operations	22
Performance Incentives	23
Summary of Progress	23
4. CHALLENGES AND THE WAY FORWARD	25
Challenges Ahead	25
Towards A Corporate Environment Strategy	26
Annex 1 Bank Group Lending for the Global Environment	28

MAINSTREAMING THE GLOBAL ENVIRONMENT IN WORLD BANK OPERATIONS

EXECUTIVE SUMMARY

1. The Global Environment Facility (GEF) Council has requested the Bank Group to provide a progress report and an action plan on the Bank Group's efforts to include the global environment in its regular operations. This paper is the response prepared by Bank Group management. It presents a progress report on the Bank Group's efforts to mainstream the global environment, but stops short of assessing the impacts of these efforts. The reason is that the Bank Group's lending and non-lending services for global environmental management are relatively young, and the contributions of these services to global environmental benefits typically have a long gestation period.

2. While examining priority areas for action, the paper is not setting out a comprehensive Bank Group strategy for the global environment or its mainstreaming in Bank work. Such a strategy needs and will be developed as part of the preparation of a Bank Group strategy for the environment as whole, covering its local, regional and global aspects. The development of such a corporate strategy is being initiated.

The Bank Group's Commitment and the Client's Perspective

3. The commitment by the Bank Group to the alleviation of poverty and sustainable development recognizes that these goals are only attainable if local, regional and global environmental issues are addressed. While the Bank Group's client countries have committed themselves to address the degradation of the "global commons", evidenced by their almost universal ratification of the global conventions, they face critical trade-offs between pressing short to medium term needs to provide food and vital services for the poor, and the need to invest in environmental management for the longer term. In addition, their ability to take action on the global environment is constrained by limited economic incentives and weak policy and institutional frameworks.

4. The Bank Group is committed to work with its clients in integrating global environmental objectives into their national sustainable development programs, and in meeting their obligations under the global environmental conventions. It proposes to do so in the following four ways: (i) enabling clients to identify and capture the so called "win-win" opportunities, that is, those that both benefit the domestic economy and the global environment (e.g. reducing greenhouse gases in a manner that simultaneously addresses local air quality concerns and meets energy demand); (ii) provide country partners access to global financing mechanisms (GEF and the Multilateral Fund for the Montreal Protocol, MFMP) which compensate countries whenever the domestic costs of actions exceed the domestic gains; (iii) help countries access markets for global public goods (e.g. carbon offsets trading); and (iv) address negative impacts from global environmental degradation.

A Progress Report

5. Important progress has been made toward mainstreaming the global environment in Bank Group operations since the Bank Group began embracing the global environmental agenda. This progress manifests itself in the lending and non-lending services that the Bank Group provides to its clients, as well as in the establishment of "in-house" mechanisms that are required to make such services global environment-friendly.

6. Global environmental priorities are increasingly reflected in *Bank Group lending*. A growing number of projects in the agricultural, forestry, energy and industrial sectors address global environmental objectives directly (biodiversity, climate friendly renewable energy, phase-out ozone depleting substances). This lending is increasing, not only as a result of rising Bank commitments using GEF and MFMP resources (now totaling a cumulative \$1.2 billion) but also because of growing commitments from IBRD/IDA and associated co-funding. Bank Group lending also supports global environmental objectives indirectly whenever projects that support national and sectoral objectives generate benefits for the global environment.

7. Hence, the picture for lending in the two main thematic areas of biodiversity conservation and energy/climate change is encouraging.

- Biodiversity Bank lending and associated co-funding in support of biodiversity conservation has gone from \$21 million in 1988 to over \$400 million in 1997 for a cumulative total of \$1.8 billion. The emergence over the last six years of the GEF as a source of Bank Group lending for biodiversity has not “crowded” out IBRD and IDA lending. In addition, an important part of our total lending for forestry (a portfolio now totaling \$4 billion) and agricultural and rural development supports conservation and sustainable use of biodiversity through improved land and forest management.
- Climate change/energy Annual Bank, including GEF, commitments for energy efficiency and renewable energy have increased since the early 1990s, despite the overall decline in Bank lending for energy in recent years. Annual average Bank/GEF financing for end-use energy efficiency has grown from roughly \$85 million in the pre-GEF period (FY81-91) to \$190 million in the FY92-9 period; and for new and low greenhouse gas emitting renewables (hydropower and geothermal excluded), from \$30 million to more than \$90 million within the same timeframe. This is still modest. However, a recent study found that since 1994, the proportion of the Bank’s energy development portfolio that is classed as highly greenhouse emissions intensive fell from about 50% to 11% as more loans than before focused on reform, restructuring, energy efficiency, and renewables.

8. *Mechanisms for mainstreaming* the global environment in lending and non-lending services are in place or being developed.

- Key operational policies on environmental assessment and economic evaluation have been developed and modified to reflect global environmental concerns.
- Sector policies and strategies in key sectors are being revised to make them responsive to global environmental concerns. An Environment Strategy for the Energy Sector Paper is scheduled for review by the Board in October this year. A review of the implementation of the Forest Sector Policy is underway, leading to the development of a forestry sector strategy.
- The process of development and dissemination of the analytical tools to facilitate integration of global objectives in environmental assessment is well advanced in respect of greenhouse gas emissions and abatement options.
- New products and partnerships for global environmental management have recently been launched or are under development.

- Streamlining GEF in Bank operations has proceeded successfully as the recommendations of the President's 1996 Task Force on Streamlining GEF in Bank Operations have been acted upon.

Challenges and the Way Forward

9. To further mainstream the global environmental concerns into its development assistance, the Bank Group will address several challenges. First, it will strengthen its own capacity to include environmental issues, including global ones, in the country assistance dialogue. This includes the capacity to identify the “win-win” options for funding under regular Bank or other donor funding, as well as beyond the “win-win” opportunities to capture additional global benefits with the support from the global financing mechanisms. Secondly, the Bank Group will step up its efforts to build capacity in client countries for analyzing and addressing the links between development and environmental objectives and global concerns. Thirdly, it will respond to the expected increased demand from its clients for GEF assistance by maximizing opportunities to integrate such assistance with Bank lending in sectors like agriculture, forestry and energy. Finally, in planning and extending support to clients countries' for their efforts to address global environmental objectives, the Bank Group will continue to recognize the limitations that the international conventions place on the obligations of client countries to take specific actions on global environmental concerns.

10. To meet these challenges, action will be required in five priority areas:

- **First**, *strengthen Global Environmental Sector Work*, by working with client countries on underpinning the country assistance dialogue with country economic and sector work that recognizes and analyzes relevant global environmental impacts and effectively relates them to national sustainable development. This involves expanding and accelerating the efforts under (i) the ongoing Global Overlays Program, (ii) National(AIJ/JI) Strategy Studies Program (for climate change), (iii) the Strategic Environmental Assessments initiative, and (iv) the Energy-Environment Review program.
- **Second**, *strengthen and accelerate in-house (management and staff) and client training on global environmental issues and analytical methods*, emphasizing the understanding of client country obligations under the global environmental conventions, the links between global environmental objectives and sustainable development, and the opportunities for addressing them in Bank Group development assistance and national sustainable development planning. Ongoing programs for staff training and identification and dissemination of “good practice” tools and methods for global environmental impact analysis will be strengthened in all thematic areas.
- **Third**, *consolidate the development of new products and partnerships and integrate them as appropriate in country assistance programs*. The initiatives for market transformation in forest or marine resource management, or market-based mechanisms for mitigating climate change under the Kyoto Protocol, are demonstrating potential to mobilize funding, and the skills and influence of mutli-stakeholder coalitions to mitigate global environmental degradation. Continued funding is essential to ensure that this piloting work is completed and outcomes appropriately included in the Bank's core business.
- **Fourth**, *complete mainstreaming GEF in Bank operations* by (i) fully integrating GEF with the Bank's business planning process, starting with the inclusion in Senior Management's forum for setting institutional priorities; (ii) removing disincentives for undertaking GEF projects by making

uniform costing fully applicable; and (iii) monitoring the effectiveness of the streamlining measures put in place.

- *Fifth, strengthen incentives for management and staff to address global environmental objectives in lending and non-lending services.* At present, global environment focused projects tend to be smaller and risky relative to the Bank's traditional lending.

11. All of these priority areas will be considered in further detail as part of the process of developing the Bank Group's Environment Strategy which will fully embrace the global environmental dimension.

Preparation of such a strategy is underway, and will define corporate objectives and targets, and set out monitorable performance incentives for Bank staff. The strategy will guide and enhance the Bank Group's efforts to effectively integrate (or mainstream) environmental objectives, in its development assistance, all in support of our client countries' goals of sustainable development.

12. The global environmental agenda cannot be expected to be of equal importance in all country assistance strategy frameworks. It would be expected to receive the greatest attention in cases where global environmental resources such as biodiversity forms an essential part of the national capital stock, or where there exist significant opportunities for reducing greenhouse gas emissions or sequestering carbon. In this context, the implementation of the Environment Strategy for the Energy Sector and the development and implementation of the Bank Group's Environment Strategy are expected to help define priorities for the Bank's further efforts.

**THE WORLD BANK GROUP AND THE GLOBAL ENVIRONMENT
-PROGRESS TO DATE-**

Goals	Accomplishments/Actions Taken
<p>A. Global Environment Lending Activity</p> <ul style="list-style-type: none"> To expand the overall volume of Bank assistance for the global environment, while meeting obligations as an implementing agency for the Global Environment Facility (GEF) and the Multilateral Fund for the Montreal Protocol (MFMP) 	<ul style="list-style-type: none"> Since inception of MFMP and GEF, Bank Group has approved \$290 million of MFMP funds and \$920 million of GEF funds for eligible projects in client countries. Bank's direct lending and associated cofunding (including GEF) for biodiversity between 1988 and 1997 totaled \$1.8 billion in over 100 projects. Average annual commitments, excluding Bank-GEF funds, increased post-Rio compared to before, i.e. GEF has not crowded out IBRD and IDA lending. IBRD/IDA funding of energy efficiency and renewable energy projects increased since the early 1990s, despite overall decline in Bank-Group lending for energy, and has expanded concomitantly with Bank-GEF financing.
<p>B. Policy Framework and Sectoral policies</p> <ul style="list-style-type: none"> To modify Bank operational policies to take account of global environmental objectives <p>(Note: Implementation of these policies is discussed in chapter III)</p>	<ul style="list-style-type: none"> Established that Bank Group assistance must be consistent with global environmental conventions of operational policy of 1984. Incorporated global environmental impacts in Environment Assessment/Operational Policy (OP/BP 4.01); 1992 Revised operational policy in economic analysis of projects (OP 10.04) to include global environmental impacts in analysis where relevant; established that global externalities are normally expected to be included in sector work and EAs; 1994 Established that CASs are to discuss global environment issues and the role of GEF where appropriate; Established operational policy precluding support to projects that would damage critical habitats and requiring compensation for damage to critical habitats; Bank Forest Policy prevents Bank Group financing of commercial logging in tropical moist forests. Initiated review of implementation of Forest Policy to develop Bank Group's strategy with monitorable indicators. (1997) Bank Group energy policies support lending only where countries commit to improve energy efficiency through policy reform, and urge efforts to promote rural applications of renewable energy. Completed an environmental strategy for the energy sector (will be reviewed by the Board in 10/98)
<p>C. Operational Tools and Methods and Training</p> <ul style="list-style-type: none"> To develop analytical tools and methods specifically to support global environment management assistance 	<ul style="list-style-type: none"> Developed a comprehensive set of monitoring and evaluation guidance (handbooks) for Bank staff and clients: <ul style="list-style-type: none"> ◇ Biodiversity Monitoring and Evaluation Guidelines: 1993 first edition; 1998 second edition

Goals	Accomplishments/Actions Taken
<ul style="list-style-type: none"> • To adopt greener accounting and adjust methodology to suit environment requirements 	<ul style="list-style-type: none"> ◊ Greenhouse Gas Mitigation Monitoring and Evaluation Handbook; 1994 ◊ Ozone Depleting Substances M&E Guidelines ; 1995 ◊ International Waters M&E Guidelines; 1996 • Launched the “global overlays” program to support identification of global environment impacts and improved management opportunities in Bank sector work and assistance with support from donors and NGOs; 1995 <ul style="list-style-type: none"> ◊ Produced global overlays concept guidance papers for specific themes and sectors: <ul style="list-style-type: none"> P Mainstreaming Biodiversity in Agricultural Development; 1997 P Guidelines for Climate Change Overlays in Energy and Forestry; 1996 P Land Degradation and Global Environmental Impacts (draft); 1997 P Biodiversity and Forestry (draft); 1997 P Transport and Climate Change (under preparation) ◊ Bank operational teams assisted client country institutions in implementing six demonstration climate change global overlays for energy sectors in Ukraine, Mexico, Mekong Delta and Russia, forestry in Argentina and transport in Mexico City and Santiago de Chile; plus biodiversity overlays for agriculture in Vietnam, land resource management in Nepal, and forestry in Turkey; initiated an additional 4 climate change and 2 biodiversity overlays. • Developed with Australian Government and Scientists the BIORAP rapid assessment of biodiversity conservation needs and priorities to help client countries define conservation needs in production landscapes and protected area expansion needs. Pioneered these tools in PNG in 1997/8. • Designed and published spreadsheet tools and a Handbook on GHG assessments for operational staff and clients in 1993 and 1995. • Launched global environment science and operational training programs in collaboration with EDI/LLC: 1995-98 • Genuine savings calculations for Latin America and the Caribbean featured in the Environment chapter of <i>World Development Indicators 1998</i>. Full table on genuine savings and resource depletion in <i>World Development Indicators 1999</i>. • Technical assistance on developing greener national accounts provided to South Africa and Mongolia. • Developed standard environmental indicator tables for country assistance strategies, including green accounting aggregates. • Initiated preparation of a “how-to” guide to sector resource accounting for forests, minerals, and water, and for valuing pollution.
<p>D. Climate Change</p> <ul style="list-style-type: none"> • To build capacity in client countries to implement the UNFCCC mandate on Joint Implementation and Activities Implemented Jointly 	<ul style="list-style-type: none"> • Launched with Governments of Norway, the pilot JI program (1993) and undertook demonstration projects in collaboration with Governments of Mexico and Poland; • Launched with Government of Norway the AIJ Pilot program and collaborated with Governments of Barbados, India, Burkina Faso, and Philippines to undertake demonstration projects and associated analysis and learning

Goals	Accomplishments/Actions Taken
<ul style="list-style-type: none"> • To build capacity in client countries to implement Kyoto Protocol • To establish a Global Carbon Market (should the Parties to the Convention find this helpful) to reduce the overall costs of limiting greenhouse gas emissions and to provide Bank client countries every opportunity to obtain an equitable share of the cost savings and access to more environmentally friendly technologies • To form a strategic partnership with the GEF to increase the competitiveness of renewable non-greenhouse gas emitting technologies 	<ul style="list-style-type: none"> • Initiated, using donor funds from Switzerland, Canada, and Finland, the National Strategic Studies Program to build capacity on climate change issues; workshops in India and Slovakia examined the potential of the PCF mechanism with prospective hosts (developing countries and economies in transition). • Developed a preliminary structure for operation of the Prototype Carbon Fund (PCF). However, the design and operation will not be finalized until after the next Conference of Parties to the Framework Convention on Climate Change and the Kyoto Protocol in November 1998. The PCF is expected to commence operations in early 1999, subject to approval of the Bank's Executive Board. • Signed a Memorandum of Understanding with 13 companies and 5 governments that have indicated their willingness, as potential participants, to take part in the development and establishment of the PCF. • Continued research on baselines, and on certification and verification of emissions reductions. • Established a working group to finalize details of a Bank-GEF partnership, which will aim to increase the scale and pace of renewable energy development in member countries; partnership being designed in consultation with IFC, environmental NGOs, and the private sector. Under this arrangement, GEF's contribution to renewable energy projects, currently \$100 million a year, will be significantly increased., to catalyze substantial Bank mobilization of funds for such projects. • Following further consultations with Bank management, the GEF Secretariat, and the GEF Council, the partnership will be piloted in 2 or 3 countries during FY99.
<p>E. Biodiversity Conservation and Sustainable Use</p> <ul style="list-style-type: none"> • To conserve and manage critical forest ecosystems by <u>inter alia</u> establishing strategic partnerships with NGOs and industry to help conserve forest biodiversity 	<ul style="list-style-type: none"> • Launched the Forest Market Transformation Initiative (FMTI) with a strategic coalition of industry, NGOs, and the MacArthur Foundation; 1994. • Established the World Bank-World Wide Fund for Nature Alliance (April 1998) and a facility (July 1998) to build a pipeline of projects and activities to achieve conservation and sustainable management targets including extension of protected areas (50 million ha of new protected forest areas plus a comparable area of existing reserves under effective protection), and by increasing the forest area under sustainable management (100 million ha each of the world's tropical and boreal/temperate production forests under independently certified sustainable management)

Goals	Accomplishments/Actions Taken
<ul style="list-style-type: none"> • Take action to protect the most critically endangered ecosystems • To conserve and manage critical marine and coastal ecosystems through market-led change toward sustainable harvest practices 	<ul style="list-style-type: none"> • The Brazilian government issued a decree (April 1998) to create 25 million ha of new protected forest areas in the Amazon, and the Alliance is looking for ways to help the government implement the decree. • Established (January 1998) an ad hoc forum of forest industry CEOs and environmental NGOs, and issued recommendations on conservation, forest management, and the creation of markets for non-timber forest products. • Established under FMTI, with World Resources Institute, Forest Trends (spring 1998) as an independent non-profit NGO with Bank and MacArthur funding. A strategic coalition of the private sector, financial institutions, NGOs, and research bodies, FT provides information on forest management and serves as a forum for resolving contentious issues. • Launched (June 1998) the Carbon Forestry and Land Use Management Action Plan to evaluate the development benefits of trade in forest and soil-based carbon offsets within framework of the Kyoto Protocol. • Initiated a study with Conservation International under the Critical Ecosystems Partnership Fund (CEPF) to evaluate the key pressures on four terrestrial ecosystems and develop a pipeline of projects as a step toward the detailed design of the CEPF. • The year-old Marine Market Transformation Initiative successfully launched three pilots in FY98: <ul style="list-style-type: none"> ◊ Support to an NGO trade association to test and certify live coral reef fish for aquariums (Philippines); ◊ Assessment of markets for the reef food fish industry and supply alternatives (including cage culture of high valued species: Hong Kong and Taiwan); and ◊ Consensus building for developing a Code of Conduct for Sustainable Shrimp Farming (Thailand). • Exploring with Donors and other international agencies (esp. FAO) the development of a global Forum for Sustainable Fisheries (FSF) to catalyze a global commitment to sustainable management of the world's depleted and over harvested fisheries and assist country clients to adjust fishing effort to sustainable levels; 1998.
<p>F. Stratospheric Ozone Depletion</p> <ul style="list-style-type: none"> • To eliminate the production of ozone-depleting substances in Russia 	<ul style="list-style-type: none"> • In conjunction with Russia's State Committee for Environmental Protection (SCEP), designed a plan, signed by each of Russia's 7 ODS -producing enterprises, to eliminate ODS production by the end of 2000. The initiative is expected to be supported by \$27 million in grant funding. A donor roundtable in Moscow is scheduled for October 1998.

Goals	Accomplishments/Actions Taken
<p>G. Desertification and Land Degradation</p> <ul style="list-style-type: none"> • To assist the Desertification Convention through a rural strategy emphasizing the links between poverty and land degradation • To establish in partnership with others, mechanisms for mobilizing financing and coordinating implementation of the Desertification Convention 	<ul style="list-style-type: none"> • In collaboration with UNDP, initiated assistance to member countries to develop National Action Plans. • Finalized a best practice study, developed training modules, organized three seminars, and established a knowledge node on technical and financial issues in dry lands management • Modus Operandi of the Global Mechanism, which is managed by the International Fund for Agricultural Development (IFAD), UNDP, and the World Bank, established during the first two meetings (March and July 1998). • Established a partnership between MNA countries to participate in the desertification initiative under the Middle East peace process.
<p>H. Water</p> <ul style="list-style-type: none"> • To support the Global Water Partnership, which offers an opportunity to solve water issues in a more holistic manner • To support, in collaboration with IUCN, the establishment of the World Commission on Dams to raise the environmental and social welfare standards for large dams • To support regional seas programs • To make water an economic asset given that it is a scarce resource 	<ul style="list-style-type: none"> • The new Global Water Partnership has established a global technical advisory committee; is preparing its work program and establishing regional technical advisory committees for Southern Africa, Western Africa, Latin America, and Asia; and has organized an African Water Resources Management Policy Workshop to be held in Tanzania in January 1999. • The World Commission on Dams, established in June 1998, is finalizing its staffing, strategic work plan, and research program. • Expanded implementation of Helsinki Commission objectives in the Baltic Sea. • Coordinated preparation of a strategic action plan for the Red Sea and the Gulf of Aqaba. • Designed a series of investment projects for the Black Sea. • Contributed to the ICZM initiatives for the protection of shared marine ecosystems in the western Indian Ocean, western Caribbean, and Black Sea • The Water Resources Management Policy emphasizes efficient water use and sustaining productive water systems. The Bank, recognizing that institutional and policy reforms are just beginning, is: <ul style="list-style-type: none"> ◊ through the Africa Water Resources Management Initiative, working to strengthen water management institutions in 14 nations and the transboundary Nile, Southern Africa, Volta and Senegal river basins; and ◊ promoting water policy reforms, including an increased private sector role in urban water management, in LAC, MENA, and South Asia.

1. INTRODUCTION

1.1 The Global Environment Facility (GEF) Council has requested the World Bank Group (the Bank Group) for a progress report and action plan on the Bank Group's efforts to introduce, or mainstream, the global environment in its operations. This paper has been prepared by Bank Group Management in response to this request. The background to the GEF Council's request is the Statement of the First GEF Assembly in New Delhi which urges that the "GEF Implementing Agencies should promote measures to achieve global environment benefits within the context of their regular programs and consistent with the global environment conventions.." The notion of such mainstreaming of global environmental objectives in the Bank's work is embedded in the Instrument for the Establishment of the Restructured GEF.

1.2 This paper does not, therefore, set out a Global Environment Strategy to guide the Bank Group's development assistance. Such a strategy has to form an integral part of a broader Bank Group Environment Strategy which recognizes the links between local, national and global environmental issues, and which should determine in which areas of this spectrum of environmental concerns and issues the Bank Group has a comparative advantage. The preparation of such a strategy is underway, and the opportunity to prepare this present paper for the GEF Council has added momentum to the in-house debate on the objectives and means of mainstreaming environment and its global dimension in sustainable development and the role the Bank Group should play in respect to this agenda.

1.3 The paper begins (Chapter 2) by explaining how the Bank Group sees its role in supporting its country partners in their efforts to make development sustainable and implement their commitments under the global environmental conventions. It goes on to summarize progress made in implementing that role (Chapter 3). The paper concludes (Chapter 4) by addressing challenges for the Bank Group to address as part of the development of a Bank Group Environmental Strategy, and by setting out proposed main elements for such a strategy that are of particular importance for the global dimension of the broader mainstreaming effort. These elements will be further developed and integrated with others, as the preparation of the Bank Group's Environment Strategy paper proceeds.

1.4 It follows that the paper is not limiting itself to the Bank Group's role as an Implementing Agency of the GEF and/or Multilateral Fund of the Montreal Protocol (MFMP). The integration of its GEF and MFMP programs with its other programs, however, is seen as an essential means of promoting the global environment within the Bank Group. The global environment issues with which it is concerned are climate change, loss of biological diversity, land degradation/desertification, and degradation of shared fresh and marine waters.

1.5 While reference is made throughout this paper to the Bank Group, no attempt is being made to systematically review global environmental mainstreaming in the context of all individual members of the Group. Focus is on the World Bank (the Bank) and IFC.

2. THE CHALLENGE OF MAINSTREAMING THE GLOBAL ENVIRONMENT

THE BANK GROUP'S COMMITMENT

2.1 The goal of meeting basic human needs is increasingly being threatened by local and regional problems such as air and water pollution, and by global environmental problems such as climate change, loss of biological diversity, land degradation and desertification, stratospheric ozone depletion, deforestation and unsustainable forestry, and degradation of fresh and marine waters. A number of regional and global conventions and/or agreements have been negotiated to address these problems. The member countries of the Bank Group have virtually all ratified these global conventions, providing evidence of the growing importance that all countries place on the environment and environmentally sustainable development.

2.2 The commitment by the Bank Group to the alleviation of poverty and sustainable development recognizes that these goals are only attainable if local, regional and global environmental issues are addressed. Senior Bank Group Management has in the last year reaffirmed this commitment. In his statement on World Environment Day June 5, 1997, Managing Director, Mr. Caio Koch-Weser presented a set of measures to protect air, land, and water resources, that the Bank Group believes should be carried out on a global scale. Later the same month, the President of the Bank Group, Mr. James D. Wolfensohn, speaking at the UN Special Session, outlined a plan of action that the Bank Group will pursue to help forge a global partnership that promotes equitable approaches to global environmental issues.

THE CLIENT COUNTRY PERSPECTIVE: TRADE-OFFS AND CONSTRAINTS

2.3 The Bank Group's client countries have irrevocably committed themselves to address the degradation of the "global commons" on the basis that they will suffer, along with all others, if insidious trends of global environment deterioration continue. They face, however, difficult decisions in defining the appropriate level of effort they should devote to global environmental management. In particular, client countries perceive real and critical *trade-offs* between

- meeting pressing short term needs such as food, water supply, and sanitation services for the poor; and investing in environmental management for the medium and long term;
- harvesting natural resources to generate foreign exchange urgently required to purchase essential imported supplies, or simply to meet the basic needs of the urban and rural poor, and the need to manage these resources for long term, sustainable use (ref. Asia and Russia situation today); and
- within the broader environmental agenda, between expenditures on local and regional pollution abatement and expenditures to take actions on global environmental change and its local impacts.

2.4 Are these real trade-offs? How far do the so called "win-win" options (i.e. those that simultaneously support the domestic economy and the environment) go? Can Convention-created opportunities to address global environment degradation give impetus to address short-term environment and development concerns? How much is too much attention to the global environment for economies in social and economic crisis? Getting the appropriate balance is not easy, especially when political regimes tend to have a short term time horizon. These questions reach to the core of defining sustainable

development in practice, and make the Bank Group's task of mainstreaming the global environment a particularly challenging one.

2.5 These perceived trade-offs impact the importance that countries attach to environmental priorities generally, and global ones in particular. In addition, client countries face a number of specific constraints that limit their ability to take action on these priorities.

- The absence of markets for trading of certain global environmental good and services *limit the economic incentives* to individual countries for taking action on the global environment.
- *Weak policy framework* in sectors, such as energy, forestry and water resources, and environmental management, combined with insufficient political commitment, limit the incentives and scope for effective action on environmental issues generally.
- *Institutional weaknesses*, particularly the lack of technical skills on environmental issues, frequently constrain actions on environmental management and environmental issues generally; and environmental externalities, global ones in particular, are rarely integrated into sector development strategies.

OBJECTIVES AND ROLE OF THE BANK GROUP

2.6 The Bank Group is committed through its development assistance to work with its clients to overcome the above constraints, and grapple with the tensions that determine the level of effort that individual countries will apply toward achievement of global environmental objectives. It proposes to do so in the following four main ways:

- enable its clients to identify and capture “win-win” opportunities , e.g. reducing greenhouse gases in a manner which simultaneously addresses local air quality concerns and meeting energy needs, or conserving biodiversity while supporting sustainable food production;
- provide country partners access to global financing mechanisms, such as the GEF, which fully compensate for the cost of actions that do not produce sufficient economic gain to be undertaken in the national interest alone;
- help client countries' access and operate on markets for global public goods in order to secure national economic gains from acting on global environmental issues, (e.g. carbon offsets trading); and
- address immediate and projected negative impacts of global environmental degradation, such as climate variability and desertification, on national development.

2.7 The Bank Group's support for its client countries' efforts to address global environmental objectives forms part of its broader program to mainstream the environment in its lending and non-lending services. This effort has been underway for a decade or so. Global environmental concerns have come to the fore since the Rio Earth Summit. While these concerns involve new and difficult issues related to global public goods, they have important links to local and regional environmental impacts. As such, they need to form part of the broader country assistance dialogue on environment and sustainable development. Also, the Bank Group will assist client countries, taking due note of the limitations that the international

conventions place on the obligations of client countries to take specific actions on global environmental issues.

2.8 To effectively engage our client countries in a dialogue on national sustainable development and the global environment, the Bank Group needs: (a) a supportive set of operational and sector policies; (b) analytical tools to evaluate sources, scale and mitigation options for global environmental impacts; (c) staff that are aware of global environmental issues and their importance, and have the skills and incentives to engage country clients in a dialogue on such issues; (d) new partnerships and products that help promote client countries access markets for global public goods; and (e) a fully mainstreamed Bank-GEF program that helps catalyze the broader efforts of global environmental mainstreaming in the Bank Group. Resources and incentives are needed to effectively mobilize this capacity.

2.9 As shown in the following chapter, many of these requirements have already been put in place or are being addressed as the Bank Group has emerged as a major financier of global environmental projects, and provided leadership to several important areas of global environmental management. Much remains to be done, however, for the full potential of this leadership to be realized. Most importantly, and as discussed in Chapter 4, the Bank Group's objectives and means for supporting global environmental management need to be fully integrated with its overall strategy for the environment.

3. REVIEW OF PROGRESS MADE

3.1 It is now ten years since the Bank Group began embracing global environmental issues in its development assistance program. It began in 1988 when the Bank became an implementing agency for the Multilateral Fund for the Montreal Protocol (MFMP), the global financing mechanism for the phasing out of ozone depleting substances. It continued in 1990 with the Bank Group agreeing to manage the GEF Pilot phase, and subsequent to the restructuring of the GEF in 1994, to serve as one of its three implementing agencies. Total MFMP and GEF resource transfers to client countries approved by Bank management since then amount to over US\$ \$1.2 billion (GEF \$920 million and MFMP \$290 million).

3.2 This growth in the Bank Group's targeted lending for global environmental purposes is an important achievement in and of itself. The greater challenge, however, is to make the Bank Group's overall development assistance services as globally environmentally-friendly as they realistically can become within its overall mission and resources available. An overview of progress made in addressing the global environment is given in the table "The World Bank Group and The Global Environment-Progress to Date" (attached to the Executive Summary). It focuses on the Bank Group's institutional and thematic goals in respect to global environmental issues, and the activities and programs that support these goals. The steps taken towards these goals represent a commitment by the Bank Group to play a leading role in addressing global environmental degradation. This commitment reflects the experience and lessons learnt by the Bank Group in the course of implementing the GEF and the MFMP programs.

3.3 The Bank Group's lending and non-lending services for global environmental management are relatively young, and the contributions of these services to global environmental benefits typically have a long gestation period. Hence it is not possible at this stage to report on the impacts of the Bank Group's development assistance on the global environment.

LENDING FOR THE GLOBAL ENVIRONMENT

3.4 Bank Group lending supports the global environment directly and indirectly. Projects or project components explicitly address climate change issues, conservation and sustainable use of biodiversity, the phasing out of ozone depleting substances or the protection of international water bodies. An overview of this direct lending for the global environment by major thematic area is presented in Annex 1. It leads to the following conclusions in respect to the two main thematic areas:

For biodiversity conservation:

- The Bank's lending and associated co-funding for biodiversity conservation totals \$1.8 billion in over 100 projects approved between 1988 and 1997, involving IBRD, IDA, GEF and the Brazil Rainforest Trust Fund. Annually, commitments from these sources and their leveraged co-funding have risen from \$21 million in 1988 to \$411 million ten years later.
- The Bank's average annual non-GEF lending for biodiversity conservation has increased during the post Rio period. Hence, the GEF has not crowded out IBRD and IDA lending.
- The bulk of the Bank's lending and co-funding has supported protected area management. More recently, however, Bank funds, often catalyzed by GEF resources, have begun flowing toward conservation or sustainable use of biodiversity in the broader agricultural landscape.

For renewable energy/energy efficiency/climate change:

- Despite an overall decline in Bank lending to the energy sector since the early 1990s, IBRD/IDA commitments for energy efficiency and global environment friendly renewable energy development have increased over this period.
- As in the case of biodiversity, GEF funds have not displaced Bank Group financing as Bank's own lending for renewable energy and energy efficiency (geothermal and hydropower excluded) has increased concomitantly with GEF financing. Projects in this area remain few in number, are concentrated in one region (Asia), and have on average accounted for 10-12% of Bank energy lending since the early 1990s.

3.5 Bank lending for agriculture, forestry, energy and other sectors also addresses global environmental concerns indirectly. For example, Bank lending in support of energy pricing reform creates incentives for adoption of climate friendly technologies. A recent Bank study found that since 1994, the proportion of the Bank's energy development portfolio that is classed as highly greenhouse emissions-intensive fell from about 50% to 11% as more loans than before focused on reform and restructuring, in addition to energy efficiency, and renewables. Similarly, support for agricultural intensification or rural non-farm employment can serve to reduce pressures on natural habitats and biodiversity. And, funding for community based natural resource management frequently leads to more sustainable use of forest and biodiversity resources. These are all "win-win" opportunities where the pursuit of economically efficient and socially feasible solutions to sector development also produce gains for the global environment.

3.6 While the scale and impact of this indirect lending for the global environment remains to be quantified, its potential for expansion is substantial. Indeed, the central challenge for mainstreaming the global environment in the Bank Group lies in developing the skills and the incentives for staff to engage country partners in identifying and evaluating global environment-friendly alternatives for the design of sector investment and other operations, noting that where such alternatives involve additional costs, GEF or MFMP resources may be used to offset them.

3.7 The compatibility of the Bank Group's broader project portfolio with the Bank-GEF objectives for global environmental management has been raised by some as an issue. Specifically, it has been questioned whether continued Bank lending for greenhouse gas intensive fossil fuel-based energy projects is consistent with the Bank-GEF objective to promote climate-friendly energy technologies. In response, it is important to note that the Bank's primary mission is to reduce poverty and promote economic development. The energy needs of the developing countries are great, and increased consumption of energy is essential for economic growth. The challenge for development institutions, such as the Bank Group, is not to bring about a rapid total phase-out of fossil fuels in client countries, but to make their use as clean and efficient as possible in the short- to medium-term, and to put measures in place now to induce a long-term transition to low- and no-carbon energy sources. This shift towards more efficient and cleaner energy use is already becoming apparent in the Bank Group's regular operations. The GEF is a key instrument in catalyzing this shift, but its resources are still modest relative to the energy financing needs of our client countries.

COUNTRY ASSISTANCE STRATEGIES, ECONOMIC AND SECTOR WORK, OPERATIONAL TOOLS AND TRAINING

(A) COUNTRY ASSISTANCE STRATEGIES

3.8 The Country Assistance Strategy (CAS) documents the understanding reached between the Bank Group and the client government on the priorities for Bank development assistance. It is influenced by all aspects of the country dialogue and the country economic and sector work, as well as by national and sectoral strategies and action plans. Unless such sector and planning work incorporates relevant global environmental concerns linked to national or sectoral development priorities, and the results are fed into the CAS formulation process, the CAS document is unlikely to be adequately informed on this matter.

3.9 Experience to date indicates that incorporating environmental issues generally in the CAS formulation process is a challenge. This is particularly true for global environmental concerns, and few CAS documents explicitly address such concerns. The reasons vary from overriding concerns for short to medium term economic problems and low client interest, to lack of familiarity with analytical tools to analyze the issues, and insufficient knowledge of Bank staff of client country obligations under the global conventions.

3.10 Having said that, the importance of the global environmental agenda in the country assistance strategy is not, and cannot be, the same for all client countries. It would be expected to receive high priority in cases where global environmental resources, such as biodiversity, forms an essential part of the national capital stock, or where there exist significant opportunities for reducing greenhouse gas emissions or sequestering carbon

3.11 The Environment Family is working to enhance the consideration of the environment generally in the CAS process, with the focus first on national environmental issues and secondly on global issues. Initial work has been spearheaded by the Africa region, which has put in place a “CAS greening” program that includes global environment issues. About fifteen CASs have been “greened” under the program. This effort will be intensified in FY99 with 5 to 6 countries selected for intensive work on CAS-environment linkages.

(B) COUNTRY ECONOMIC AND SECTOR WORK

3.12 Local environmental impacts have generally been recognized and addressed with increasing frequency in Bank sector and country analysis. This is less true, however, with respect to global impacts. Country Environmental Strategy papers prepared by the Bank or National Environmental Strategies and Action Plans prepared by client countries have largely suffered from the same shortcoming, i.e. poor integration of global environmental concerns with sectoral development.

3.13 The lack of familiarity among Bank staff with the “development – global environment links” and knowledge of how to evaluate them are in themselves barriers to addressing global environmental issues in the country dialogue. Hence, improving staff awareness and access to relevant operational tools and methods with which to engage country partners in evaluating global environment-friendly development options or investment projects is of the highest priority. Thus, to provide staff with the tools to apply the Bank’s policy that global externalities should “normally” be covered in country economic and sector work (para. 3.33), the Bank Group in 1995 launched the Global Overlays Program in partnership with other donors and NGOs (para. 3.16).

3.14 More recently, and in the context of the possible development of market-based instruments under the Kyoto Protocol to the UNFCCC, the Bank Group, in collaboration with other donors, has begun a program of “National Strategy Studies” (NSS). The program aims to help client countries explore the opportunities and benefits of the different market-based mechanisms. Since the program has just commenced, it is premature to pass judgement on its effectiveness. Nevertheless, by exploring the future implementation of emissions trading mechanisms, the program provides an appropriate vehicle for the identification of new Bank Group projects. The first projects have developed dialogue for potential collaboration with interested donors on Activities Implemented Jointly (AIJ).

(C) OPERATIONAL TOOLS AND TRAINING

3.15 How do alternative agricultural development paths impact biodiversity and how do we value biodiversity losses at the national and global levels? How do we assess greenhouse gas emissions from alternative power sector development programs and how do we analyze the options for emission reductions? How do we measure progress in reducing greenhouse gas emissions or impacts on biodiversity? To help answer these and similar questions, the Bank Group has, in partnership with others, launched the Global Overlays Program and included the global environment in its work on developing environmental indicators.

3.16 The Global Overlays Program has as its objective to demonstrate, through a set of specific country studies, how biodiversity conservation or greenhouse gas reduction objectives can be included side-by-side with traditional objectives in sector analysis and planning. To support such studies, initial conceptual guidance papers for specific themes have been prepared or are under preparation. Nine overlay studies have so far been completed by Bank teams working with client country institutions; six for energy/transport and climate change and three for forestry/agriculture and biodiversity. Another six studies are in progress.

3.17 The success of the program has to be measured in terms of its ability to first, help promote the inclusion of global environmental issues and concerns in relevant parts of the Bank’s sector work (and thereby inform the CAS process), and second, help identify global environment-friendly investment projects. To date, the impact of the program on both these fronts has been limited. Nevertheless, the country studies have helped to demonstrate synergies between local-regional pollution reduction and greenhouse gas emissions mitigation and methodologies for measuring economic benefits from biodiversity conservation. They have also led to the identification of several projects for GEF funding. In addition, the country studies have supported the technical competence in client institutions, and as such, enhanced the dialogue with the client countries involved on global environmental issues.

3.18 Looking ahead, the Bank operational units will become more directly involved in program planning and management of the overlays program so as to ensure that their priorities and opportunities for building global environmental objectives into sector work are addressed. Priority in allocating program resources will be given to countries and sectors which offer the best prospects for capturing development and environment links of fundamental importance in the national or sectoral economies. Finally, program funding has, up to the current fiscal year, relied almost exclusively on trust funds from bilateral donors. Regular Bank budget support for the program was made available to the ENV Family for the current fiscal year to ensure adequate Bank staff input and enable skills to be internalized. Further expansion of the program will depend on the availability of resources.

3.19 Environmental Indicators. The Bank Group has been actively involved in the development and use of environmental indicators, both at the project level, where the M&E requirements of GEF projects have

spurred rapid development in the use of indicators (see Executive Summary Attachment, Part C) and at the national level. In the latter context, the Bank Group has played a key role in the development of the OECD-DAC Development Goals for the 21st Century exercise. As part of this exercise, a set of 22 DAC-Goals indicators have been identified to monitor the progress of developing countries towards more sustainable and equitable growth. The set includes six on environmental themes, including ones for energy use, GHG emissions, and freshwater use. By highlighting these concerns, the indicators focus on a number of issues of global importance. By permitting comparisons across countries, one can begin to monitor what is happening at the global level. More experience is required with overall global environmental indicators, however, if we are to effectively incorporate global objectives into development planning.

3.20 Green Accounting. The idea of natural resource accounting -- so-called "green accounting" whereby the depletion or use of natural resources is explicitly accounted for in estimating traditional measures of national growth such as GDP-- has been around for some time. A number of pilot studies have been carried out over the past 10 years (some with World Bank assistance) but few countries have continued to develop and maintain complete Green Accounts. Rather than focussing on single indicators such as "green GDP", or on complex and extensive systems of accounts, the Bank has emphasized resource accounts (the building blocks for Green Accounts) for selected sectors of national importance (e.g. minerals, fisheries, forests), which are both more realistic to carry out and maintain and have more direct policy relevance.

3.21 Present efforts in the Bank aim to assign values to environmental change in selected sectors. A practical "how-to" guide to sectoral resource accounting is being prepared. Sectoral level analyses have been carried out or are presently underway in a number of countries in Asia, including China, India, Indonesia, and Mongolia; work is just beginning in southern Africa. To date, however, there has been little impact on global objectives because the initial focus has been at the national level. While sectoral accounts could reflect global objectives, the main constraints have been a lack of interest in using this approach on the part of governments, lack of data, and lack of trained people to do the studies when there is interest. To address these concerns, the Bank has spearheaded the development of two different types of environmental/economic indicators derived from these same sectoral accounts -- National Wealth measures (a stock concept) and Genuine Savings estimates (a flow measure). In both cases, the management of environmental resources and the production of pollution is factored into the measures to help provide useful insights to policy makers on the sustainability of a country's development path. While global values are only partially reflected, they can easily be accommodated within this analytical framework.

3.22 Training -- Internal and External The Bank Group's *internal training* program on global environmental issues has up to recently been largely limited to the yearly GEF Workshop for task managers. In FY98, however, there was a major revision of the entire environment training program for Bank staff in FY98. An important new thrust in this revised program is the global environmental agenda. The environmental economics training program now covers mainstreaming of environmental concerns, both in policy making and in linking macroeconomics and the environment. Specific workshops on CAS/environmental links, and global inter-linkages are also planned. Furthermore, the new training program for IFC operational staff on the "Revised IFC Environmental and Social Review Policy and Procedures" will include consideration of global environmental issues.

3.23 Notwithstanding these developments, staff training on global environment issues tends to focus primarily on the global conventions and the obligations they impose upon countries, but does not yet give adequately attention to how sectoral investment programs or projects can benefit by incorporating global environment components. The Global Overlays Program and its experience in deriving good practice should help address this deficiency. Finally, the in-house environmental training program needs to include

not only staff but also managers. The decision to include an environmental module in the Executive Development Program will in part help address this objective.

3.24 Turning to the Bank Group's *external training* program on global environmental management issues, the Bank Group, in collaboration with UNDP and UNDP, has presented 40 country and sub-regional GEF/global environment training workshops world-wide over the past three years, serving 2,500 client country representatives. These workshops have provided briefings on key global environment issues and the role of the related conventions. In addition, the Africa Region has sponsored country capacity building activities on climate change through two sub-regional conferences; integrated coastal zone management, via the SEACAM network; and six environmental assessment workshops.

3.25 A new initiative "Integrating Global Environmental Concerns in National Sustainable Development" by the Economic Development Institute (EDI) is examining practical ways in which global environmental objectives can be incorporated in sectoral, countrywide, and regional sustainable development programs. It takes the form of training and learning seminars on global environmental issues for policy makers and representatives from other stakeholder groups. The program seeks to: (a) raise awareness of the economic and social costs arising from global environmental problems; (b) assess the constraints faced in taking measures consistent with global environment improvement; (c) improve understanding of the roles and potential contribution of government and various sectors of civil society, and (d) identify prototype responses (local, national, and transnational) that would incorporate global environmental initiatives within programs of national sustainable development. The initiative has already piloted policy seminars with senior government and multi-stakeholder participation from developing countries on land degradation and agricultural intensification (Middle East and North Africa Region), biodiversity and land use (South Africa and Central America), and coastal zone management (South Pacific).

3.26 Knowledge management is a growing mechanism for capturing, organizing and sharing information and best practice, and Bank Group Senior Management is committed to make it a central element of the "new Bank". The new electronic Knowledge Management (KM) System incorporates nodes specializing in global environmental themes in addition to two other nodes that focus on GEF and MFMP Operations. These nodes have catalogued a series of knowledge objects electronically, which can be easily accessed, searched and downloaded.

OPERATIONAL POLICIES

3.27 The Bank-Group's operational policies have developed, or been modified, to address environmental concerns. Global environmental concerns have reflected in these policies following the Rio Earth Summit in 1992. Hence, the Bank Group has a set of operational policies and associated procedures that support the design of environmentally sound projects.

3.28 To reinforce the importance of strict compliance with environmental and social "safeguard" policies, a Safeguard Compliance Unit was recently established in the ESSD Vice Presidency. Its responsibility is to audit the implementation of these safeguard policies and related procedures during project preparation and supervision, and to report to senior management on a regular basis. The Unit will also provide advice on policy issues and mandatory training of staff.

3.29 Policies on Environmental Assessment (EA) and Natural Habitats (OPs 4.01 and 4.04) require inter alia that the natural environment and trans-national and global environmental issues be taken into account, preclude Bank support to projects that would damage critical habitats, and provide for

compensation for damage to critical habitats. While biodiversity concerns are generally well covered in the application of these policies, climate change issues are addressed less frequently.

3.30 The Second Bank-wide EA Review (1997) highlighted the need to move EA upstream to make environment part of the criteria used for strategic choices and policy making. Follow up action includes the Strategic Environment Assessment (SEA) initiative which responds to country needs for primarily sectoral and regional EAs. It is now being piloted in the Bank's Africa region in the areas of river basin management, and the mining, rural development and road transport sectors.

3.31 More frequent use of SEAs addressing global environmental impacts, as appropriate, will help increase the effectiveness of the EA and Natural Habitats policies and results on the ground. Supporting better implementation of mitigation plans through project supervision is another priority, as is the adaptation of environmental and social assessments to various forms of private sector oriented projects, such as financial intermediary, privatization and guarantee operations. Through awareness building and dissemination of good practice, SEA should be an efficient tool to make project-specific EA more of an adjustment within the proper sectoral or regional policy frameworks.

3.32 Another initiative responding to the call for moving EAs upstream is the use of Energy-Environment Reviews (EERs). Responding to the needs of client countries, these reviews are designed to cover the whole energy chain and the whole range of its environmental impacts (global, regional, and local). EERs will also help map out Bank Group assistance on the supply and demand side of the energy sector as well as pollution avoidance and control in areas such as efficiency, conservation, rehabilitation, and decommissioning. Of equal importance, they will highlight the possible institutional and financing mechanisms that can be used. The aim is to work with our client countries in carrying out a program of five to seven EERs in FY99 and up to 10-15 per year thereafter.

3.33 The policy on Economic Evaluation of Investment Projects (OP 10.04) states that global environmental impacts are normally to be identified in sector work and EAs. As discussed above (para. 3.13) the coverage of global environmental impacts in sector work needs to be improved. The case for such coverage varies between sectors. One would expect the linking of sector analysis to global environmental impacts to be most relevant in sectors like agriculture, energy, fisheries, forestry, mining and transport.

3.34 The policy directive also requires global externalities to be included in the economic analysis of GEF-financed projects, or when the recipient country has made a commitment under a related international agreement. At the project level the policy is effectively applied. However, as clients have not committed to internalizing global environmental externalities under binding international agreements, it effectively applies only to GEF projects.

SECTOR POLICIES

3.35 Key sector policies and strategies for energy, forestry and rural development are being revised to make them fully responsive to environmental issues, including those of global concern.

- The Bank Group's energy policies support lending only when countries commit to improving energy efficiency through policy reform¹ and promote renewable energy. The Bank's Operations Evaluation Department has concluded that, while good progress has been made on the sector reform agenda, the volume of lending for energy efficiency, renewables and rural energy remains modest. This is largely because environmentally friendly energy projects are more labor-intensive, borrower commitment to fundamental reform is often weak, and energy efficiency and renewable energy are relatively new business products for which skills and experience are scarce.
- The Bank's Forestry Policy (1991) precludes Bank Group financing of commercial logging operations in moist tropical forests, and involves the private sector and local people in forestry and conservation management. The Bank's lending operations in the forest sector are conditional on government commitment to sustainable management and conservation-oriented forestry. A review of the implementation of the forest policy is underway, with the intention of developing a forest sector strategy with monitorable progress indicators.
- Rural Development Strategy. The Bank Group's rural development strategy (1997) recognizes the link between rural development and global environment issues. To help build this link into Bank operations, global environmental concerns are being integrated into sector activities through a Sustainable Land and Crop Thematic Team. Agriculture sector performance indicators are being revised to include global environmental concerns. The topic of land degradation and desertification is given special importance. With IFAD and UNDP, the Bank Group is helping to establish mechanisms for mobilizing financial resources for implementation of the Desertification Convention.
- Water Resources Policy. The Bank Group's Water Resources Management Policy (1993) acknowledges that protection of water resources is essential for sustainable development and calls for a comprehensive management approach. It emphasizes rigorous attention to maintaining biodiversity and protecting ecosystems in water project design and implementation.

NEW PRODUCTS AND STRATEGIC PARTNERSHIPS

3.36 Over the past year, the Bank Group has embarked on a number of new initiatives that emphasize the global environment or global public goods (details in Sections D and E of the Attachment to the Executive Summary).

- The establishment of a *Prototype Carbon Fund* is being examined by the Bank to help develop a market mechanism for the transfer of carbon offsets. The PCF would fund GHG reducing

¹ In certain cases, IFC may finance efficient private sector investments in the energy sectors of countries that are in the early stages of restructuring or reform where such investments support the momentum towards further sectoral restructuring or policy reform. (*Fuel for Thought: A New Environmental Strategy for the Energy Sector*, final draft, July 15, 1998)

projects by covering the cost of emission reduction measures above a baseline, through contributions made by industrial countries and private sector companies. The proposal will be brought to the Bank's Executive Board for endorsement only after the COP4 in November 1998.

- A strategic *Bank-GEF partnership for renewable energy technologies* is under development . The objective is to increase the competitiveness of new and renewable non-GHG emitting technologies by developing a large-scale program of renewable energy investments. GEF is expected to earmark funds against programmatic objectives, and the Bank Group to ensure leveraging with non-GEF financing (own and other) for Bank supported projects in client countries.
- The Bank Group has recently launched two *Market Transformation Initiatives* with coalitions of industries and NGOs that aim to promote market-led change to the adoption of ecologically sustainable forest and marine production and harvesting practices. The Bank Group is exploring opportunities for linking GEF funding to Bank supported country projects to meet eligible costs for reducing the barriers to the adoption of such practices.
- Several strategic partnerships have been established to support conservation and sustainable use of biodiversity in forestry. Among them are: (i) *The World Bank -World Wide Fund for Nature Alliance* to help achieve forest conservation and sustainable management targets through the preparation of a pipeline of projects and activities; (ii) *Forest Trends*, an independent non-profit NGO (together with World Resources Institute), to provide information on forest management and serve as a forum for resolving contentious issues; and (iii) a study on the evaluation of pressures on four critical terrestrial ecosystems to develop a pipeline of projects (with Conservation International) as a first step in the detailed design of the Critical Ecosystems Partnership Fund.

3.37 The above initiatives are all undertaken to help client countries overcome constraints they face in integrating the global environment in national sustainable development. They are still mostly at early stages of establishing dialogue and identifying opportunities, and their impact on the Bank Group's development assistance, and in particular project portfolios in energy, forestry, coastal zone and marine areas, can only be judged later.

MAINSTREAMING GEF IN BANK OPERATIONS

3.38 The Bank Group views its role as an implementing agency for the GEF (and the MFMP) as an opportunity to catalyze broader awareness and preparedness among management and staff to engage in a development assistance dialogue with its clients on global environmental issues. Ensuring that the Bank's GEF program is fully mainstreamed in Bank Group operations is, therefore, an important element in the Bank Group's broader global environmental mainstreaming effort.

3.39 To this end, Bank management has, over the last year and a half, designed and implemented, in consultation with the GEF CEO, a set of actions to reduce overall transactions costs of processing Bank-GEF assistance, aligning Bank and GEF processing procedures and documentation, and integrating GEF projects in the Bank's portfolio management.

3.40 As a result, the format and contents of the Bank's GEF project documents have been harmonized with the Bank's standard documentation; the internal review process has been aligned with the external

review steps; the integration of GEF operations into largely portfolio management, business planning, quality control functions and service standards has been completed; the responsibility for management of the GEF administrative budget has been transferred from the Bank's central GEF Coordination Unit to the operational departments; and GEF policies, operating procedures and processing guidelines have been developed and fully integrated into the Bank's knowledge management system.

3.41 The implementation of the Bank's GEF program inevitably involves reporting, documentation and review requirements necessitated by the external GEF governance. To the extent that these requirements can be reduced and/or simplified the transactions costs of processing Bank-GEF projects will be reduced and mainstreaming facilitated.

3.42 One outstanding problem in the streamlining of the GEF in Bank operations is the disincentives for operational managers and staff to engage in GEF work that has been created by the less-than-full cost funding of indirect incurred by operational units in GEF project processing. This shortfall in funding, caused by the Bank's practice not to charge its full management costs to the GEF, has now become transparent under the Bank Group's new uniform costing policy. Steps are under consideration for addressing this problem within the current Bank-GEF budgetary envelop.

PERFORMANCE INCENTIVES

3.43 The global environment business is new. Solutions to sustainable and cost-effective mitigation of greenhouse gas emissions or conservation of biodiversity require an innovative and flexible approach to project design, requirements that translate into risk-taking through small to modest sized operations; all this in contrast to the regular large-volume projects that traditionally have characterized the Bank portfolio. A multiplicity of stakeholders add to the challenges and complexity of the dialogue with client countries. As a result, the costs of linking the global environmental dimension to our regular sectoral or project dialogue is still perceived as high by many managers and staff. There is a need, therefore, to examine how these costs can be reduced, and to make sure that the budgeting, programming, and performance evaluation and reward systems support the integration of the global environmental agenda into Bank Group operations.

SUMMARY OF PROGRESS

3.44 The preceding stocktaking of the Bank Group's efforts to mainstream global environmental management objectives in its operations shows that important progress has been made.

3.45 First, as an implementing agency for the GEF and the MFMP, the Bank Group has satisfied an increasing demand from its clients (governments and private sector) for access to grant funding from the global financing mechanisms. In so doing, the Bank Group has acted to streamline the processing of these operations, in particular the GEF projects, with standard Bank documentation and review procedures, and to include them in the Bank's portfolio management and business planning systems. While accomplishments need to be consolidated, an internal level playing field is being established for processing Bank-GEF operations. This helps to catalyze the inclusion of global environmental objectives more generally in Bank operations.

3.46 Second, the Bank's broader portfolio in lending for energy and rural development (including forestry and agriculture) is, in a modest, but gradual way, beginning to reflect the inclusion of "win-win" opportunities, that is, opportunities that our client countries have for promoting their traditional national and sectoral development objectives while at the same time addressing global environmental concerns. The

supportive operational policies are in place, and lending policies are being revised to appropriately address global environmental objectives. To make further progress, global environmental concerns linked to national sustainable development and client country obligations under the global conventions need to be properly anchored in the country assistance programming framework. And here there is a long way to go before the country economic and sector work that underpins such a country assistance framework is adequately addressing global issues when called for. Accelerating the development of the tools and methods for analyzing global environmental impacts holds the key to further progress.

3.47 Third, the Bank Group has demonstrated leadership in the development of new products designed to help countries access and operate on markets for global environmental goods and services. Also, the Bank Group has catalyzed a series of new and innovative partnerships between industry, NGOs, foundations and the donor community for the purpose of promoting through the market the adoption of sustainable use and effective protection of terrestrial and aquatic biodiversity. Ultimately, the value of these initiatives will be measured by how effectively our client countries are able to integrate global environmental concerns in their national sustainable development programs and how effectively the Bank Group's lending and non-lending services have contributed thereto.

4. CHALLENGES AND THE WAY FORWARD

CHALLENGES AHEAD

4.1 The reflection of global environmental objectives in the Bank Group's lending and non-lending services is the outcome of a country assistance dialogue between the client country and the Bank Group. Hence, a main challenge for the Bank Group is to strengthen its own capacity in such a dialogue to assist clients in (i) identifying the "win-win" opportunities in sectoral reform and investment programs for capturing global benefits, for funding under conventional development finance; and (ii) the beyond "win-win" options for securing additional global benefits, for funding through the GEF, the MFMP or other future global compensation and market-based mechanisms that may become accessible to client countries.

4.2 A second challenge is for the Bank Group to step up its efforts to help build the capacity in client institutions to pursue and analyze these opportunities. This challenge involves not only technical training of staff in client institutions, but also the strengthening of administrative and managerial functions in key agencies, as well as supporting networking of professionals within and between countries. The challenge is not to help promote centralized "global environmental management capacity" within environmental ministries. Rather, it is to help senior officials, planners and technicians, such as those in agricultural or forestry ministries/agencies, to recognize the importance of conservation or sustainable use of biodiversity and carbon sequestration to sustainable production, or to enable energy sector planners and engineers to see the opportunity to use climate-friendly technology as complementary to their goal of pollution management locally. In meeting this challenge, the Bank Group's operations teams will want to take full advantage of the renewed commitment of EDI to strengthen and expand training for clients and development partners in local and global environmental management.

4.3 The interest of client countries to pursue global environmental issues in their dialogue with the Bank Group is likely to continue to be dictated, at least in the near term, by access to GEF grant resources. As countries complete their national strategies and action plans in response to obligations under the conventions, and as guidance from these conventions expands, the demand for Bank-GEF assistance will increase. Hence, a third challenge for the Bank Group is to respond to this demand in a way that meets both GEF's objective to catalyze additional Bank Group co-funding for these projects, and integrates GEF support in the Bank's development assistance in the agricultural, forestry, energy sectors of its client countries. Hence, the importance of underpinning the country dialogue with sector work that captures essential links to global environmental objectives, such as the new series of country energy environment reviews. Furthermore, to meet this challenge the Bank needs to complete the mainstreaming of GEF into its overall business planning process.

4.4 It is less clear what priority client countries will assign to investments in "win-win" opportunities, i.e. those which benefit the global environment and the domestic economy simultaneously. These opportunities must be vetted against the many competing claims that developing countries face. There is, as discussed in the opening chapter, a real tension between the need for high rates of return on scarce development capital and the frequently lower rates of return on longer term investments that are required to usher in sustainable use of key natural capital assets such as soil, water, forests, coral reefs and biodiversity more generally.

4.5 Hence, even when so called "win-win" investments in, say, sustainable use or globally-friendly technologies and practices, meet the desired hurdle rate for return on capital, they may be discriminated against because of their relatively lower return. An important question, therefore, that the Bank Group could consider, is whether there are ways through financing or other instruments which can help neutralize

this discrimination, whenever investments in long-term sustainable developments are at stake. In this context, the Bank Group is taking note of OECF's recently launched initiative to offer its clients highly preferential lending terms, designed to buy down the transaction costs to countries of introducing climate friendly renewable energy technologies with consequent gains for the global environment.

TOWARDS A CORPORATE ENVIRONMENT STRATEGY

4.6 Given these challenges for further incorporating the global environmental agenda into the mainstream of Bank Group development assistance, some five priority areas for further action emerge:

- **First**, *strengthen Global Environmental Sector Work, including the required analytical methods.* This would involve expanding and accelerating the efforts under the (i) ongoing Global Overlays Program (for climate change and biodiversity), (ii) National Strategy Studies Program (for climate change), (iii) Strategic Environmental Assessments initiative (currently AFR pilot), and launching (iv) the Energy Environment Review program (for climate change) and consider extending the application of this methodology to other relevant sectors; all to identify and help disseminate analytical tools and good practice with the view to integrating global environmental concerns in the Bank's sector and project work. These programs have to be effectively oriented towards the needs and priorities of the operational units within the Bank and be backed by adequate funding.
- **Second**, *strengthen and accelerate in-house (management and staff) and client training on global environmental issues.* Such training would emphasize the understanding of the links between global environmental objectives and sustainable development, and the opportunities for addressing them in Bank Group development assistance as well as national sustainable development planning. It would involve (i) EDI-LLC in including global environmental issues and links to sustainable development in relevant management and sector staff (agriculturists, foresters, energy specialists) training, and integrating global concerns in national sustainable development in client training and policy seminars, (iii) Bank-GEF in strengthening its program of workshops in-house and in-country, and (iv) Bank regular lending in addressing capacity building for global environmental management as part of overall support for institutional strengthening for environmental management in client countries.
- **Third**, *consolidate the development of new products and partnerships and integrate them as appropriate in the country assistance program* The market transformation initiatives in forest or marine resource management, or market-based mechanisms for mitigating climate change under the Kyoto Protocol, are all designed to mobilize private capital, additional public funding, and the skills and influence of multi-stakeholder coalitions to mitigate global environmental degradation. Although young, these initiatives are already starting to demonstrate this potential and need to be consolidated. Plans are also in-hand to expand them to address other critically endangered ecosystems (e.g. through the Critical Ecosystems Partnerships Fund)) and the management of biologically important natural resources, such as offshore fisheries. The challenge the Bank Group faces, sector by sector, with these new products and partnerships, is to ensure their effective integration and support for other ongoing international efforts, such as the International Forum on Forests, and within the Bank's own country assistance and sector strategy.
- **Fourth**, *complete mainstreaming GEF in Bank operations* by (i) fully integrating GEF in the Bank's business planning process, starting with the inclusion in Senior Management's forum for

setting institutional priorities; (ii) removing disincentives for undertaking GEF projects by making uniform costing fully applicable; and (iii) monitoring the effectiveness of the streamlining measures put in place.

- *Fifth, further strengthen incentives for management and staff to address global environmental objectives in lending and non-lending services*, to ensure a level playing field between relatively small and frequently complex and risky global environment focused projects, and the more traditional large volume projects. In addition, it may prove rewarding to revisit the interpretation of sustainable development through the Bank Group's assistance, the modalities for achieving this core objective, and the role in such modalities of Bank Group support for the management of global public goods.

4.7 Actions on several of the above priorities are proceeding under ongoing programs. All of them will be considered in detail as part of the development of an Environment Strategy for the Bank Group. Preparation of such a strategy is underway, and will define corporate objectives and targets, and set out monitorable performance incentives for Bank staff. The strategy will guide, enhance and set priorities for the Bank Group's efforts to effectively integrate environmental objectives in its development assistance, all with the intent of more effectively supporting the client countries' goals for sustainable development.

4.8 The corporate environment strategy will embrace the global dimension. To our member countries, acting on global environment priorities is of interest when it results in enhancing national sustainable development and/or generates local or regional environmental benefits. Hence, if we are to be successful in integrating the global environment in our lending and non-lending services, we need to understand and build on the synergies and complementarities between local, regional and global environmental benefits. We need to recognize the links among various environmental issues and identify technologies, policies and practices that have multiple benefits, as well as interventions that address multiple environmental problems (local to global). All this calls for a discussion and integration of the Bank Group's strategy on global environment issues with the development of a broader corporate strategy for the environment.

4.9 Finally, it needs emphasizing that the global environmental agenda cannot be expected to be of equal importance in all country assistance strategy frameworks. It would be expected to receive the greatest attention in cases where global environmental resources, such as biodiversity, form an essential part of the national capital stock, or where there exist significant opportunities for reducing greenhouse gas emissions or sequestering carbon. In this context, the implementation of the Environment Strategy for the Energy Sector and the development and implementation of the Bank Group's Environment Strategy are expected to help define priorities for the Bank's further efforts.

BANK GROUP LENDING FOR THE GLOBAL ENVIRONMENT

An Overview

Targeted and Non-Targeted Lending

1. Bank Group lending addresses the global environment objectives through various channels. First, targeted environment projects or project components address global environmental concerns directly or indirectly.
 - Bank Group managed projects funded by GEF and MFMP or GEF aim at reducing greenhouse gas emissions, promoting conservation, and sustainable use of biodiversity, protection of international water bodies and the phasing out of ozone depleting substances. GEF funded project activities are increasingly integrated into Bank Group projects, e.g. a protected area management within a Bank Group supported forestry development project; a renewable energy component within a Bank power sector development project, or a biodiversity conservation component within an IFC supported private sector investment project for agricultural or forestry production. Funding is typically a combination of GEF and Bank Group/other donor funding, with the latter funding the “baseline” and the GEF the “incremental costs” for capturing global environmental benefits.
 - IDA/IBRD funds projects which provide institutional or technical support for general environmental management and which frequently help countries plan and take action on local problems impacting global environment concerns.
2. Secondly, Bank Group lending for agriculture, forestry, energy and other sectors support the global environment indirectly, that is without explicitly targeting it. Lending in support of energy pricing reform creates incentives for adoption of lower greenhouse gas (GHG) emission technologies. Support for agricultural intensification can importantly reduce pressures on natural habitats and biodiversity. Also, funding for community based natural resource management frequently lead to more sustainable use of forest and biodiversity resources. These are the “win-win” opportunities where pursuit of economically efficient and socially feasible solutions to sector development are expected to simultaneously produce gains for the global environment.
3. In this “win-win” context, and in the private sector area, IFC’s own resources and commercial sources of equity and debt are funding projects that generate local, as well as global, environmental benefits. This often results from the forces of the market place, which lead private sponsors to adopt efficient technologies and processes that minimize environmental impacts. Where there are “incremental” costs to achieving global environmental objectives, IFC uses GEF and other concessional resources to support ventures that either appear to IFC to be commercially viable but are too risky for private sector investors/lenders; or are close to, but not quite at, commercial viability.
4. Funding of the Bank Group’s targeted lending for the global environment comes from GEF, MFMP, IBRD/IDA, IFC and trust funds. Bank managed GEF and MFMP funds have now built up a healthy Bank

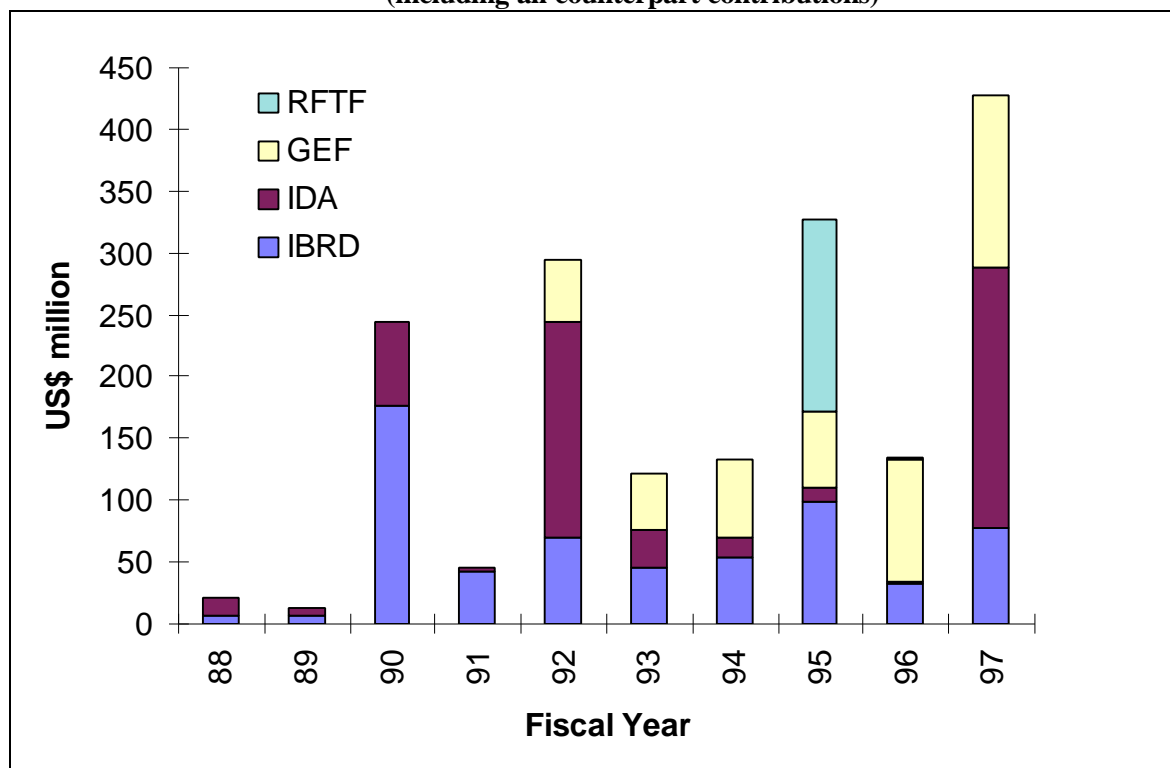
Group portfolio of targeted global environmental projects of over \$1.2 billion (GEF funding \$919.2 million and MFMP \$0.3 million). These resources have helped greatly to mobilize cofinancing from multilateral agencies (including the Bank Group), bilateral donors, the private sector, foundations and recipient governments. For Bank-GEF funded projects, an average of four dollars of co-funding was associated with one GEF dollar, demonstrating effectiveness of the Bank Group in using GEF resources to leverage funding for the global environment.

5. Leveraging is a primary feature of IFC's contribution to the Bank Group's GEF program. Consistent with its corporate objectives, IFC explicitly seeks to maximize the leverage of GEF funding as a catalyst for other sources of capital. Hence, it expects to achieve a leverage ratio of 5 to 11 times (non-GEF funding to GEF funding) for its approved GEF projects, which is well above GEF's corporate target and the average public sector projects. IFC has also pioneered the use GEF resources in the form of non-grant financing mechanisms such as low-interest loans or contingent repayment equity. These types of instruments provide targeted, incremental assistance needed to offset specific risks and could increase the expected leverage use of GEF funding beyond the levels noted above.

Biodiversity

6. The Bank Group's lending and associated cofunding for biodiversity conservation (including biodiversity components of environment or sectoral investment projects) totals US\$1.8 billion over the last ten years, involving resources from IBRD, IDA, GEF, and the Brazil Rainforest Trust Fund (RFTF). The bulk of the funds (own and others) administered and implemented by the Bank have supported the establishment of new protected areas or management of existing national parks. More recently, Bank funds, often catalyzed by GEF resources, have begun flowing toward conservation or sustainable use of biodiversity in the broader agricultural or rural landscapes. While annual funding levels have varied considerably, the Bank's lending (and associated co-financing) for biodiversity has grown steadily, from US\$21 million in FY88 to a record US\$411 million in FY97 (see Figure 1).

**Figure 1: Annual Biodiversity Investments (US\$ million)
(including all counterpart contributions)**

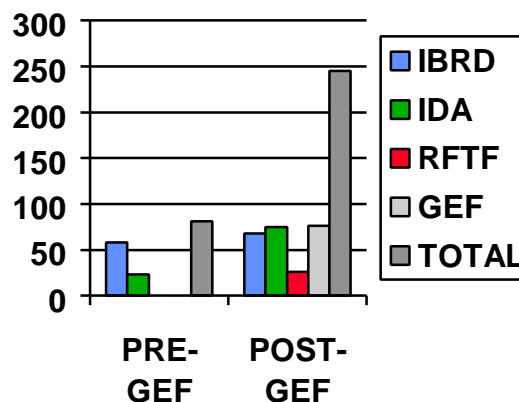


7. The emergence over the last six years of the GEF as a source of Bank lending for biodiversity conservation has not reduced the commitments by IBRD and IDA resource for biodiversity conservation. (see Figure 2 and Table 1). Overall, the Bank's commitments to biodiversity conservation, even without the GEF, have increased several fold, particularly since the 1992 Rio Conference. This is consistent with the GEF philosophy that limited GEF resources do not "crowd out" existing development lending.

**Table 2
Yearly Averages, Pre- / Post-GEF (US\$m)**

	PRE-GEF (1988-1991)	POST-GEF (1992-1997)
IBRD	57.8	62.9
IDA	23.4	76.9
RFTF	0	26.3
GEF	0	73.2
TOTAL	81.1	239.2

**Figure 2
Yearly Averages, Pre- / Post-GEF (US\$m)**

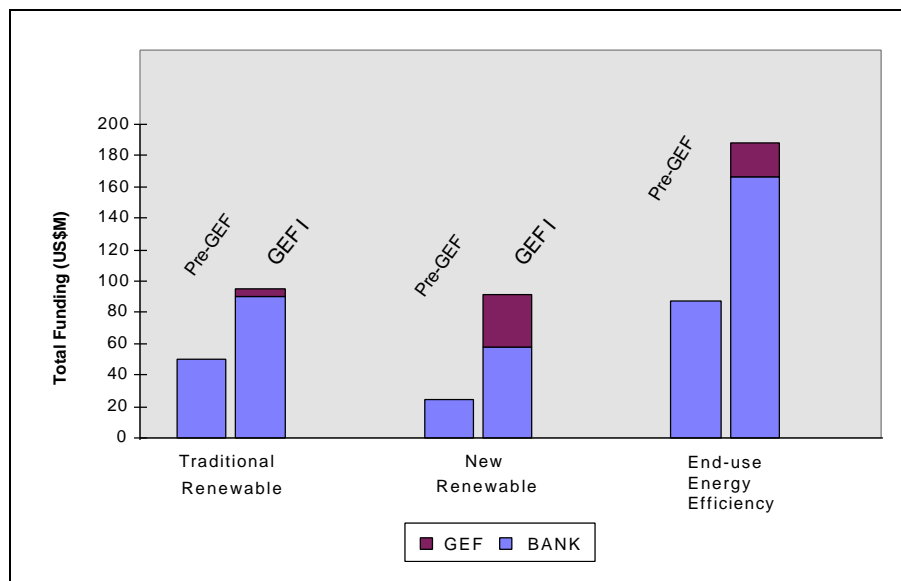


8. Finally, it needs to be noted that the part of the Bank Group lending for forestry that indirectly benefits biodiversity conservation through improved forest management and development (i.e. non-targeted lending) is not reflected in the above data.

Climate Change

9. Despite an overall decline in Bank lending for energy since the early 1990s, the Bank’s commitments for energy efficiency and renewable energy during the same period have increased. Figure 3 shows the Bank’s portfolio in three sectors: traditional renewable energy (principally geothermal), new renewable energy (e.g., wind, solar, biomass), and end-use energy efficiency. In each case, Bank lending commitments in these areas have increased concomitantly with GEF financing. Thus, annual average Bank/GEF financing for end-use energy efficiency has grown from roughly \$85 million in the pre-GEF period (FY81-91) to \$190 million in the FY92-9 period; and for renewables (geothermal and hydropower excluded) from \$30 million to more than \$90 million within the same timeframe

Figure 3. Annual Bank/GEF Commitments for Renewable Energy and Energy Efficiency



10. These financing trends provide strong evidence that GEF funds for the global environment have not displaced or substituted for World Bank financing. However, it should be noted that the new renewables and energy efficiency projects are still very few in number, and on average, have accounted for 10-12% of the overall Bank energy lending since the early 1990s. In addition, the majority of such projects have been undertaken in the South and East Asia regions. This is owing largely to the existence of a programmatic approach facilitated by the Asia Alternative Energy Unit, which is funded by bilateral donors to help identify environmentally friendly energy projects.

Desertification and Land Degradation

11. Financial assistance from the Bank Group can help country partners reduce losses of global environment benefits in the areas of biodiversity, climate change, and environmental services of international water bodies, which occur as a result of land degradation and desertification. Over the

period 1990-95, the Bank supported 34 land degradation control projects totaling US\$1.3 billion, and another \$5.3 million (over 70 projects) for natural resource management more broadly.

12. New and proposed lending activities for the period 1995 to-date indicate that the Bank expects to commit over \$2.2 billion for an additional 57 projects over the period 1996-99, 27 of which would primarily address land degradation and the underlying causes of desertification identified in the UNCCD, while another 30 have broad natural resource management components. As expected, a major share of these projects (39%) are in Sub-Saharan Africa, followed by Latin America and the Caribbean (25%), the Middle East (14%), and South Asia (4%). The remaining 12% are in Central Asia and other parts of Africa. GEF funding can help ensure that, wherever feasible, the design and implementation of these projects help conserve biodiversity, secure carbon sinks/reduce carbon emissions.

World Bank User
N:\envgc\MAINSTREAMING\Final Mainstreaming\Final9_30.doc
09/30/98 12:22 PM