

# What are future financing options for shock responsive social protection? A technical primer

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# Executive summary

**Awareness of the need for more Shock Responsive Social Protection (SRSP) systems has grown rapidly over the past few years**, as part of a broader effort by humanitarian and development partners to both reduce risk and more effectively address new risks as they arise. However, the diverse aspects and potential of financing for SRSP remain underexplored, and shock responsive elements in social protection systems and programmes are rarely institutionalised or adequately funded.

**Financing for SRSP has been given added impetus by the COVID-19 crisis**, as countries use and adapt social protection systems and programmes in an attempt to reach existing and newly affected people in a timely and appropriate manner. The pandemic has at once underlined the importance of routine and shock responsive approaches to social protection in helping address covariate shocks and has created the prospect of a global economic downturn that could threaten investment in these same systems and programmes in the near future.

**The relationship between financing, policy, and programming is symbiotic** – programming follows the boundaries and prerequisites set by financing sources and instruments, and financing is limited or enabled by the context, planning, capacity, and flexibility of the systems and programmes in-country. Understanding this interplay is crucial to improving how SRSP is designed and delivered, and to increasing the range of financial sources and instruments available.

**This paper aims to advance these discussions in a number of ways. As ‘financing for SRSP’ is understood differently by different people, it starts by providing greater clarity on what this term constitutes, and its relation to disaster risk finance.** It acknowledges the broad potential remit of financing for SRSP (including the financing of routine social protection, longer-term risk reduction, and resilience-building efforts), and the need for a balance of investments to reduce and transfer risks - reducing the size of the risks to be transferred also reduces the cost of transferring the risk. However, the paper focuses on those aspects of financing linked to shock preparedness, response, and recovery.

**It then outlines the key principles that shape both approaches to financing for SRSP and disaster risk finance, and suggests a ‘money-out / money-in’ framework to guide practitioners, reflecting the relationship between financing, policy, and programming mentioned above.** We note that adopting such a framework requires ensuring that different types of ‘routine’ and ‘shock responsive’ programmes are adjusted and connected to better address the multi-dimensional risks posed by covariate shocks more coherently. Further, increasing investments in flexible systems that support a diversity of partners and programmes represents a ‘win-win’ for policymakers, improving effectiveness and efficiency of delivery, and ‘future proofing’ systems against the shocks to come. Lastly, and relatedly, financing routine social protection is fundamental to advancing SRSP and presents a core challenge in itself. While not the focus of this paper, we reference this issue and related resources throughout.

**The paper then provides a high-level overview of two different ‘money-in’ aspects.** The first is current and potential **financing sources** and actors for SRSP (we look specifically at the social protection, humanitarian, and climate sectors), discussing some of their applicability and limitations. Broadly, financing SRSP (as the name suggests) has tended to focus on the social protection sector, but other sectors can and are financing SRSP efforts, and offer avenues to expand financing in the future. The second is a review of a range of possible **risk financing instruments** that can be used to support SRSP. The introduction of a wider range of innovative instruments in recent years is a potential game-changer, yet many barriers still exist in realising their potential. We weigh up some of their pros and cons and reflect on how they can be better institutionalised. Likewise, political economy factors, and the perennial challenge of coordination across diverse partners, loom large in this discussion, and must be more seriously considered as part of a holistic approach to financing.

**The paper ends with a series of reflections and recommendations for a broad policy and programme audience, designed to inform decisions** on financing for SRSP for the COVID-19 response and beyond. Along the way, we signpost the reader to useful resources through footnotes, a recommended reading list, bibliography, and a glossary.

**Recommendations start with the broader context in which financing for SRSP is set.** Funding disasters is political. Shifting the focus from ex-post to ex-ante approaches moves the loci of power and the onus of responsibility from international to national stakeholders in ways that sometimes challenge (though also enhance) traditional decision-making processes and relationships. The importance of these shifts should not be under-estimated, as it also cuts to the core of the coordination question, which is the making or breaking of good SRSP. New forms of financing SRSP and risk management could help leverage reform in key areas relevant to SRSP, but actors must be willing to get round the table and speak with one voice. We flag that multilateral climate finance holds the potential to support SRSP but it is currently unclear what it can finance and how. Likewise, the full range of SRSP efforts financed by humanitarian actors need to be brought more squarely into the picture. Social protection, whilst crucial, is not the only way to deliver SRSP, and in some cases are not the most appropriate. This includes contexts of conflict, where more research is needed on how financing for SRSP can be applied.

**Recommendations also focus on the technical specifics.** We note that while risk financing instruments have evolved in exciting ways in the last few years, there are still notable deficits to address in terms of technical expertise (especially outside international financial institutions) and affordability (such as for insurance premiums), and that there is a need to consolidate and present risk finance instruments in a way that is more accessible and understandable for stakeholders beyond the financial sector. Diagnostic tools developed by risk finance practitioners should be more widely applied, and data-driven innovation (including improving data quality and analysis for designing risk financing instruments) require greater investment, which in turn would improve broader programming. The capacity to deliver SRSP at national but especially sub-national and local levels needs boosting so as not to further overburden those actors charged with responding to shocks, supported by risk-aware and data-driven information and delivery systems. Without these measures, financing instruments can become more advanced, but the means to deliver benefits to those most in need, in a timely and cost-efficient manner, will remain overwhelmed or inflexible.

**As we move forward into a post-COVID-19 world, the case for financing approaches to SRSP remains strong, yet the availability of both resources and political will may be at a premium.** Enhancing investment requires enlarging the business case for SRSP in ways that demonstrate the potential scale and diversity of sources and instruments, and the fundamental relationship between improved financing, systems building, and programming. We hope that this paper contributes to making that case.

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# List of abbreviations

ARC	African Risk Capacity
CAT-DDOs	Catastrophe Draw-Down Options
CBPFs	Country-Based Pooled Funds
CDP	Centre for Disaster Protection
CERF	Central Emergency Response Fund
DAC	Development Assistance Committee
DRF	Disaster Risk Financing
DRM	Disaster Risk Management
FAO	Food and Agriculture Organization
FCDO	UK Foreign, Commonwealth and Development Office
FTS	Financial Tracking Service
GCF	Green Climate Fund
GDP	Gross domestic product
GHD	Good Humanitarian Donorship
IBRD	International Bank for Reconstruction and Development
IDA	International Development Association
IFI	International Financing Institution
IFRC	International Federation of Red Cross and Crescent Societies
ILO	International Labour Organization
IMF	International Monetary Fund
MDB	Multi-lateral Development Bank
NGO	Non-governmental organisation
OCHA	Office for the Coordination of Humanitarian Affairs
ODA	Official Development Assistance
OECD	Organisation for Economic Co-operation and Development
OPM	Oxford Policy Management
PFM	Public Financial Management
SDGs	Sustainable Development Goals
SRSP	Shock Responsive Social Protection
UNDRR	UN Office for Disaster Risk Reduction
UNEP	UN Environment Programme
UNFCCC	UN Framework Convention on Climate Change
UNHCR	UN High Commissioner for Refugees
UNICEF	UN International Children's Emergency Fund
USAID	US Agency for International Development
WFP	World Food Programme

# 1. Introduction

**The human, social, and economic impacts of COVID-19 have been severe. Beyond mortality and morbidity risk, COVID-19 has impacted national economies, hitting the global poor and vulnerable hardest.** The pandemic has demonstrated again how crucial it is for national and international actors to not only provide support to those most affected in a timely and appropriate manner, but also to be able to cushion the longer-term impacts of covariate shocks and better prepare for and anticipate these in the future.

**Utilising and scaling-up social protection systems and programmes has been one key strategy implemented by governments and international partners around the world to address the effects of COVID-19.** This has been done in various forms, for instance by providing additional support to routine beneficiaries, adding additional beneficiaries to routine recipient rosters, utilising existing social protection systems, such as databases, to inform different programmatic responses, or in some cases creating entirely new programmes (Gentilini *et al.*, 2020). In some cases, this has also been done in concert with the disaster risk management (DRM) or humanitarian sectors. These efforts can broadly be referred to as Shock Responsive Social Protection (SRSP) (see [Annex II](#) for a Covid-19 financing case study).

**SRSP is part of a broader effort by humanitarian and development partners to establish new ways of working that both reduce risk and more effectively address new risks as they arise, facilitated by improved financing modalities.** In humanitarian contexts, where most crises are protracted in nature, this move towards multi-partner, multi-year approaches to risk management and resilience building, through the use of a more diverse and flexible range of financial instruments, is seen as crucial to protecting the most vulnerable, reducing fragility and building national capacity, and supporting collective outcomes (UN Office for the Coordination of Humanitarian Affairs [OCHA], 2017; Bowen *et al.*, 2020).

**However, shock responsive elements in social protection systems are rarely institutionalised or adequately funded.** The way in which programmes are financed fundamentally shapes how they are implemented and their ability to manage risk and address need in an efficient, effective, economic, and equitable manner. While the global literature on SRSP has surged in the last five years, the question as to how the different dimensions of SRSP should be appropriately and sustainability financed has received less attention (though this is growing – see, for instance, Calcutt *et al.*, 2021).

**Furthermore, both the social protection and humanitarian sectors were underfunded prior to COVID-19, and the pandemic has triggered a global economic slowdown from which a rapid rebound and economic recovery seem unlikely.** This has exacerbated pre-existing vulnerabilities ('COVID-19-intensified') and created new vulnerabilities ('COVID-19-specific') (Devereux *et al.*, 2020; Archibald *et al.*, 2020), particularly around gender equity and social inclusion. The effects of the pandemic have therefore demonstrated the need to strengthen routine social protection systems and to continue to expand the coverage of these, as well as to enhance their capacity to respond to both idiosyncratic and covariate shocks. This process includes establishing systems and plans, and putting financing in place in advance of shocks, at a very challenging time for decision makers, who are facing tough decisions on where to prioritise investment.

**This paper is designed to inform the discussion on financing SRSP.** It starts by clarifying what is meant by SRSP financing and provides a framing to guide practitioners' approaches to SRSP financing, including the prerequisites, such as coordination and delivery architecture, required to improve financing options. It then provides a high-level overview of current and potential sectoral financing sources for SRSP, as well as specific financing instruments, their applicability and limitations for SRSP, and how they can be better institutionalised. It ends with a series of reflections for a broad policy and programme audience, designed to inform decisions on prioritising financing for SRSP for the COVID-19 response, recovery, and beyond. Along the way, it signposts the reader to useful resources through footnotes, a recommended reading list, bibliography, and a glossary.

**Answering these questions requires first taking a look at definitions to establish the scope of this paper, but ultimately, we argue that principles matter more than definitions.** Definitions for 'shock responsive and adaptive social protection', as well as interrelated terms such as 'disaster risk finance', tend to have ambiguities and overlaps. The community of practice has started to create distinctions between definitions, but they are not commonly shared. This is important for financing purposes, as



definitions are closely tied to how funding is allocated and tracked, and to the purposes for which money can be used. We review definitions and reinforce some key messages for conceptual clarity. This includes, most importantly, that financing for SRSP (such as adaptive social protection) is broad and can cover the whole spectrum of interventions across the risk cycle (from prevention to preparedness, response, recovery, and mitigation). Disaster risk financing (DRF) constitutes one approach among others that can be utilised in SRSP, from a range of sectoral sources and donors, through a range of financing options. In terms of scope, this paper acknowledges the broad remit of financing SRSP (including longer-term risk reduction, resilience-building efforts, and the financing of routine social protection), but focuses on those aspects of financing linked to shock preparedness, response, and recovery. Both financing for SRSP and DRF share similar principles, and it is these principles that we forefront as the main way to improve how SRSP is designed, delivered, and funded.

**Lastly, following principles means reinforcing a key message: improving financing for SRSP is more than a discussion about financial instruments – it requires first an understanding of context, then downstream factors and processes.** Programming follows financing and cannot become more flexible or coherent if the financing is not. At the same time, understanding context, then getting the ‘downstream’ right in SRSP, i.e. planning, coordination, targeting, disbursements, fund management, monitoring, and evaluation, etc. (what we term the ‘money-out’ dimension), is as important, if not more important, for financing SRSP than the financial instruments themselves (what we term the ‘money-in’ dimension). While the scope of options for financing SRSP is broad and context specific, and therefore cannot be addressed fully here, the paper presents some of the options for financing SRSP, flags issues around financing, and poses some important questions for further consideration.

## 2. Key concepts and definitions

**One issue with concepts such as SRSP that involves different sectors is that definitions can at once appear familiar but contain distinct differences.** Different communities of practice either believe they all hold the same understanding of a concept (when perhaps they do not) or can be adamant that their understandings are very different (when perhaps they are not). There are no universally understood definitions for the main concepts used in this paper, so our working definitions are provided below. See the Glossary in Annex I for further detail and additional definitions.

**Shock Responsive Social Protection (SRSP):** SRSP looks at the linkages between the social protection and DRM sectors (including humanitarian assistance). It ‘focuses on shocks that affect a large proportion of the population simultaneously (covariate shocks). It encompasses the adaptation of routine social protection programmes and systems to cope with changes in context and demand following large-scale shocks. This can be ex-ante by building shock responsive systems, plans and partnerships in advance of a shock to better prepare for emergency response; or ex-post, to support households once the shock has occurred. In this way, social protection can complement and support other emergency response interventions’ (O’Brien *et al.*, 2018, p. 7).

In other words, SRSP aims to strengthen social protection systems as well as its linkages with DRM and other relevant sectors, to jointly improve the coverage, comprehensiveness, and adequacy of the support provided to the most vulnerable before, during, and after a shock occurs – and to pre-empt the needs imposed by potential future shocks (TRANSFORM, 2020). In this paper, the different attempts around the ‘linkage agenda’ that look to link humanitarian assistance and social protection (especially in fragile and conflict-affected situations) are taken as being part of the definition of SRSP, including in contexts ranging from a non-existent through to highly advanced social protection systems, and the different ways that humanitarian actors deliberately design their activities to ‘lay the ground for’ and/or improve the delivery and coordination of current or future social protection systems.

➔ In terms of scope, as noted in the definition of SRSP financing below, this paper acknowledges this broad scope of SRSP, but focuses on those aspects of SRSP and SRSP financing linked to shock preparedness, response, and recovery.

**Risk:** The convergence of the social protection, DRM, and humanitarian worlds under SRSP has thrown a spotlight on the use of different understandings of key interrelated terms of ‘risk’, ‘vulnerability’, and ‘shocks’. For the purposes of this paper, risk is understood as the likelihood of something occurring

through the interaction between hazards, exposure to hazards, and underlying vulnerabilities and coping capacities (UN Office for Disaster Risk Reduction [UNDRR], 2017).

**Shocks:** A 'shock' is used here to denote the wide array of events (e.g. natural, economic, epidemiological, conflict-based, etc.) that households, governments, and humanitarian and social protection systems aim to address (TRANSFORM, 2020). In this context we can take a shock to mean the realisation of risk that can lead to losses or negative outcomes. They can affect the individual or household (idiosyncratic) or a large number of people simultaneously (covariate). The focus of SRSP is on addressing covariate shocks.

**DRF:** The Centre for Disaster Protection (CDP) defines DRF as an approach covering 'the system of budgetary and financial mechanisms to credibly pay for a specific risk, arranged before a potential shock. This can include paying to prevent and reduce disaster risk, as well as preparing for and responding to disasters' (CDP, 2020). While this definition of DRF is broad, in practice DRF can tend to focus more narrowly on a specific range of processes and financial instruments to anticipate, respond to, and recover from (often climate- and weather-related) shocks (see Dercon and Clarke, 2016; Maher *et al.*, 2018, World Bank, 2020).

**Financing for SRSP:** There is no common definition of what financing for SRSP actually constitutes. In reality, it is a combination of financing sources and instruments from different sectors that addresses different aspects and layers of risk. Financing SRSP is about integrating the DRF approach into a wider system and approach to financing that also focuses on longer-term efforts to reduce residual risk and anticipate future shocks. Financing for SRSP (such as adaptive social protection) is broad and can cover the whole spectrum of interventions across the risk cycle (from prevention to preparedness, response, recovery, and mitigation). This can also include investing in longer-term, risk-aware social protection and resilience programmes, or connecting to other forms of financing such as humanitarian assistance and climate finance. What matters are the principles that guide these adjustments, integrations, and connections, and whether they are intentional and operational, or only theoretical or coincidental in nature.

➔ In terms of scope, this paper acknowledges the broad remit of financing SRSP (including longer-term risk reduction, resilience-building efforts, and the financing of routine social protection), but focuses on those aspects of financing linked to shock preparedness, response, and recovery.

**In summary, this paper underlines that both the definitions of SRSP and adaptive social protection are in effect similar and both are applied in a context-specific manner.** SRSP can cover multiple dimensions of the risk cycle, and is the term used throughout this paper. DRF is one necessary component of SRSP financing, but not the only one. Systems and programmes are only 'shock responsive' or 'adaptive' if their component parts are integrated or connected in a conscious and collaborative way, and only if they are designed and delivered to address multi-dimensional risks and needs coherently. This slight tangent into terminology is important because behind terminology lies politics, and terminology is never more necessary than for financing, where a lot hinges on definitions.

### 3. A conceptual framework for financing shock responsive social protection: money-out / money-in

**Disaster risk finance is about planning comprehensively for the occurrence of a shock, looking both at the required response and how this response will be financed.** It involves ensuring that plans, capacity, coordination, delivery mechanisms, and financing arrangements to pay for implementation are in place before a shock occurs. SRSP is about integrating that approach into a wider system that also focuses on longer-term efforts to reduce residual risk and anticipate future shocks. This can include investing in longer-term, risk-aware social protection and resilience programmes, and aligning a broad constellation of actors to provide a 'web of support' for vulnerable people in times of shock that is more coherent, comprehensive, and adequate.



## 3.1 Principles for effective shock responsive social protection and disaster risk finance

Financing SRSP and DRF aim to follow the same principles, ones that permit a flexibility in approach, and alignment across stakeholders. This means that principles for effective SRSP and DRF should be (adapted from Hobson, 2020):

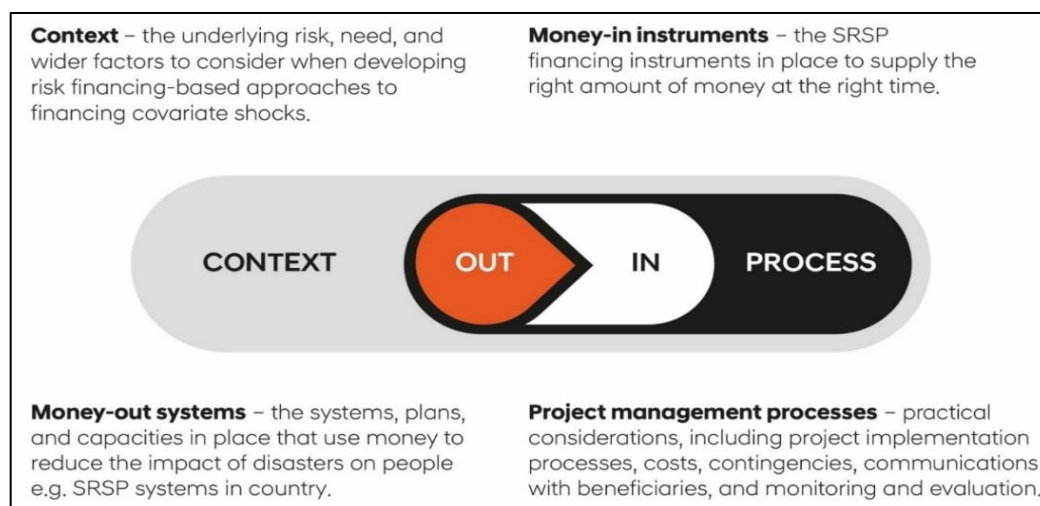
- **Timely:** The release of financing and delivery of response are both swift and timely.
- **Appropriate:** The right financing and interventions are sequenced according to need over time.
- **Available:** Rules to release resources and deliver support are pre-agreed and understood before a shock or disaster, and the process for accessing resources is straightforward and administratively light.
- **Deliverable:** The capacity, infrastructure, and enabling conditions are in place to deliver support from financing instruments; in this sense, the ability to deliver is as important as the financial arrangements themselves.
- **Informed:** Objective and commonly agreed/understood data and information is used to decide on the right types of financing and programming to address the risks posed by different shocks.
- **Predictable:** All stakeholders have confidence that the finance will be available on time and that the agreed actions will be adequately financed and implemented.
- **Coordinated:** Different forms of financing are aligned, integrated, and coordinated in an intentional and coherent manner.
- **Equitable:** Ensure that financing and delivery put people first and reach those most in need, including ensuring gender equity and social inclusion in any response.

As per the CDP, financing for SRSP (as for DRF) can be thought of terms of in four elements, set out in Figure 1. Each element and its relevance to financing for SRSP is outlined below.

While the sequencing of elements may seem counter-intuitive (most notably, why would you look at 'money-out' factors before 'money-in'?), this framework is intentionally designed to flip this sequence around, and draw attention to the fact that to get financing for SRSP right, you need to:

- Understand and design approaches that are grounded in context.
- Ensure that funds from risk finance instruments are linked to systems and programmes that can get the 'money-out' to the right people.
- Design 'money-in' from pre-arranged financial instruments so that plans are backed by the right amount of funds that come at the right time.
- Ensure that approaches are supported by effective project management processes.

Figure 1: Dimensions of financing a SRSP or DRF approach



Source: Adapted from Centre for Disaster Protection, 2020b

## 3.2 Understanding the context and prioritising risk

**Understanding the context is of great importance to designing a SRSP approach.** Assessing context means first understanding which risks the approach should respond to and what the need for such an approach is. The context is a key aspect in determining the success of the initiative: Is the targeted risk really a priority risk for the country/region in question? Could there be any political matters that might stand in the way of actually implementing the plan as it exists? How well are different policy levels connected as part of one and the same DRF strategy?

**Prioritising risk requires considering (1) whom the SRSP system should protect and (2) what they should be protected against** (World Bank, 2014). There are no definitive answers to these questions and they will depend on a variety of factors, including the expected impact of certain risks on certain population groups, particularly women and girls, the elderly, the disabled, and LGBTQI+ groups, the total financial cost associated with them, and overarching political objectives, noting also that not all decisions around addressing risk come down to a question of cost efficiency.<sup>1</sup> These factors should be considered carefully in a structured process, so that policymakers are enabled to select the risks they would like to manage intentionally and strategically (Lung, 2020b). This can include developing a baseline for prioritisation, such as preparing a quantitative disaster risk assessment using probabilistic statistical techniques to analyse the likelihood of specific disasters occurring, the size of associated expected losses and costs, and the impact of disasters on vulnerable populations.<sup>2</sup>

**Different financing instruments can also support efforts in other policy areas, such as combating climate change or supporting agricultural development.** A successful prioritisation process of political objectives requires the involvement of a broad range of stakeholders from national to local level, inclusive of development and humanitarian actors, since the resulting financing framework should serve as a voice for others not represented in the discussions (Start Network, 2019).

**Likewise, it is important to understand the capacity, coverage, and flexibility of the social protection system already in place,** its current or future capability to scale for covariate shocks, and its connections with other systems and programmes to do this. Being 'risk-informed' as part of an SRSP approach means that routine programmes may have to be adjusted to reflect and address the risks posed by shocks, and also their integration of, or connection to, preparedness, response, and recovery mechanisms and actors enhanced. SRSP is about both addressing and reducing residual risk, as well as improving the effectiveness and efficiency of shock response. Rarely is such a holistic picture to be found at country level, and more rarely still can it be found connected to different risk financing instruments for different types of shock.

**Lastly, understanding context means any new SRSP initiative or financing mechanism must integrate well with other existing humanitarian and disaster response initiatives, policies, and programmes, ideally coordinated by one central strategy.**<sup>3</sup> At policy level, this requires updating policies to ensure they address shock responsive approaches (and refer to each other as needed). This is especially important given that certain SRSP mechanisms (such as insurance) can take time to demonstrate their full potential (e.g. they trigger only for severe shocks, which can take years to manifest and for the SRSP mechanism to be triggered). Meanwhile, factors such as recency bias (our cognitive tendency to give greater importance to recent events), fiscal pressures, and elections cycles mean governments may not always want to commit to longer-term solutions if no immediate returns are

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<sup>1</sup> This is the starting point for analysing 'value for money', which looks to understand and balance of four factors: economy, efficiency, effectiveness, and equity. Economy is achieved through the minimisation of the cost of inputs, while efficiency involves maximising the amount of output achieved for a given input. Effectiveness relates to the extent to which the intended outputs lead to desired outcomes. Equity allows us to examine the distribution of costs and benefits, and whether this is in line with a programme's stated objectives. Finally, overall cost effectiveness relates to the extent to which the whole causal chain, from inputs to outputs to outcomes, results in the desired impacts. Value for money indicators are then expressed simply as the cost to achieve the outputs, outcomes, and impacts as defined by a causal chain. What is clear is that value for money can never be assessed in a vacuum: it is always a relative concept, a tool to guide decisions about which option represents the best use of society's scarce resources (Wylde, 2015).

<sup>2</sup> Given the complexity of disaster risks, as well as frequent data gaps in many countries, technical specialists, including local experts, will be required to conduct such an assessment. Methodological approaches are proposed, for example by the UNDRR (2017) and the Global Facility for Disaster Reduction and Recovery (2014).

<sup>3</sup> See Lung (2020b) for a further elaboration of the different points to consider.

evident. Hence policymakers should consider including SRSPs in long-term financial and political planning (e.g. by setting up a dedicated budget line) to help lend the initiative the breathing space it may need to become fully effective. At programme level, understanding context means ensuring new and existing humanitarian and SRSP measures are aligned in a coherent manner, and do not duplicate each other unless by design (e.g. to provide complementary benefits to the same household). This is expanded upon in the next section.

### 3.3 Establishing the ‘money-out’ parameters

**After having considered which risks the SRSP mechanism is meant to address, policymakers will need to design a shock responsive delivery system and the actual mechanisms themselves** – in other words, the activities that will occur in response to a shock. Financing should find its way to the right target groups, through well-functioning, planned, and coordinated delivery systems and appropriate shock response mechanisms. We call this the **‘money-out’ system**. This is in fact the prerequisite for ‘money-in’ financial instruments to function, and why we discuss it first. The design of these activities is not the focus of this paper, since much has been written about this (e.g. Bowen *et al.*, 2020; O’Brien *et al.*, 2018; TRANSFORM, 2020). However, certain best practice considerations deserve mentioning.

**First, a shock responsive mechanism should be built into an existing social protection or other programme wherever possible** (for example, using a DRF instrument such as parametric insurance to channel funds to an existing social assistance programme, triggered to address a covariate shock) to reduce development and learning costs, enable a smooth transition between routine and shock responsive support, maximise economies of scale, and increase response times. Working through existing systems and investing in ex-ante approaches also brings clear cost-benefits (see Box 1 below).

➔ **This implies that the pre-existing system or programme has to function efficiently during normal times before being used for covariate shock response.** Planning ahead through a DRF strategy can highlight where the flaws are in the system and can create additional incentives to address them. Where these types of systems and programmes do not currently exist or are nascent, thought should be put into how to design interventions that can enable the development of such a system in the medium to long term.

#### Box 1: The cost–benefit argument for investment in SRSP

At a global level, the cost-benefits of investing in early-action, resilient, and shock-responsive social protection systems, as opposed to conventional and cyclical humanitarian responses, have become clear but are not yet being fully realised. For instance, global evidence from USAID’s Economics of Resilience study (Cabot Venton, 2018), modelling the economics of early response and resilience across 15 million people in Kenya, Ethiopia, and Somalia, showed that investment in early response and resilience could have saved US\$ 4.3 billion over the previous 15 years, or an average of US\$ 287 million per year, and that every dollar spent on safety net and resilience programming results in net benefits of between US\$ 2.30 and US\$ 3.30. A cost-benefit analysis of the African Risk Capacity (Clarke and Vargas Hill, 2013) estimated late response losses at US\$ 1,294 per household, and early response losses at US\$ 49 per household, an increased cost factor of over 2.5 to 1. The Cost Effectiveness of Early Warning study (Hallegate, 2012) looked at benefits derived from investment in early warning by extrapolating from systems in developed to developing countries, which estimated returns of between US\$ 4 and US\$ 36 for every US\$ 1 spent on investment in early warning (Hobson, 2020). Lastly, a joint study undertaken by the World Food Programme (WFP), the United Nations International Children’s Emergency Fund (UNICEF), and the UK Foreign, Commonwealth and Development Office (FCDO) calculated the financial ‘returns’ derived from specific preparedness interventions, including emergency supply prepositioning, infrastructure development, staff training, and contingency arrangements for external contracting in three pilot countries (Chad, Pakistan, and Madagascar). It found that increased investment in preparedness could reduce the costs of humanitarian response by more than 50% (UNICEF/WFP, 2015).

Such studies point to the potential of programme alignment, the sequencing of investments, and the mutual co-benefits of investing in flexible, risk-aware systems that can be utilised by multiple actors and programmes, increasing programmatic efficiency through reducing the overheads associated with parallel approaches and improving the timeliness of delivery. They can also enhance programme effectiveness and equity through better targeting, and through facilitating end-user experience by simplifying delivery. Such investments can potentially help overcome the dichotomous thinking of whether to fund ‘either’ routine social protection ‘or’ shock-responsive programmes.

**Secondly, ensuring inclusive participation – including of women, people with a disability, older people, and other vulnerable groups – in planning** helps identify inter-sectional needs and solutions for individuals and communities in times of crisis. However, this is often not done, or is considered only as an afterthought. The system needs to be well-designed to target the poorest and most vulnerable households, noting that opinions on who should be targeted and how can differ (O’Sullivan-Winks, 2020). Inclusive participation includes having functional and connected grievance referral mechanisms to enable beneficiary feedback from programme implementation and to adjust errors in an adaptive manner as they (inevitably) arise, improving design and implementation, and tailoring the approach for future shock responses. Local engagement also helps maximise the transparency, legitimacy, and local ownership of the approach (O’Sullivan-Winks, 2020), and can play a critical role in the sensitisation of local communities, ensuring that assistance reaches those most in need, and that risks are flagged and mitigated. More broadly, the more inclusive the routine social protection system, the stronger the base for the shock response to build on.

**Thirdly, vulnerability needs to be assessed in a multi-dimensional manner to ensure that SRSP systems respond to those risks that are most relevant to poor and vulnerable households** (many disaster risk finance instruments currently do not do this), noting that covariate shocks can differ in their impact across geographic regions and across different dimensions of vulnerability (e.g. poverty, food security, etc.), and that targeting different forms of vulnerability is complex. This also includes ensuring that SRSP systems deliver assistance in the most suitable way, considering programmatic parameters such as modality (e.g. cash or in-kind), transfer mechanism (e.g. cash-in-transit, mobile money, bank etc.), timing, and value (Hill, 2020).<sup>4</sup> There are evident trade-offs to be navigated (for instance, between numbers reached and amount provided, or simplicity of triggers versus inclusion/exclusion errors). As noted, potential end-users (such as local authorities and delivery partners) and beneficiaries should participate actively in the design process.

**Last of all, any SRSP initiative should consider ahead of time when it intends to activate and deliver shock responsive support; ideally this support should be built around triggers for rules-based disbursement.** A trigger could be anything from someone simply deciding that the activation should happen to a fully automated data-driven process. The more concretely that moment is defined before it actually happens, the fewer discussions need to be had on whether or not a mechanism should be activated (in short, minimising political influence). This type of response has the potential to be much faster. The benefits of a rules-based approach to triggering have been demonstrated extensively by the DRF literature (see e.g. World Bank, 2014). In the world of DRF and insurance, two broad categories of triggers are being used: ‘hard triggers’, which are based on objective data to define a specific criterion that launches the shock response; and ‘soft triggers’, which leave an element of discretion to individual people or processes to decide whether or not the response should be launched. Systems can use a combination of both (Lung, 2020a). See Annex III for a further elaboration of trigger design.

## 3.4 Developing appropriate ‘money-in’ mechanisms

**Making sure money-in mechanisms are in place in advance of a shock, so that the right amount of financing can be accessed in a timely manner when a disaster happens**, is the next crucial step. There are different options for pre-arranged financial instruments. Each instrument offers certain advantages but also comes with distinct challenges and prerequisites that need to be considered carefully. Pre-agreed plans and triggers are often crucial to avoid any delays in accessing money that can lead to larger damages and losses. Layering different instruments to address different levels of risk is complicated, with few examples to be found globally of integrating different DRF instruments into SRSP delivery mechanisms.

➔ The remainder of this paper (from Section 4 onwards) is focused on a summary of the principal financing sources and instruments for SRSP.

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<sup>4</sup> Often, there may also be an argument for targeting recipients of shock-related services before the shock occurs. For example, for the SRSP systems in Kenya and Uganda, the beneficiaries of planned scaled-up cash transfer programmes are pre-registered and pre-enrolled; this enhances response speed substantially and can also help financial planning considerations (Calcutt *et al.*, 2021).



## 3.5 Project management processes

**Project management should be effective to enable shock responsive programmes to function.** It should be clear what the tasks and related timings are to the different actors involved, and that they each have the required capacity to execute tasks. Planning ahead helps overcome the challenges arising from the current way of paying for disasters, which is generally reactive, resulting in slow, uncoordinated, and inadequate funding – though this is slowly beginning to change. The lack of planning can cause the response to be overly influenced by political motives, as opposed to evidence-based plans (Lung, 2020a). Conversely, a well-implemented, pre-planned shock response, and financing approach can make the response faster, more cost-effective, less politicised, and more dependable for any target beneficiaries.

### Box 2: The importance of well-functioning Public Financial Management systems

Public Financial Management (PFM) refers to the laws, institutions, systems, and processes by which public resources are planned and managed. This includes the management of revenue and expenditure: mobilising, allocating, executing, and monitoring it. PFM is often referred to as the ‘financial plumbing of the state’ – the pipes need to be maintained and improved to ensure sustainability of the delivery of public services. The three principles of good PFM are:

1. Aggregate fiscal discipline: spending in line with available resources to ensure economic stability.
2. Allocative efficiency: allocating scarce resources across areas to achieve development goals.
3. Operational efficiency: using funds effectively in-service delivery.

The relationship between PFM and DRF works both ways. Good DRF is important for PFM stability, while PFM systems support effective DRF. Disasters have the potential to severely disrupt public finances. They often result in increased expenditure pressures, along with a reduction in budgetary revenues, thus eroding fiscal discipline (the current COVID-19 pandemic is perhaps the clearest example of this). DRF mechanisms aim to mitigate these impacts through advanced planning and preparation.

Looking at the relationship in the other direction, it is important to recognise that PFM systems are essential in operationalising DRF instruments. While the mix of risk financing instruments should be part of a country’s DRF strategy, PFM systems and rules will impact the extent to which resources can be accessed, allocated, disbursed, and monitored. For example, PFM systems show whether there is adequate coverage and priority in the planning and budgeting process, whether resources are spent on their intended purpose in a timely manner, how and what revenues are collected, how debt is negotiated and managed, how resources are procured, etc. (CDP and OPM, 2020).

Looking to instruments, risk retention mechanisms are typically budgetary mechanisms (e.g. contingency budgets or disaster funds). Those held by governments are governed by a set of rules or regulations – typically set out in a country’s PFM law. Risk transfer mechanisms, too, typically rely on PFM systems to distribute funds, and therefore must abide by the PFM rules and regulations. Any additional cash spent by the government, including in the case of DRF instruments, will need to be introduced into the budget in order for governments to have the authority to spend such additional cash. In general, countries need to pass a supplementary budget (by which we mean an additional budget, which amends the original budget approved at the start of the fiscal year) in order to allocate those funds to a specific ministry, programme, or project to enable the execution of funds. Without the authority to spend, funds remain stuck with the national treasury.

Regardless of which instruments are utilised, if funds (regardless of the source) are to be disbursed through government systems, it is important to take into consideration the strengths and weaknesses of the domestic PFM systems. Some weaknesses may rule out certain mechanisms or necessitate PFM reform as a prerequisite. As such, before introducing DRF instruments, it will be important to assess the domestic PFM system to ascertain which instruments might function most effectively, and how and where they might do so. Furthermore, it is likely that any identified weaknesses during ‘normal’ times will be accentuated during a crisis. For example, if there are typically large leakages in spending, or substantial delays to releasing cash, these factors need to be taken into consideration when designing instruments and the procedures related to their implementation. For example, how funds are disbursed following an insurance pay-out is an important consideration and one which not always fully factored into the instrument design. Niger and Senegal both received insurance pay-outs from their risk transfer with the African Risk Capacity (ARC) in 2014/15 following a drought. However, there were significant delays in implementation as funds were retained by the national treasury, with an inability to transfer these funds to the responsible government departments in a timely manner. <sup>[1]</sup>

Source:<sup>[1]</sup> ARC, 2017. *Lessons Learned Summary Report: 2014/15 ARC Payouts: Senegal, Niger, Mauritania*, [link](#).

**Coordination is the key concept around which the success of SRSP hinges.** This means ensuring meaningful and accountability-based interconnection across practitioners and programmes. It includes defining as far as possible in advance of a shock, in terms of who is affected and to be targeted for different shocks, the roles and responsibilities, the potential size of caseloads, the modalities of implementation, the duration of programming, the alignment of programmes, the use of systems, and – of course – how it is all financed. Again, wherever possible, the aim is to utilise similar systems – for targeting or delivery, for example – to pool resources and exploit economies of scale. This requires understanding how shock response measures are complemented by longer-term risk reduction and resilience measures that both protect households and incentivise them to reduce risks themselves. Lastly, it includes understanding where social protection is not best suited to address a shock (Longhurst *et al.*, 2020).

**Essential questions about who ‘owns’ the risk also need to be thought of beforehand.** In the current funding model, it is often unclear who is responsible for financing needs during and after a crisis. This can cause unnecessary budget reallocations by the government that can be damaging for crucial sectors, or new borrowing that is harmful to the national economy. The aim is to have a more coordinated response, aligning the actions of governments – including those actions related to social protection – with international financial institutions, the humanitarian sector, etc., by ensuring that discussions on risk ownership have taken place before the shock occurs and needs are generated. A huge benefit of having a sufficiently specific and evidence-based DRF approach is that it could encourage greater development and use of SRSP and increase its ability to address covariate shocks more reliably, supporting finance that is more objective and predictable, and incentivising more effective disbursement, as well as enabling the routine system to continue functioning during crises (Scott and Omtzigt, 2021). This also enables the humanitarian sector to focus on responding to crises that are less predictable and/or exceed the capacity of routine programmes to address.

## 4. Money-in options for shock responsive social protection: actual and potential sources

**Different categories of finance could apply to SRSP, with funding potentially coming from social protection, humanitarian, climate finance, and other development sectors,** as well as from different actors (donor governments, national governments, private sector, etc.), making it hard to track. This section will look at both the sectoral sources of finance for SRSP and the actors that provide it (within each sector). For the sake of limiting scope, the focus will be mainly on international financing sources such as Official Development Assistance (ODA), while acknowledging there are also important flows coming from governments towards their own systems and programmes relevant to SRSP.<sup>5</sup>

**Levels of finance to shock responsive approaches themselves, regardless of source, remain small in overall terms.** We look at several of these sources below, focusing on who provides and receives funding within the social protection, humanitarian, and climate sectors, including total volumes of global flows, how financing in the sector has evolved towards SRSP, and why it is or could be relevant to SRSP in the future. We look at both support for ‘routine’ and ‘shock responsive’ social protection, or related forms of assistance, as both constitute important parts of SRSP, and funding that supports SRSP measures may not currently be disaggregated between its ‘routine’ and ‘shock responsive’ components (e.g. multi-annual support to cash transfers that could be allocated to routine or shock responsive top-ups depending on the year, the design of a social registry that supports routine or shock responsive programming, etc.).

**Few of these potential financial sources for SRSP have been interrogated in depth, or there are currently barriers to their use in shock responsive approaches.** Having provided this context, the

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<sup>5</sup> This paper also acknowledges that remittances and other local sources of funding, although not channelled to SRSP in a traditional sense, play a significant role in responding to shocks and make up a key part of wider development and humanitarian financing. Local sources of funding are not looked at here as they fall outside the formal tracking system, and need to be acknowledged and tracked much more rigorously.



next section looks at the financial instruments themselves, i.e. the mechanisms that are or could be used to channel finance to relevant programmes from these and other relevant sectoral sources and actors.

In summary, we find that:

- **Low funding to the social protection and humanitarian sectors before COVID-19 is now likely to be further constrained, potentially limiting SRSP efforts.** Funding in the coming years is expected to be impacted by the COVID-19 crisis, in terms of both national and international finance (see Annex II for a Covid-19 financing case study). This could put a strain on financing efforts for SRSP, at a time when its effectiveness at addressing covariate shocks has been comprehensively demonstrated in responding to COVID-19. With a likely reduction in available resources, there could be the temptation to retrench investment decisions along traditional sectoral lines, reducing investment in routine social protection, and thus impacting SRSP efforts, or focusing spending on immediate needs, as opposed to investing in future risk.
- **The investment case for governments to finance SRSP can appear divided.** One big hurdle for governments is the lack of incentives to invest, as the direct political gains are unclear, and the opportunity costs seemingly high. However, with climate change causing increasingly severe disasters, and in light of the effective response to COVID-19 through SRSP systems and programmes, investing more in well-structured shock responsive and disaster risk finance approaches is expected to continue.
- **Multiple sectors have the potential to fund SRSP, and financing comes from a mixture of sectoral sources and actors, yet funding in overall terms is currently low and hard to track.** While attention to DRF has been growing over time, only very small amounts of funding are properly organised in advance of crises. Of this, very little is allocated against appropriate delivery systems, such as those used for SRSP. Definitional ambiguity or a lack of obligation to report expenditure limits attempts to track financing in general, and SRSP financing in particular (which in any case is a relatively new area), which generally falls between initiatives supported through development and through humanitarian ODA.
- **There are a limited number of institutions that offer risk finance instruments, limiting in turn the options available to improve and diversify risk financing, and putting more pressure on humanitarian response in the event of shocks.** The increased focus of international financial institutions, such as the World Bank, on introducing a wider range of instruments, including in fragile and conflict-affected situations, offers potential new inroads for poorest countries to access finance, such as through Catastrophe Draw-Down Options (CAT-DDOs), and the Pandemic Emergency Financing Facility. However, some of these instruments have responded more slowly than expected, or have in effect been about reallocating funds, as opposed to enabling access to new funding.
- **Financing for SRSP can be channelled through the social protection sector, but other sectors, such as humanitarian finance, can make an important contribution, both now and in the future.** Humanitarian financing can make an important contribution, especially through anticipatory action measures, supporting the piloting and scaling of SRSP programmes (e.g. social assistance), and aligning interventions to support the social protection sector. For instance, humanitarian pooled funds have grown considerably (from a low base) in the last five years, and have begun to promote anticipatory action, offering a key connection to SRSP. However, humanitarian finance itself is framed by a range of factors (donor conditionality, government capacity, humanitarian principles, etc.) that limit its use for financing SRSP.
- **ODA is a critical component of financing for developing countries for both social protection and humanitarian assistance, but structural shifts in how support is provided are changing the picture of how states manage their resources.** Overall amounts of ODA have fluctuated substantially over the decades (Organisation for Economic Co-operation and Development [OECD], 2020), but overall ODA growth for Least Developed Countries is slowing, and spending in sectors key for strengthening human capital – health, education, and social protection – is decreasing as a share of total ODA (Caio et al., 2020). At the same time, there has been a pronounced growth in the percentage share of developmental ODA being delivered through bilateral and multilateral loans in crisis-affected countries, raising larger questions about how states will manage debt during the current economic crisis, and the impacts this will have on financing for SRSP in the future.
- **Climate finance, especially adaptation finance, has significant potential to fund SRSP, yet faces a series of barriers to doing so, particularly within the multilateral climate funds (see Box 6 for more details).** However, some successful country projects (e.g. the Philippines) offer hope that more funding for SRSP, presented in the right way, could be supported through climate finance funds such as the Green Climate Fund (GCF). Loss and damage finance could also provide a potentially relevant funding source

for SRSP, but this too faces multiple fundamental hurdles before it can become a reality (see section 4.3 on climate financing below).

## 4.1 International financing for social protection

### What is it?

Financing for national routine and SRSP in most low- and middle-income countries comes from a mix of domestic and donor funds, with low-income countries being particularly dependent on external donor funding for systems development and implementation due to their limited domestic resource mobilisation capacity (McCord *et al.*, 2021)].

This sub-section focuses mainly on international funding to social protection through ODA (which goes to both international and national actors, including national governments), though overall national governments fund the majority of social protection programmes through their domestic revenue. The intricacies of the domestic fiscal space and the sources of finance for social protection are not explored in this paper, as this is a topic that is extensively covered in the literature (e.g. Ortiz *et al.*, 2018). Shock responsive financial instruments used by governments for channelling revenue to programmes are explored in the next section.<sup>6</sup>

Total ODA, inclusive of allocations to social protection, humanitarian assistance and so forth, totalled US\$ 180 billion in 2019.<sup>7</sup> ODA comprised two thirds of total net resource flows to developing countries. ODA is provided through a mix of grant and concessional loan financing and is a critical component of financing to lower- and middle-income countries for social protection, both state-funded national provision, and also humanitarian provision. ODA may be allocated bilaterally, direct from the donor to the recipient governments, or multilaterally, through International Financing Institutions (IFIs) such as the World Bank Group, IMF, EU institutions, and regional development banks, or multilateral UN agencies. While overall ODA is dominated by bilateral flows, this is not the case for the social protection sector, where 69% of ODA was provided by multilateral agencies in 2019, a share which has increased steadily over the last decade. ODA growth overall for Least Developed Countries is slowing, and spending in sectors key for strengthening human capital – health, education, and social protection – is decreasing as a share of total ODA (Caio *et al.*, 2020).

At the same time, there has been a pronounced growth in the percentage share of developmental ODA (i.e. total ODA minus humanitarian finance) being delivered through bilateral and multilateral loans in crisis-affected countries, which rose from 13% of total ODA in 2010 to 30% in 2018. Long-term developmental grants have decreased in share from 75% to 55% over the same period (Development Initiatives, 2019; Caio *et al.*, 2020).<sup>8</sup>

Social protection forms one component of ODA financing<sup>9</sup> and is provided through bilateral and multilateral agencies and IFIs. ODA spending on social protection and other sectors has fluctuated over the decades. Of total ODA, 1–1.5% was directed to social protection during the late 2010s, and there was an increase in financing to the sector in 2020 due to the COVID-19 pandemic (McCord *et al.*, 2021). Donor agencies recognised the potential of social protection as a potential mechanism for shock response provision following the global financial crisis of 2008, resulting in significant investments in systems development. Interest in the sector was also stimulated by a number of major initiatives during the 2010s, most notably the adoption of the Agenda 2030, the Sustainable Development Goals (SDGs)

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<sup>6</sup> For an overview related to domestic financing opportunities for social protection, see Ortiz *et al.*, 2017: [www.social-protection.org/gimi/RessourcePDF.action?ressource.ressourceId=51537](http://www.social-protection.org/gimi/RessourcePDF.action?ressource.ressourceId=51537).

<sup>7</sup> The OECD DAC CRS data analysed in this report was retrieved from [OECD QWIDS](https://data.oecd.org/qwids/), and refers to gross ODA disbursements, using 2018 constant prices.

<sup>8</sup> Loans are also unevenly distributed across the most crisis-affected countries, with a small number of protracted crisis countries receiving a disproportionately large share of all ODA loans (Development Initiatives, 2019; Caio *et al.*, 2020).

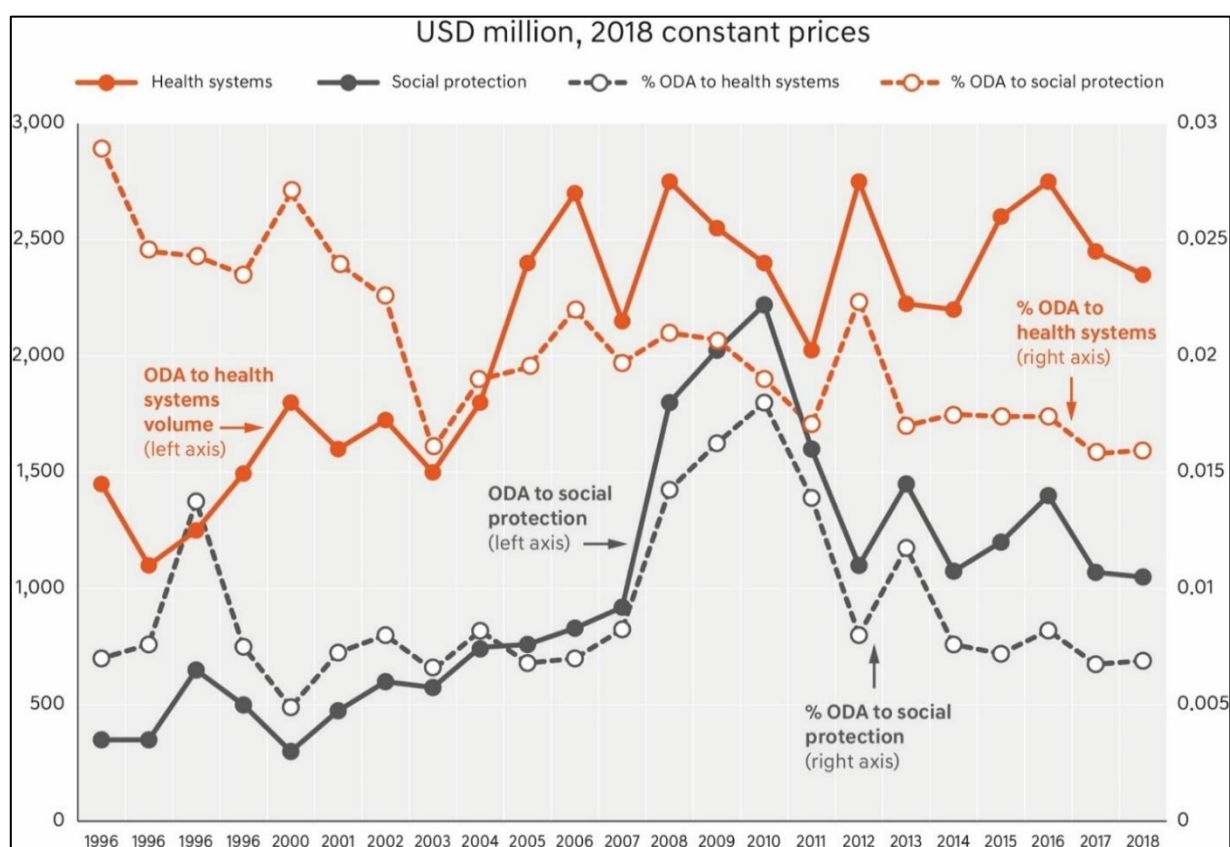
<sup>9</sup> OECD DAC code 16010 defines social protection as ‘social protection or social security strategies, legislation and administration; institution capacity building and advice; social security and other social schemes; support programmes, cash benefits, pensions and special programmes for older persons, orphans, persons with disabilities, children, mothers with newborns, those living in poverty, without jobs and other vulnerable groups; social dimensions of structural adjustment’ (OECD, 2020).

in 2015, and the World Humanitarian Summit in 2016, which identified social protection as a key instrument for attaining the SDGs (McCord *et al.*, 2021). Donors have played a key role in developing social protection systems in many low-income and also some middle-income countries, with donor flows to social protection through ODA used to finance state- and international partner-supported programmes.

## How much of it is there (overall and in relation to need)?

Before discussing financing for SRSP, it is worth noting that over the six years prior to the pandemic, only a little over 1% of total ODA was disbursed in support of routine social protection provision, reaching a high point of US\$ 2.4 billion in 2019. It is not possible to estimate the proportion of development or humanitarian ODA allocated to SRSP due to limitations in the granularity of the data collected by the OECD.<sup>10</sup> Social protection coverage is low, with only 45% of the world's population having access to any form of social protection, a figure which falls as low as 18% in sub-Saharan Africa overall, and is below 10% in many low-income countries (ILO, 2017). At the same time, needs are rising, with global extreme poverty increasing in 2020 for the first time in decades due to the combined impact of the pandemic, conflict, and climate change, pushing an additional 119–124 million people into extreme poverty in 2020 (Lakner *et al.*, 2021). The ILO notes that even prior to the pandemic there was a significant financing gap in terms of the provision of basic social protection (a universal package for child, maternity, disability, and old age care), in line with the commitments set out in the SDG Target 1.3 for social protection, and that post-pandemic the global funding gap will be US\$ 707 billion per annum, confirming the need for continued and increased financing from the international community. This gap represents 45% of total tax revenues in low-income countries in 2019 and at current levels ODA would be insufficient to close social protection financing gaps even if all of it were allocated to that single priority (Durán-Valverde *et al.*, 2020).

**Figure 2: Social protection and health systems allocations to ODA 1996-2018**



Source: Ahmad *et al.* (2020)

<sup>10</sup> ODA data is produced using the OECD-DAC Creditor Reporting System, which enables the measurement of allocations by sector or other purpose category 'non-sector allocable aid' (e.g. general budget support, humanitarian aid, etc.). It does not refer to the type of goods or services provided and each activity can be assigned only one purpose code activities; as a result, where funding cuts across several sectors, either a multi-sector code or the code corresponding to the largest component of the aid activity is used (McCord *et al.*, 2021).

Much of the limited social protection which is currently available is funded domestically, financed through taxation and deficit financing, and also through contributions in contexts where large-scale contributory social insurance schemes are in place. However, average public social protection expenditure remains low outside Europe, at 9.7% of gross domestic product (GDP) in Latin America and the Caribbean, 8.2% in East Asia, 7.4% in Southern Asia, 4.5% in Sub-Saharan Africa, and only 1.4% in South Eastern Asia, compared to 17.7% in Northern, Southern, and Western Europe (ILO, 2017).

ODA plays a significant role in social protection provision in some lower-middle-income countries and many low-income countries, particularly in terms of supporting non-contributory social assistance provision, and is likely to continue to do so in the future, particularly in the context of the COVID-19-induced fiscal contraction. However, notwithstanding the growing funding gap identified by the ILO. By way of example, in 2020 the UK government, one of the major social protection donors, announced cuts to its bilateral aid budget from 0.7 to 0.5% of Gross National Income, and other OECD DAC contributors may reduce contributions in 2022, having ringfenced or increased allocations in 2020 and 2021, including sources of IDA in the context of a global recession, and there is a risk that ODA may be significantly reduced in the short term (McCord *et al.*, 2021). It is not yet possible to assess whether the aggregate medium term effect of the Covid-19 shock on funding for the social protection sector will be positive, as in the case of the Global Financial Crisis of 2007/8 - or negative, as this will depend on both future ODA trajectories overall, and also the extent to which social protection is identified as a key instrument for recovery.

It is also critical to note that the economies of low- and middle-income countries are themselves facing significant fiscal constraints due to the economic contraction, and the existential debt crisis affecting many low-income countries even prior to the pandemic. Domestic financing for the social protection sector is likely to be severely compromised in the coming years, and even maintaining existing levels of provision may be a challenge unless external and domestic resources are ring-fenced for this purpose. The IMF has introduced some conditions as safeguards to protect domestic social sector allocations in a context of austerity, but it is not yet clear whether these will be effective given the severity of the crisis (McCord *et al.*, 2021).

This combination of low baseline domestic financing combined with domestic resource constraints, and fiscal constraints in DAC countries, means that conventional financing channels for social protection are likely to be inadequate in the short term to finance the expansion of provision anticipated under the SDGs.

## Who gives it?

As noted, much of routine social protection globally is funded from domestic sources, through taxation, deficit financing, and contributions from social insurance schemes. ODA is provided by members of the OECD DAC, an international forum of most of the world's largest donors, along with a small number of other donors who are outside the DAC framework. The five major ODA donors to social protection in recent years are the UK, which disbursed US\$ 250 million in 2019, the US (US\$ 112 million), Germany (US\$ 87 million), Denmark (US\$ 26 million), and Australia (US\$ 18 million) (McCord *et al.*, 2021).

## Who gets it?

Of the US\$ 2.4 billion ODA allocated to social protection in 2019, 50% was directed to low-income countries and 30% to lower middle-income countries (McCord *et al.*, 2021). As of 2018, half of all ODA for social protection was channelled through the public sector, 21% through civil society, and 18% through multilateral organisations, rising to 63% to the public sector in fragile states (OECD, 2020).

## Why does this matter for financing SRSP?

Evidence from the COVID-19 pandemic has confirmed the narrative developed within the shock responsive and adaptive social protection discourses, that the existence of basic social protection systems – including established institutions, personnel, national registries, identification, and payment mechanisms – is a key enabler of effective shock responses (see, for example, Barca, 2017; O'Brian *et al.*, 2018b; Lindert *et al.*, 2020; and Lowe *et al.*, 2021). In the absence of such systems, shock response interventions will necessarily remain reliant on predominantly externally financed humanitarian interventions (Costella *et al.*, 2021) (see [Annex II](#) for a Covid-19 financing case study).



Reducing the size of the risks to be transferred also reduces the cost of transferring the risk (Hobson, 2020). Adequate financing for the expansion and strengthening of 'routine' national social protection provision is an essential pre-requisite for being able to better respond to covariate shocks, inasmuch as it enables the development of systems (such as registries or payment systems) which can be adopted for shock responses. However, it is not necessarily sufficient unless those measures are 'risk-aware', meaning that they are able to address current or future covariate risk sufficiently. For instance, if routine social protection is not tailored to address a changing climate, its utility is limited.

One big hurdle for governments is the lack of incentives to invest in SRSP, as the direct political gains are unclear, and the opportunity costs seemingly great (if money is aside for something that is not guaranteed to happen, this reduces the potential to invest in tangible and visible projects), though as we note later, other investments (such as building the resilience of systems and people) do offer clear benefits in the immediate term. Another issue, as noted, is the limited number of institutions that offer risk finance instruments; in the cases where they do, the concern is that these hold the potential to increase the debt burden countries face unless well planned, without necessarily opening up avenues to new and fair forms of finance.

## 4.2 Humanitarian financing

### What is it?

There is no common definition of 'humanitarian financing' nor a common obligation across humanitarian donors on how to report their contributions to humanitarian crises. Broadly, humanitarian assistance is intended to save lives, alleviate suffering, and maintain human dignity during and after natural hazard-induced and man-made crises, as well as to prevent and strengthen preparedness (Development Initiatives, 2020). It should be governed by the humanitarian principles of humanity, impartiality, neutrality, and independence (Sphere Association, 2018). In addition, humanitarian financing according to the Good Humanitarian Donorship (GHD) group<sup>11</sup> should aim to be flexible, timely, efficient, coordinated, and predictable, and should support capacity building, partnership building, and strategy setting (GHD, 2016). This current paper follows the definition of humanitarian financing set out by Development Initiatives (2020), which 'refers to the financial resources for humanitarian action spent outside the donor country ... based on what donors and organisations report as such and does not include other types of financing to address the causes and impacts of crises ... referred to as crisis-related financing' (Development Initiatives, 2020, p. 81).

Organisations can track international humanitarian financing through the main reporting platforms of OECD DAC Creditor Reporting System, and OCHA's Financial Tracking Service (FTS), as well as data on humanitarian activities published by the International Aid Transparency Initiative Standard. Different terms are used across these databases to tag resources, meaning it is difficult to obtain an overall picture of funding flows to different actors and activities. The above methodology generally does not capture the contributions of national actors to their own crises, and the data on private donations to international humanitarian assistance is limited, as few private donors voluntarily report their contributions to the UN's FTS or the OECD DAC's Creditor Reporting System, and it is not possible for agencies to indicate whether the funding they received was from institutional or private sources (Development Initiatives, 2020).

### How much of it is there (overall and in relation to need)?

In 2019, a total of US\$ 29.6 billion was provided by donors in international humanitarian assistance from all sources to all types of crisis. This marked a 5% decrease from 2018, and was the first fall since 2012, mostly due to a reduction in support from public donors such as governments and EU institutions. However, humanitarian needs continued to rise. When looking solely at UN-coordinated humanitarian appeals, there was a 5% increase from 2018 in funding requested across 36 regional and national

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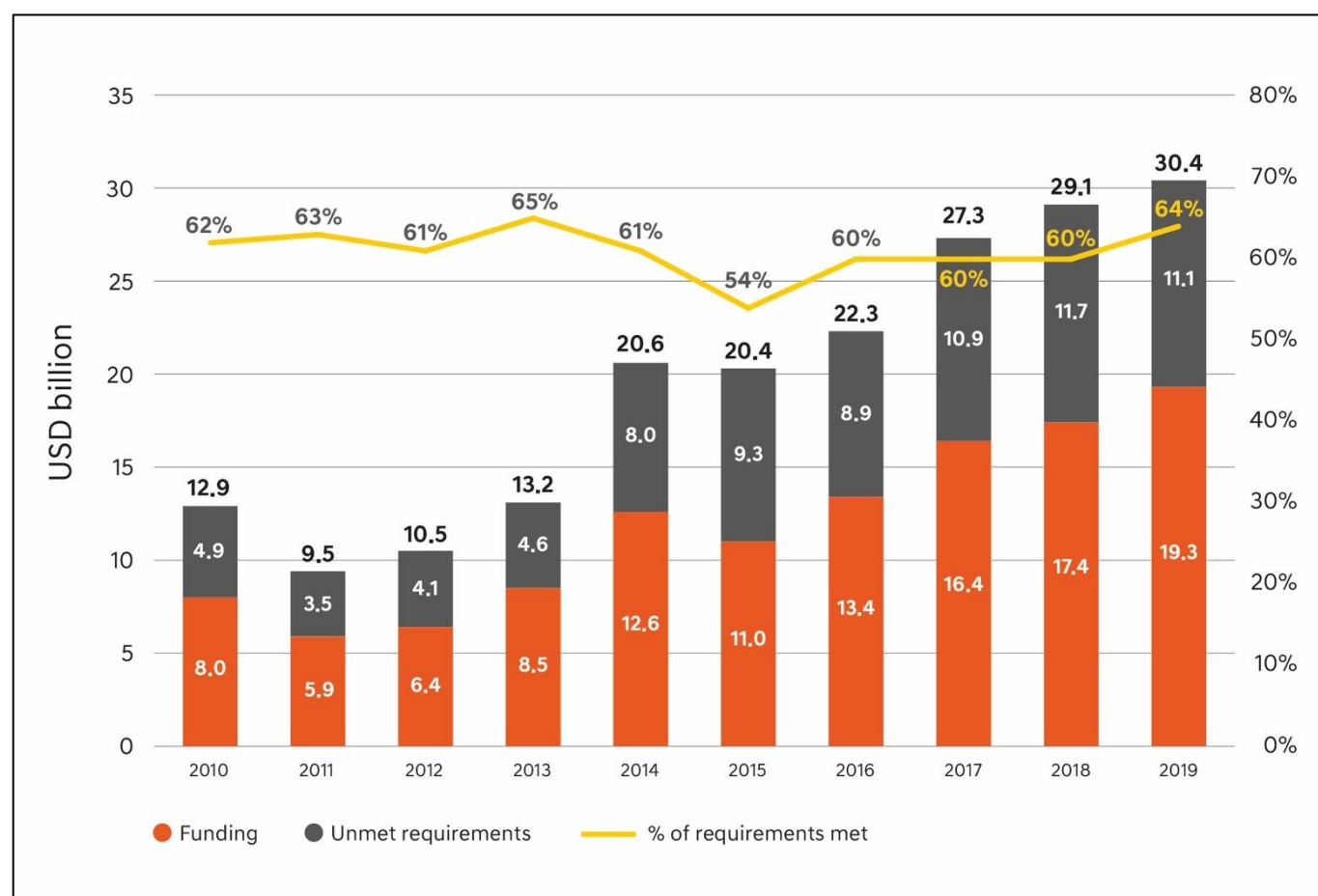
<sup>11</sup> The GHD initiative is an informal group of 42 donors who work together to advance an endorsed set of 24 GHD principles and good practices. In so doing, they aim to improve donor coherence and coordination, and engagement in humanitarian action. The GHD framework has played an important role in underwriting the process of humanitarian reform, most notably around financing mechanisms and cluster-based coordination. See: [www.ghdinitiative.org/ghd/gns/home-page.html](http://www.ghdinitiative.org/ghd/gns/home-page.html)

appeals, rising to a new high of US\$ 30.4 billion. As shown in Figure 3, between 2010 and 2019, humanitarian appeals increased 135%, from US\$ 12.9 billion to US\$ 30.4 billion.<sup>12</sup>

In addition, the size of appeals, and the amount they are funded varies widely. Of the 36 UN appeals in 2019, the Syria Refugee Response and Resilience Plan requested US\$ 5.4 billion, while at the other end of the scale the Iran appeal requested US\$ 25 million. A quarter of appeals received 75% or more of the funding, while a third received 50% or less, with the average needs-to-funding ratio across all appeals at 64%, in keeping with the decadal average of 61% (Development Initiatives, 2020).

Meanwhile, a look at global trends shows that humanitarian assistance makes up a relatively small percentage of overall ODA (for example, 16% or US\$ 27 billion of US\$ 167 billion in 2016), but in the top crisis-affected countries it has grown faster as a total share of overall ODA in the last decade (Development Initiatives, 2017; Development Initiatives, 2020). Other international flows to crisis-affected countries are also important. For instance, for countries with humanitarian appeals for two or more consecutive years, remittances make up 37% of international finance, while foreign direct investment constitutes 12% (Development Initiatives, 2020). Likewise, a very small percentage of ODA is channelled to disaster risk reduction activities (0.88% in 2018, US\$ 1.3 billion out of US\$ 147 billion), a telling statistic given that the majority of major crises are protracted, and 13 of the 20 countries most vulnerable to climate change also have a global humanitarian appeal in 2021, with most also experiencing an active conflict (Development Initiatives, 2019; Caio *et al.*, 2020; The New Humanitarian, 2021).<sup>13</sup>

**Figure 3: Funding and unmet requirements, UN-coordinated appeals, 2010–2019**



Source: Development Initiatives, 2020, based on UN OCHA FTS and United Nations High Commissioner for Refugees (UNHCR) data

<sup>12</sup> The increase between 2007 and 2019 is even steeper, at 452%.

<sup>13</sup> It is, however, well targeted. Of the total of US\$ 1.3 billion, 77% (US\$ 973 million) went to 60 countries at very high or high risk of experiencing natural hazards (Development Initiatives, 2019).



## Who gives it?

Humanitarian donorship has long been monopolised by a few key players, though the picture has begun to change. Twenty donors provide 97% of international humanitarian aid, with the top five dominated by the US, UK, and EU. In the last three years Turkey, Saudi Arabia, and the UAE have also made the top 11, with Turkey currently the largest humanitarian donor, although its contributions are not directly comparable, given that most of its expenditure goes on supporting Syrian refugees within its borders and through its own systems.

Between 2015 and 2019, private sector contributions consistently made up just over a fifth of total international humanitarian assistance, averaging US\$ 5.7 billion between 2014 to 2018, with the single largest source coming from individuals (68%), and the majority going to non-governmental organisations (NGOs) and natural hazard-induced disasters. Another growing role of the private sector is investment in risk transfer mechanisms, also discussed in more detail in Section 5 below (Development Initiatives, 2019).

## Who gets it?

Organisational recipients of international humanitarian funding have remained relatively stable over the past five years, even as the total volume of aid has increased, with initial trends from the COVID-19 response appearing to continue and retrench this pattern. Donors have clear preferences as to where their money goes.

In 2018, two thirds of funding from donor governments (US\$ 15.6 billion) went to multilateral organisations, reflecting the approximate average for the last five years. Despite a slowdown in donor giving in 2019, funding committed through UN-coordinated appeals rose to a record high of US\$ 19.3 billion (Development Initiatives, 2019; Development Initiatives, 2020). Meanwhile, during a fourfold increase in humanitarian funding since 2002, the top three UN humanitarian agencies – the WFP, the UNHCR, and UNICEF – have consistently accounted for around half of the total figure given to all UN agencies (see Table 1 below) (Konyndyk, 2018).

Beyond the UN agencies, in 2019 donor governments directed 16% (US\$ 4.1 billion) to NGOs, a decrease of 20% from 2017 (Development Initiatives, 2020). As noted, the private sector provides the majority of its funding to NGOs (89% – US\$ 5.3 billion – in 2018), with private contributions comprising 56% of the total funding received by NGOs in 2018. The International Red Cross and Red Crescent Movement fundraise separately from the UN-coordinated appeals, and generally meet about 80–90% of their needs annually (Konyndyk, 2018). International Committee of the Red Cross (ICRC) appeals, which respond mainly to conflict-related situations, remained 92%-funded in 2019, consistent with their five-year average (Development Initiatives, 2020).

**Table 1: Net allocations of humanitarian funding, 2002–2017**

Organisation type	Average 2002–2017
<b>WFP, UNHCR, UNICEF combined</b>	48.7%
<b>Other UN</b>	9.4%
<b>Red Cross/Crescent Movement</b>	9.4%
<b>Pooled funds</b>	5.3%
<b>National government</b>	3.6%
<b>NGOs</b>	20.8%
<b>Other</b>	2.8%

Source: Konyndyk, 2018

Despite the Grand Bargain signatory donors committing to channel at least 25% of international humanitarian assistance to local and national actors by 2020, in 2019 this figure stood at 2.1% (US\$ 444 million), actually decreasing from 3.5% (US\$ 782 million) in 2018. Of this, the majority in 2019 (72%) was provided directly to national governments, with local and national NGOs receiving 25%, an increase from 12% in 2016, and 3.5% going to the Red Cross Red Crescent movement (Development Initiatives,

2020). Obtaining information on how much countries contribute to their own responses is also difficult, as most governments do not report this as international humanitarian assistance (except in certain cases, such as Turkey). However, as the Turkey case indicates, these sums, be they in cash or in-kind (food assistance, technical and logistical support, human capacity, etc.) can be sizeable.

### Box 3: Humanitarian reform and links to financing

Faced with these financing and other challenges, humanitarian stakeholders have implemented several rounds of large-scale reform, in 2005, 2011, and 2016; these have often been launched following large-scale crises that highlighted wider structural faults in the humanitarian system.<sup>1</sup> Each had similar key financing themes at their core – linking resources to needs-based programming, more predictable, adequate, flexible and multi-year funding, improving coordination and leadership, and decentralising financing down to crisis or country level (Overseas Development Institute and Centre for Global Development, 2015; Konyndyk, 2019). The COVID-19 crisis has further exposed some of these fundamental structural weaknesses (see [Annex II](#) on COVID-19 below).

One central weakness in these rounds of reform has been, as Konyndyk puts it, the push for 'better-coordinated fragmentation, while ignoring the upstream business model that finances and shapes incentives for humanitarian response' (Konyndyk, 2018, p. 1).<sup>1</sup> There is also the symbiotic relationship between the largest donors and 'Big Three' UN humanitarian agencies – WFP, UNICEF, and UNHCR – which over the last decade have accounted for 50% of humanitarian funding (see Table 1 above).

This permits donors to channel resources, pool administrative responsibility, and manage corporate risk and downstream partners, while the agencies' end-to-end business model defines the needs, delivers the assistance, and evaluates programmatic results. However, this not only provides little incentive for reform, it generates sector-specific business models ill-equipped to support multi-sectoral needs, and leaves little room for the empowerment of governments, NGOs, and beneficiaries (Anderson *et al.*, 2012; Konyndyk, 2018). While the focus in global discussions and commitments has shifted towards finding sustainable, multi-sector solutions for humanitarian crises that put governments first, humanitarian financing trends demonstrate that those commitments are not being met. A lack of appropriate humanitarian financing also hampers the ability of the humanitarian community to do their work effectively, as well as to engage in wider programming 'across the nexus' (Cherrier *et al.*, 2019).

However green shoots are emerging. Recent reform efforts such as the Grand Bargain of 2016 included donors as direct signatories for the first time; they committed to change their own practices and to demand greater transparency and efficiency from the principal implementers, though the agreements again lack enforcement mechanisms (Konyndyk, 2018). The use of unrestricted cash transfers in humanitarian crises increased by 64% between 2015 and 2019, comprising 19% of global humanitarian spending in 2019 (Abell *et al.*, 2018; Development Initiatives 2020); this by definition erodes the boundaries between sectors by letting the beneficiary decide how transfers are spent. Likewise, as noted, contributions to global and country based pooled funds are increasing, as is investment in anticipatory action, with humanitarian actors also looking to support countries to invest in risk transfer and pooling mechanisms such as ARC. The COVID-19 response has forced humanitarian donors and implementing agencies to introduce significant flexibility to some existing and new funding arrangements to ensure programmes can continue, address new needs, and operate remotely. Examples include increased budget-line flexibility and altering cost eligibility to continue staff employment during project suspension (Development Initiatives, 2020). In the case of CBPFs, there is an indication that newly adopted flexible guidance will be applied beyond COVID-19.

Pooled funds (either at global or country level) combine contributions from different donors to provide rapid, needs-based support to humanitarian responses (including underfunded appeals). Pooled funds were used and adapted significantly to address the effects of the COVID-19 crisis. Global pooled funds have seen sustained growth since 2010, more than doubling in size from US\$ 827 million to US\$ 1,869 billion, while Country-Based Pooled Funds (CBPFs) have more than doubled since 2015, reaching a total of US\$ 1,040 billion in 2019.<sup>14</sup> International and national NGOs consistently receive more than two thirds of the funding allocated from CBPFs (Development Initiatives, 2020). As discussed in Section 5 below, a growing area of investment for pooled funds is in anticipatory and forecast-based action, integrating many of the principles of DRF into humanitarian action. A wide array of actors are piloting and scaling such initiatives, some initiatives with strong links to social protection,<sup>15</sup> and although overall levels of finance to anticipatory action remain small, this reflects the important role that anticipatory

<sup>14</sup> In 2019, four CBPFs (Yemen, Syria cross-border, South Sudan, and Iraq) accounted for over half this total.

<sup>15</sup> See, for instance, the range of initiatives in Forecast Based Action alone, one part of wider anticipatory action, in Wilkinson *et al.* (2018).

humanitarian action can play in the wider vision of SRSP financing. However, various constraints on humanitarian action (humanitarian principles, aid politics, etc.), mean that broader simultaneous investment is required from development and government actors to mainstream risk and prepare for crises (Levine *et al.*, 2020).

## Protracted crises

The majority of crises are protracted and complex.<sup>16</sup> The number of countries experiencing such crises has increased 58% over the past 15 years, from 13 in 2005 to 31 in 2019. Over one billion people live in countries experiencing protracted crises; these countries are home to half of the world's people living in extreme poverty (Development Initiatives, 2018; Development Initiatives, 2020). As a result, in 2016, 74% of humanitarian funding went to crises of eight or more years in length, and in 2018, all of the ten largest humanitarian aid recipient countries were experiencing protracted crises (Development Initiatives, 2017; Development Initiatives, 2020). Financing for these crises should reflect their complex and long-term nature, addressing humanitarian and development needs in tandem. Yet the majority of humanitarian funding remains short term in length (one year or less) and earmarked (to specific projects or activities), limiting the capacity of humanitarian actors to manage resources flexibly, holistically, and cost-efficiently. Meanwhile, as noted above, for the 20 largest recipients of humanitarian assistance, increases in humanitarian assistance have not been met by increases in non-humanitarian ODA (Development Initiatives, 2018).

## Summary – Why does this matter for financing SRSP?

Global social policy dialogues are increasingly coalescing around the shift away from conventional humanitarian models towards nexus and shock responsive programming. Humanitarian financing features in DRF or SRSP financing discussions, although in many instances this is seen as a costly provider, post-crisis. This reflects the tension at the heart of international humanitarian financing, which was originally set up to act as a 'provider of last resort' when states were incapable or unwilling to address crises within or across their borders, but in many protracted crises has become the continuous provider of life-saving support, as well as other essential services, for those most in need.

A restrictive view of humanitarian action and finance elides the important role it will continue to play pre- and post-crisis, including as part of shock responsive approaches, regardless of overall increases in SRSP systems efficiency. In fact, a significant number of humanitarian actors are already financing SRSP initiatives, mostly on a small scale or in a pilot form, either independently, aligning with government, or (to a lesser extent) through national systems and programmes themselves. This is especially true in certain fragile and low-income countries and contexts, where national governments elect to transfer the risk of responding to covariate shocks onto humanitarian actors and instruments, for a mixture of reasons, including an unwillingness to take on the risk/expense, or a lack of capacity; or where humanitarian actors and instruments may in fact be the more appropriate shock responsive model to use (based on geography, shock typology and scale, beneficiary type, government capacity and legitimacy, etc.).

Structural constraints – such as tight donor conditionality, and limited investment in multi-year, pooled fund, or anticipatory mechanisms – limit the ability of the humanitarian community to meaningfully engage in nexus and shock responsive approaches. More efforts are needed to support systematic reform in areas of relevance to SRSP, such as the increased use of pooled funds, anticipatory action, and cash; to align and leverage investments 'across the nexus' between humanitarian, DRM, and social protection partners; and to prompt wider governmental reform in areas key to this agenda (around institutional mandate, PFM, the fiscal space, etc.). Without this concerted effort inclusive of humanitarian actors, donor and national government prioritisation to SRSP (and its financing) may remain low in countries that could benefit from it the most and make up the largest percentage of year-on-year humanitarian requirements.

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<sup>16</sup> Protracted crisis countries are defined as countries with at least five consecutive years of UN-coordinated humanitarian or refugee response plans (Development Initiatives, 2020).

## 4.3 Potential financing: climate finance

### What is it?

According to the Standing Committee on Finance of the UN Framework Convention on Climate Change (UNFCCC), climate finance is defined as 'finance that aims at reducing emissions, and enhancing sinks of greenhouse gases; and aims at reducing vulnerability of, and maintaining and increasing the resilience of, human and ecological systems to negative climate change impacts' (UNFCCC, 2014). This definition is purposefully broad to include public and private finance and flows within and between developed and developing countries. It also encompasses both mitigation finance (which aims to reduce greenhouse gas emissions as the root cause of climate change) and adaptation finance (which aims to support the adjustment to climate change in order to moderate harm or exploit beneficial opportunities).

The above definition notably does not include loss and damage finance; this covers adverse impacts of human-induced climate change that cannot be or will not be avoided by mitigation or adaptation. Loss and damage finance remains a politically charged topic in international climate change negotiations, and one which has not, to date, resulted in any financial provision under the UNFCCC, multilateral climate change funds, or bilateral and multilateral climate finance support. There are increasing demands for dedicated source of financing for loss and damage, emanating from several particularly vulnerable developing countries and some civil society organisations (see Care and Oxfam International, 2017), and at the last Conference of Parties in 2019, in Madrid, a decision was made to establish an expert group tasked to clarify how the access of developing countries to existing GCF funds and existing financial resources for loss and damage can be facilitated. Commentators have noted, however, that discussions to date have largely been symbolic in nature (Raju *et al.*, 2021).

For the purposes of this paper, the focus is on climate finance which flows from developed to developing countries; within this, particular emphasis is on adaptation flows as these have the most potential relevance for financing SRSP (discussed further in this sub-section below). Should discussions on loss and damage finance bear fruit in future, this may in turn become a potentially relevant funding source, but the discussions here reflect the financing currently available.

### How much of it is there (overall and in relation to need)?

Estimating how much climate finance is needed, and tracking how much is being provided, is fraught with methodological difficulty. The question of need relates to complexities in terms of the scenario-based forecasting of climate change impacts, and for the question of tracking, the issue relates to the definitional ambiguity of what counts as climate finance (vs finance for routine development spending). Nonetheless, various estimates have been made.

Regarding needs for adaptation finance, the UNEP 2016 Adaptation Gap Report concluded that annual costs of adaptation in developing countries could range from US\$ 140 billion to US\$ 300 billion annually by 2030, potentially rising to US\$ 500 billion per year by 2050. Estimates of mitigation needs in developing countries required to limit global temperature rises to 2°C vary widely, but the main studies suggest a range of US\$ 180–540 billion per year between 2010 and 2030 (Fankhauser *et al.*, 2016). There has been a longstanding recognition that developing countries cannot be expected to fund these costs themselves: the UNFCCC is founded on the principle of 'common but differentiated responsibility and respective capabilities', which enables and requires developed country parties (termed Annex II parties) to provide financial assistance to developing country parties in implementing the objectives of the UNFCCC. In the Copenhagen Accord in 2009, Annex II parties pledged to mobilise US\$ 100 billion annually by 2020 to support developing countries with mitigation and adaptation (specific targets or shares were not specified); in the 2015 Paris Agreement, this target was further reinforced, with a goal to raise the target after 2025 and a recognition that this funding would come from a 'wide variety of sources, public and private, bilateral and multilateral, including alternative sources of finance'. If met, this commitment would go some way towards narrowing the climate financing gap, but would stop far short of closing it (the 2020 target, if fully realised, represents less than a third of the lower bound estimated costs by 2030, providing further justification for loss and damage finance, and more ambitious adaptation and mitigation finance commitments).

The authoritative account of realised climate finance flows comes from the UNFCCC Standing Committee on Finance's Biennial Assessment, the primary purpose of which is to track performance against financial commitments under the Paris Declaration. At the time of the last assessment (published in 2018, covering flows in 2015 and 2016), a total of US\$ 49.4 billion was reported by Annex II countries



in 2016, up modestly from US\$ 45.4 billion in 2015. Of this amount, approximately US\$ 5.6 billion (11%) was for adaptation purposes (UNFCCC Standing Committee on Finance, 2018). More recent estimates point to further growth in recent years. For example, CPI's 2019 Global Landscape of Climate Finance report identified US\$ 72 billion of climate finance flows from OECD to non-OECD countries in 2017/2018 (averaged across the two years) (CPI, 2019). Meanwhile, OECD 2020, which looks at total pledges in 2020 from climate finance from public sources only (multilaterals, bilateral, and climate funds) identifies US\$ 66.8 billion of funding, of which 24% or US\$ 16 billion was for adaptation. There are significant challenges associated with tracking climate finance, some of which are discussed in Box 4 below; these challenges go some way towards explaining the variation between these estimates.

#### Box 4: Challenges in tracking climate finance

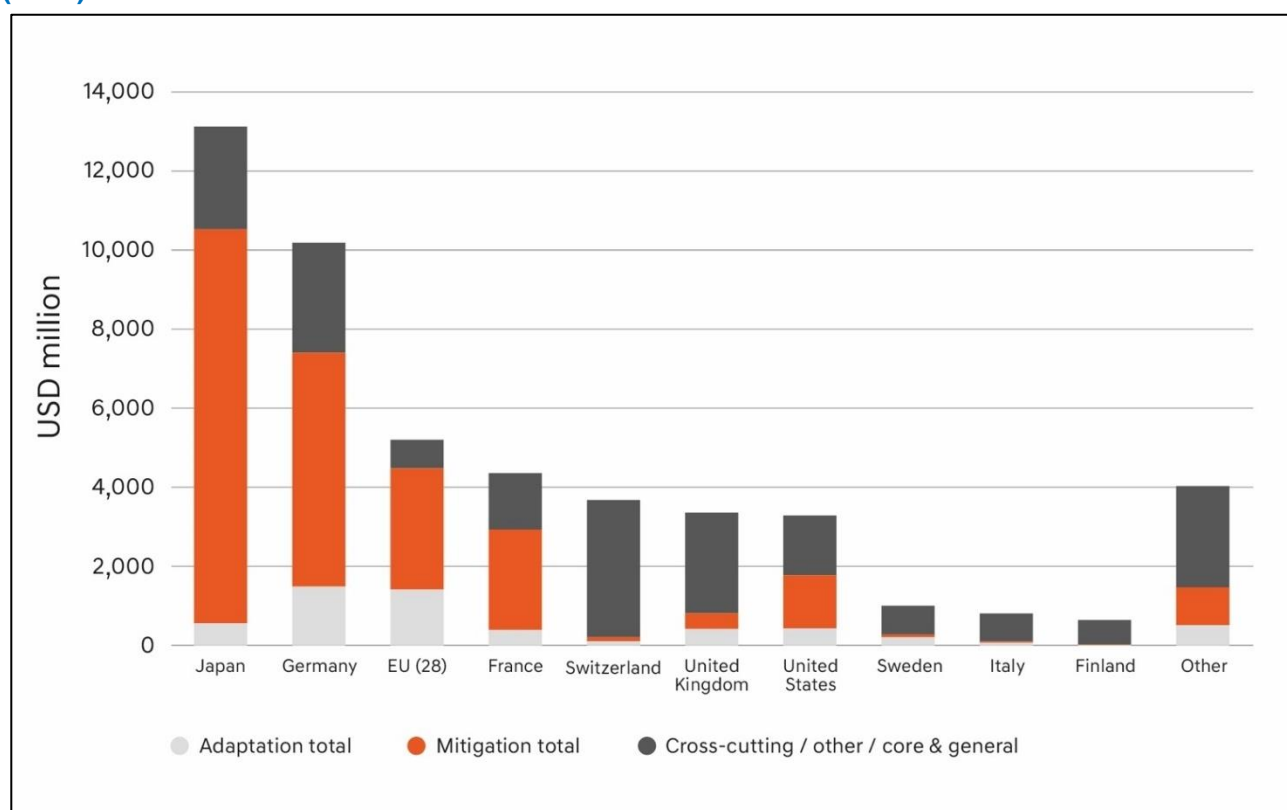
Some of the methodological challenges associated with tracking climate finance include definitional ambiguity around what does or does not count as climate spending. This problem is particularly pronounced for adaptation spending, which delivers routine development benefits, as well as benefits related to climate resilience. Accusations of overclaiming climate relevance have led to accusations of 'green washing' in order to show progress against targets. Double counting is another commonly discussed challenge, one particularly important in relation to climate ODA which may flow from donor governments through multiple channels of multilateral, climate funds, and/or implementing agencies. Much debate is also had around how to report on climate finance through lending instruments, and whether it should be counted differently from grant finance. Further, the US\$ 100 billion target is clear in that it relates to new and additional financing, but in practice distinguishing between flows which are additional and flows which have been reprogrammed, for example from other ODA budgets, is challenging. Lastly, while relative reliable and timely reports on donor funds can be sought through the OECD DAC Creditor Reporting System and in Annex II Party Biennial Reports, significant data gaps exist around the tracking of private sector investment and domestic government expenditure on climate change, particularly in developing countries.

Source: UNEP 2020, OECD 2020. and UNFCCC SCF 2018

#### Who gives it?

The top largest donors of climate finance for developing countries are noted below, with the largest contributions coming from Japan and Germany in 2016.

Figure 4: Climate finance flows from developed to developing countries, by donor and theme (2016)



Source: UNFCCC SCF 2018. Amounts of climate-specific finance and core/general funding provided to developing countries in 2016, as reported in their Biennial Review tables

Of the total US\$ 49 billion in climate finance flows going from developed to developing countries, the majority of this (68%) came through bilateral and regional channels, with the remainder going through multilaterals (8% as contributions specifically for climate, and 24% as core support for multilaterals, thereafter spent on climate change investments). Multilateral flows include financing via the international climate funds. Table 2 below lists all international funds which made commitments to developing countries in 2016. Chief among these is the GCF under the UNFCCC, which was set up with the intention of becoming a primary channel through which to route the US\$ 100 billion to developing countries. However, slow disbursement progress has prevented it from realising this ambition; this linked to various factors including a project-by-project funding approach, and onerous access and investment eligibility criteria (GCF Internal Evaluation Unit, 2019).

**Table 2: Multilateral climate funds**

Commitments, FY 2016 (US\$, million)

	Adaptation	Mitigation	REDD+	Multiple objectives	Total
<b>Adaptation for Smallholder Agriculture</b>	35	0	0	0	35
<b>Adaptation Fund*</b>	32.34	0	0	0	32.34
<b>Least-developed Country Fund*</b>	74.2	0	0	0	74.2
<b>Pilot Program for Climate Resilience</b>	10.43	0	0	0	10.43
<b>Special Climate Change Fund*</b>	7.58	0	0	0	7.58
<b>GCF*</b>	344.51	798.18	163.49	8.5	1314.68
<b>Forest Investment Program</b>	48.77	0	48.77	0	97.54
<b>UN-REDD Programme</b>	32.22	0	32.22	0	64.44
<b>Clean Technology Fund</b>	0	498.5	0	0	498.5
<b>Global Environment Facility*</b>	0	191.12	0	0	191.12
<b>Scaling Up Renewable Energy Program in Low Income Countries</b>	0	73.45	0	0	73.45
<b>Partnership for Market Readiness</b>	0	0.35	0	0	0.35
<b>Global Climate Change Alliance</b>	0	0	0	51.36	51.36

Source: Authors, based on UNFCCC SCF 2018. \* Indicated fund established under the UNFCCC

## Who gets it?

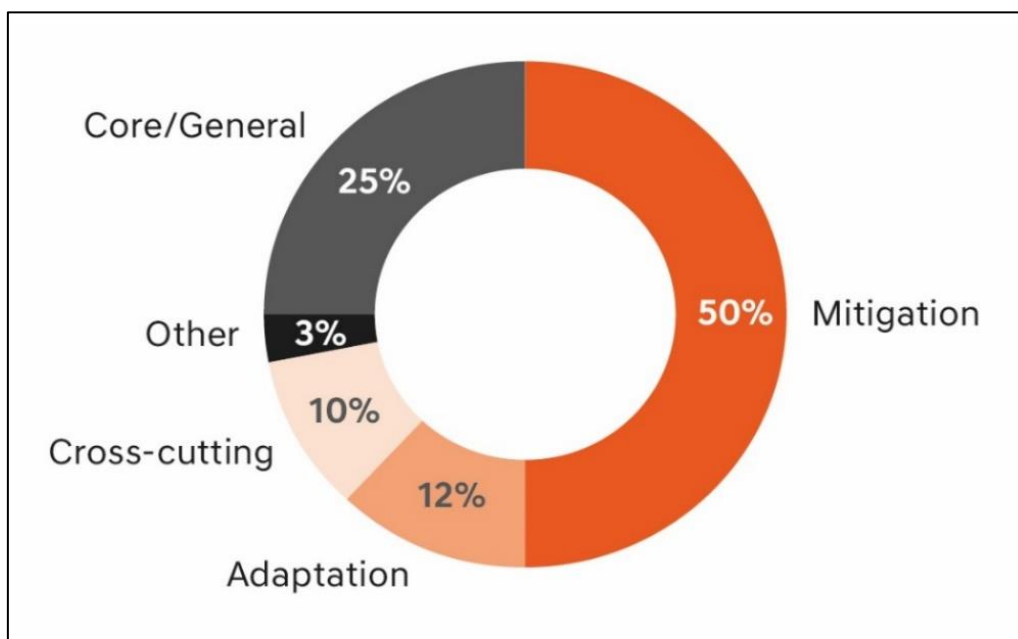
In terms of the geographic destination of climate finance flows to developing countries, over the 2015–2016 period, Asia was the principal recipient region for public climate finance flows, receiving 31% of funding from multilateral climate funds, 42% of bilateral finance, and 41% of Multi-lateral Development Bank (MDB) flows. Sub-Saharan Africa secured 22% of financing from multilateral climate funds, 30% of bilateral financing, and just 9% of MDB financing in the same period. Smaller shares went to other regions (UNFCCC SCF, 2018).

In relation to the type of recipient, 61% of climate finance from bilateral agencies went to national and sub-national governments, with the rest going to international organisations, NGOs, and private organisations. Climate finance from multilateral development banks and development agencies, such as the World Bank, regional development banks, and the EU, also goes primarily to governments; this accounts for 65% of total disbursements in 2016 (these are distinct and recorded separately to the multilateral climate funds in the table above). In the case of international climate funds, each have



different rules on eligible recipient entities. For the GCF, accredited entities (who have the right to apply for GCF funds) can be state or non-state actors (usually, they are UN agencies or private sector entities), but accreditation for low-income governments can prove an overly burdensome process, and as a result some 82% of commitments have been channelled through international accredited agencies rather than national ones (GCF Internal Evaluation Unit, 2019). This reflects varying attitudes to fiduciary risk from the different providers of climate finance. Given that social protection systems tend to be systems led and managed by governments, the implication is that access to climate funds for social protection systems is likely to be more challenging in the case of international climate funds, as compared to bilateral or multilateral providers.

**Figure 5: Thematic split of developed country climate finance flows to developing countries (2016)**



Source: UNFCCC SCF, 2018

In relation to the thematic destination of climate finance, most climate finance flows to developing countries is for mitigation (50% in 2016), with much smaller amounts going to adaptation (12%). This tallies with the sectoral distribution of climate finance as reported in OECD 2020, which indicates that between 2016 and 2018, the energy sector accounted for 34% of the three-year average flows, followed by transport and storage (14%). Other dominant sectors are agriculture, and water and sanitation. In general, very little climate finance is presently understood to be channelled to the social protection sector, although concrete estimates could not be found. This is particularly the case for multilateral climate funds. In the case of the GCF, for example, in a review of the 11 approved adaptation projects with government implementation partners, just one had a component which was related to SRSP (see Box 5). For climate finance delivered through bilateral and multilateral agencies, there is anecdotal evidence of more funding going to social protection; however, not all funders report to this level of detail. The World Bank, for example, reported commitments of US\$ 14 billion in climate-related finance in 2019, of which US\$ 445 million was identified as being for ‘social protection and jobs’ (distinguishing between these is not possible in available data) (World Bank, 2020). The UK Government’s *2020 UK Climate Finance Results* report documents that of the £5.8 billion of climate finance between 2016/17 and 2020/21, 87 programmes were reported to have contributed to the goal of ‘helping people cope with the effects of climate change’, a portion of which went to ensuring that social protection mechanisms are in place to make sure that people are able to cope with and quickly recover from weather-related shocks (HMG, 2020) (a detailed breakdown of the financing for social protection from the UK could not be identified).

Un-earmarked climate finance, through the form of general budget support linked to broader climate policy reforms, is a small but promising modality; some of this could certainly be used to finance SRSP at government discretion. However, this is currently provided only by a few multilateral partners (chiefly the World Bank and the EU) in a handful of countries.

## Box 5: GCF support for Shock Responsive Social Protection in the Philippines

The Government of the Philippines had an adaptation project approved for funding under the GCF in 2019 focusing on “Multi-Hazard Impact-Based Forecasting and Early Warning System”. It includes a component to develop early action protocols for shock-responsive social protection in four local governments, building on a pilot implemented by the UN. In particular, the project was designed to install and expand observation networks, generate hazard maps and risk-models, and develop early-action protocols, communication strategies and cyclone-response plans. The proposal did not request GCF funding to finance the actual transfers of the SRSP system, but rather to strengthen the forecasting component of the system. This was likely critical in getting GCF board approval for the project, which emphasises the need to be “sustainable” and “transformational” in its financing agreements.

*Authors, based on GCF 2019*

This relates to a broader debate around what does or does not count as climate adaptation, with some funders (including the GCF) so far showing some hesitation to accept wider definitions of climate adaptation which could be construed as development investment, albeit with a climate resilience angle. The case of a rejected GCF proposal, summarised in Box 6, is an example of this.

## Box 6: Definitional ambiguity in what counts as adaptation: GCF financing in Ethiopia

In a very few cases, proposals for funding submitted to the GCF have been rejected, or the applicants have been advised to withdraw the proposal to avoid the political embarrassment and negative press attention that goes along with rejection. These cases have primarily been related to adaptation projects, with the applicants and some GCF board members displaying diverging views on what should or should not be considered climate change adaptation.

The first rejected proposal under the GCF related to a submission in 2017 from UNDP and the Government of Ethiopia for a US\$ 99 million adaptation project proposal. The project aimed to support 1.2 million vulnerable people by a combination of improving access to water and food, promoting alternative livelihoods, empowering women, improving health and well-being, increasing access to climate information, improving the resilience of ecosystems, and introducing improved and climate-smart technologies. The project was presented to the GCF as a climate adaptation project; the justification for this was that with a diverse number of interventions, the communities would be more resilient to climate change.

Prior to the board meeting at which the project was considered, the GCF’s independent Technical Advisory Panel had recommended that the project should not be approved in its existing format and that it should be redesigned to prioritise water-related activities and other sectoral and landscape interventions. This led to a divergence of opinions on the board, with some members objecting based on the panel’s report, and the disparate nature of the components, not all of which were considered to be clearly climate-linked. Broadly speaking, the developed country board members opposed the approval of the project, while developing country members were more in favour of it. For example, the UK board member is cited as stating that the extensive list of actions was to improve rural development and that climate additionality was not clear. The board member from the Democratic Republic of Congo reportedly appealed for a solution to be found, stating ‘people forget that this institution is not a bank. This is a Fund of the UN Framework Convention on Climate Change [and] Article 4.9 of the Convention is about giving special considerations on finance and technology to the Least Developed Countries.’ The delegate went on to note that there was no seamless differentiation between climate and development, and that a good adaptation project must address different aspects of vulnerability. Similarly, the Malawi delegate argued that the project was trying to support communities who had become vulnerable due to climate change, so it was a climate-change project (TWN, 2017; GCF 2017).

With no consensus to be found, the project was ultimately rejected, a decision which drew criticism from some commentators. For example, Oxfam US is quoted in *Climate News* as saying that ‘this is the kind of thing the GCF needs to fund; it is part of the reason we advocated for the GCF to be created in the first place. I think there is a clear bias against projects focused on people. They are okay with making bridges climate-proof, but not poor communities.’ Saleemul Huq, a Bangladeshi researcher into climate adaptation, expressed similar frustrations, saying that the board ‘are putting impediments in the path of the most vulnerable and they are passing stuff that’s just routine infrastructure’ (Climate Home News, 2017).

*Source: TWN, 2017; GCF 2017; and Climate Home News, 2017*

## Why does this matter for financing SRSP?

Presently, large portions of climate finance – particularly that emanating from international climate funds – is not a relevant financing source for SRSP for the reasons set out above: funding to date has focused more on mitigation than adaptation, and some of the providers of adaptation finance have shown a hesitance to adopt a holistic definition of adaptation which could include interventions such as SRSP. Arguably, however, these interventions should be included: climate change is a risk multiplier, and gradual climate-related temperature changes and extreme events are damaging livelihoods, and increasing poverty, in turn making more people dependent on social protection mechanisms. At the same time, social protection can promote adaptive capacity, provide a stepping stone towards climate-resilient livelihoods (Wallis and Buckle, 2016; Food and Agriculture Organization (FAO) and Red Cross, 2019).

If these perspectives gain traction within the climate finance community, it may in the future become an important funding source for SRSP. There are calls for this, and these are gaining momentum in the run-up to the UN Climate Change Conference of the Parties (COP26), to be held in late 2021. For example, a blogpost for the International Institute of Environment and Development makes an argument that COVID-19 relief packages have used social protection programmes as vehicles to get finance directly to those in greatest need, and the big climate funders could do the same by investing in these programmes that reach out to the extreme poor. The blogpost calls for the GCF to include social protection as an adaptation response as one of its strategic priority areas (International Institute for Environment and Development (IIED), 2020). As an additional example, the Risk-Informed Early Action Partnership (REAP), which is a community of stakeholders working across the climate, humanitarian, and development sectors launched at the UN Climate Action Summit in September 2019, has positioned social protection/SRSP as critical to the ambition for making one billion people safer from disasters, and as a key delivery mechanism under Target 2 of the partnership – to ensure one billion more people are covered by financing and delivery mechanisms connected to effective early action plans, ensuring they can act ahead of predicted disasters and crises (REAP, 2021). In addition to supporting these calls, other practical ways the social protection community could increase its access to climate finance would be to adopt targeting approaches that purposefully include the climate vulnerable (even where there is overlap with poverty/food security targeting approaches).

## 5. Money-in options for shock responsive social protection: potential instruments

**Having looked at sources of funding in the previous section, this section explores several instruments available to governments for financing SRSP and provides a commentary on their suitability, given a range of shocks and their financial impacts.** We see ‘instruments’ in this context as types of finance, finance packages, or products specifically designed to provide money for certain risks.

**It is intentional that these have been reviewed in the second half of this paper, as too often systems design and development are dictated by the instruments available.** Instead, this paper recommends developing robust systems design, with risk analysis, targeting, and alignment considerations agreed first, and instrument considerations coming later.

**As with other DRF literature, there is some discussion around a strategic and ‘layered’ risk financing approach for SRSP,** where flood risk is covered by Instrument A and earthquake risk by Instrument B (known as ‘risk layering’), given that the frequency and severity of the shocks are different.

**However, in practice, there are limited examples of SRSP systems using more than one instrument to fund shocks.** Rather than working to perfect a sophisticated and layered risk financing structure to address every possible risk, SRSP systems should experiment with financing instruments and sources, tailoring approaches to deliver the agreed priorities and meet the needs of beneficiaries. This may mean implementing only one instrument in some contexts.

**These instruments can, of course, be put in place outside of the SRSP system, at the national government level, with some funds then being channelled through to scale up the social protection system.** The 'money-in' decision making would then need to consider how much money the SRSP system would need to scale, as well as the other needs the government wished to fund. This is particularly important if the social protection coverage is low in proportion to those at risk in a country. Using the example above of risk layering, an existing social protection system may be able to expand to cover most or all of those affected by a flood (if adequately prepared and capacitated, especially at sub-national levels); however, an earthquake could affect larger numbers of the population, including demographics not normally covered by social protection programmes, as well as impacting public assets and the private sector, overwhelming a social protection system.

**There are a limited number of institutions that offer risk finance instruments.** IFIs such as the World Bank have increased the range of instruments available to governments, including in fragile contexts, on the back of their IDA support, aimed at financing crisis response. Some of these include pre-arranged finance, such as CAT-DDOs, and the insurance-like Pandemic Emergency Financing Facility, which could be credible options for funding SRSP in the future. Likewise, there has been increased loaning and fund reallocation within governments and from international partners, as well as triggered humanitarian finance, following the impact of COVID-19.

**While some of the instruments available have performed well and were the only options possible when COVID-19 hit, others have proved slow or unpredictable,** and have in many instances ultimately led a reallocation of existing budgets, as opposed to enabling access to new forms of finance. Increased loaning and fund reallocation also raises further questions over the debt burden faced by countries who may then be forced to issue humanitarian appeals to address other shocks experienced simultaneously or consecutively (Development Initiatives, 2019). With the additional impact of COVID-19 pushing up borrowing in the poorest countries, the question of debt relief for countries in debt distress will once again become pressing (Hill *et al.*, 2020).

**In terms of conceptual framing, when considering financing approaches for SRSP, the instruments can be separated by:**

- Money planned and agreed before the shock occurs (**ex-ante**).
- Money arranged after the shock has occurred (**ex-post**).

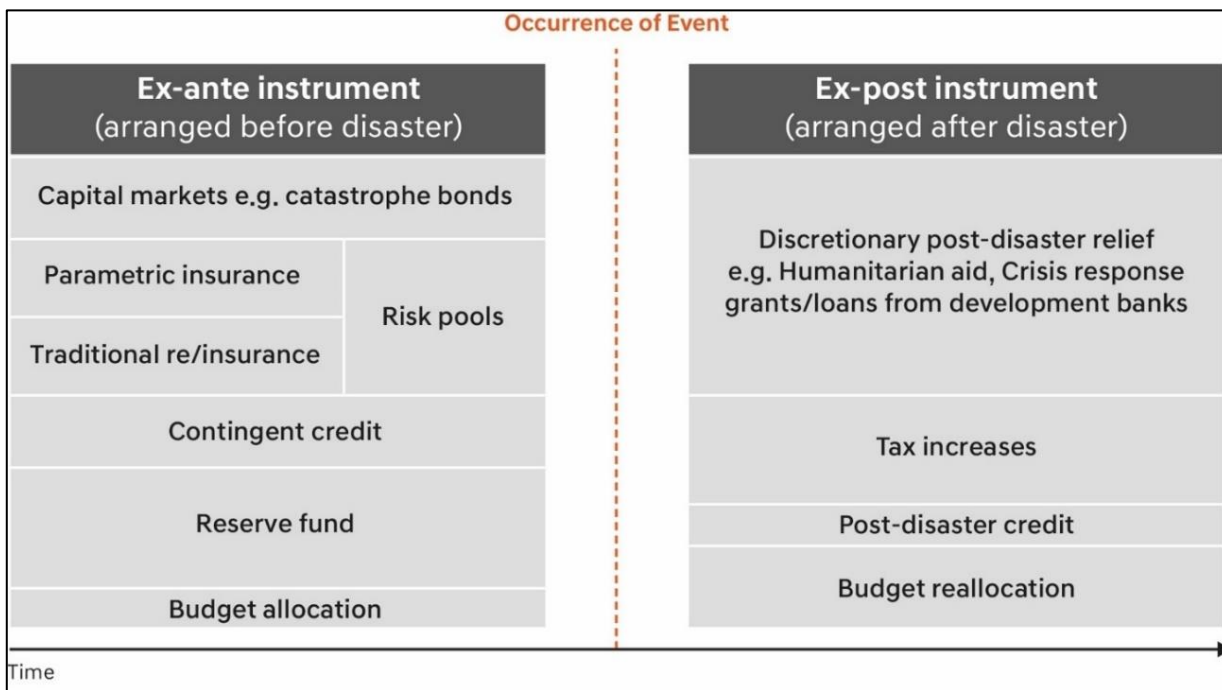
Of course, these distinctions can be blurred depending on the specific instrument, and its use and timing. It is also important to note that 'ex-ante' and 'ex-post' refer to when the financing is arranged, not when an instrument pays out (for instance, insurance is arranged in advance of a shock, and therefore is known as an 'ex-ante' instrument, even though it pays out after a shock).

**The tables in Section 5.1 and 5.2<sup>17</sup> explore several instruments available to governments and international actors for financing SRSP, broken down broadly by these two categories** (noting the de facto blurred lines). They also provide reflections on their suitability for SRSP given a range of shocks and their financial impacts, noting that a feature of any instrument can be an advantage or disadvantage depending on how it is used.

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<sup>17</sup> Tables adapted from Maher *et al.*, 2018.

**Figure 6: Ex-ante and ex-post risk financing instruments**



Source: Centre for Disaster Protection (forthcoming)

**Overall, there is no perfect solution for a country when considering how to strengthen its SRSP financing strategy and there are several factors to consider.** Rather than simply selecting an instrument, or purchasing one because it is offered, **these questions can instead be useful for system design:**

- How much money will the system need to respond to a specific shock?
- When will we need that money to be ready to put into the system, and when will beneficiaries need it?
- Who will pay for the shock response? Is this different to who pays for routine programming?

As these questions are being decided, those responsible for the decision making for SRSP should also consider the points below:

- **Context is king.** SRSP systems are not all designed to address the same needs or shocks, nor are they all targeted to meet every need of their beneficiaries. It is crucial that financing for SRSP is not copied like-for-like in different countries; instead, risk analysis, financial needs assessments, and political priorities should be determined before being constrained by instruments.
- **Financial instruments can be tailored, but the downstream delivery coordination and planning, as well as delivery channels, targeting approaches, systems, etc., have to be right.** While some government budget instrument types are quite restrictive, others, such as parametric insurance, are highly flexible to meet the needs of the SRSP system. Regardless of instrument, pre-planning and coordination ahead of a shock is essential. This means reviewing data needs and estimating the impact of shocks, establishing triggers (soft to hard) that are often required in order to release or request funds, developing action plans with roles and responsibilities, and then linking to pre-allocated finance. The fundamentals of delivery (the partners, modalities, targeting criteria, monitoring and evaluation, etc.) also have to be agreed and established, with capacity to scale.
- **Instruments can deliver more than just money.** For instance, while the primary objective for disaster risk finance instruments is to scale up with money agreed in advance of a shock, many instruments can incentivise better risk management, improve systems strengthening for SRSP, enhance coordinated contingency planning and response, encourage better risk ownership and management, and institutionalise stronger fiduciary discipline.
- **Instruments can be financed from different sectoral sources and actors but are predicated on a range of decision points.** When introducing such instruments, governments and donors have an array of considerations, including fiscal constraints, political will, a sense of opportunity cost, and reputational risk. How much governments agree to dedicate towards such mechanisms will depend on several factors, but fiscal space inevitably plays a large role. The opportunity costs of creating fiscal buffers (e.g. paying off



debts in advance of a shock so they can borrow more when the event happens) can be significant, especially when fiscal space is scarce, as building buffers will imply forgoing other high-return expenditures geared towards developing the economy and increasing its long-term growth rate. Resolving this trade-off will depend on the relative magnitude of the opportunity costs in relation to the benefits provided by the buffers.

- **Risk ownership needs to be driven at different levels of government.** This relates to risk ownership and where the financing responsibility will sit; what is needed is a body empowered to put instruments in place. Depending on the country, most of the instruments discussed below could be adaptable to any level of government, although not all would be permissible (given regulatory barriers), feasible, or suitable.<sup>18</sup> Typically, as you move down through the layers of government, Public Financial Management (PFM) systems and transparency weakens.<sup>19</sup> The key is to drive risk ownership, at whichever level of government is best placed to respond to the shock, through the financing instrument, creating robust government plans and reducing the reliance on humanitarian financing approaches, which may be unreliable. It follows that if there is no government in place to own the risk, the government cannot take responsibility for financing that risk (this is especially important to consider in fragile contexts).

## 5.1 Ex-ante instruments

**These are instruments arranged in advance of a shock and which pay out once the shock has occurred (if not before; see forecasts).** Depending on the instrument, they also consider the financial cost associated with a shock, identify who will be responsible for implementing the response once a shock occurs, and consider both money-in financing and money-out systems.

### 5.1.1 Instrument type: contingency / reserve funds

#### Description:

Contingency funds (or a dedicated disaster fund) refer to funds set aside, ex-ante, as a financial buffer. These vary in form and the ways in which they can be set up. The most basic, a contingency budget, is an often small but flexible pot of funds most governments have available to draw upon in the annual budget in order to meet unanticipated need. The government has the authority to spend this flexible pot on additional financing needs with the fiscal year, such as salary increases, maintenance needs, or natural disaster response, dependent on the PFM law. Governments can opt to set a legal limit on the size, normally a share of total expenditure, and some earmark a share of the overall contingency budget for natural disasters (e.g. Indonesia). Some countries have contingency lines for specific programmes within the budget, as is the case with the Productive Safety Net Programme in Ethiopia.

A natural disaster fund goes further: it is a dedicated financing source for natural disasters determined annually within the budget, in some cases with the amount of funding prescribed in law. Such funds have restrictive rules regarding how resources can be used, but upon the declaration of a qualifying disaster can typically be used without the need to seek additional legislative authority. Funds can, however, be used for any stage of the disaster cycle, depending on how they are established. They can also sit at any level of government, but require the associated legal framework. Some countries have disaster funds whereby the funds are, to a degree, pre-allocated, so that when a disaster occurs, it is already known who will respond; others keep the pot unallocated to maintain flexibility.

#### Country examples:

- **Philippines:** The National Disaster Risk Reduction and Management Fund is financed through an allocation in the annual budget, the value of which is derived from a recommendation of the National Disaster Risk Reduction and Management Council, proposed by the Department of Budget Management, and ultimately approved by the President as part of the national budget. Recipients of the Fund include government spending agencies, as well as local governments and community organisations. The Fund is structured into a series of sub-funds, which is a means of ensuring an appropriate balance of spending (between preparedness, relief, reconstruction, and rehabilitation) and of strengthening oversight. The structure is mirrored at the local government level through the

<sup>18</sup> For instance, the regulatory environment, such as sanctions or having no pre-existing insurance law, would mean that certain countries would not be able to access the markets required for these instruments.

<sup>19</sup> PFM systems at the sub-national level are typically less developed, since they have typically been established for less time than the national structures, and have received less funding from donors to enhance reforms with more of a focus on the national level. With less money at their disposal, they are often subject to less scrutiny.

Local Disaster Risk Reduction and Management Funds, where there is a legally prescribed budget allocation annually (5% of local government revenues).

- Peru: There are four reserve funds in Peru – the contingency reserve, the Fondo para Intervenciones ante la Ocurrencia de Desastres Naturales ('Natural Disaster Response Fund'), the Fondo de Promoción a la Inversión Pública Regional y Local ('promotion fund for regional and local public investment'), and the stabilisation fund. The Fondo, the main fund, finances projects for mitigation, response capacity, rehabilitation and reconstruction. Additionally, it finances the reinforcement of essential public services corresponding to the health, education, and sanitation sectors that could be affected by the occurrence of natural disasters. For post-disaster rehabilitation, the Fondo is authorised to finance, among others, actions in the sectors of health, education, sanitation, irrigation, road infrastructure, and flood protection services.

#### Advantages

- Fast and flexible: money is in theory available immediately (and before disasters hit).
- Encourages forward planning: there are action plans on how money will be allocated and spent (disaster fund only, not contingency funds).
- Relatively cheap, particularly for frequent shocks.
- Approach has been used in many contexts; thus, experience is available for countries to build upon.
- Governments can retain control over their use (as opposed to other forms of external/international finance).
- High potential to support early action measures.

#### Disadvantages

- Potentially high opportunity cost of funds, given higher rates of return on other government investments, often making them harder to defend, particularly in countries with limited fiscal space.
- Requires fiscal discipline to ensure funds are used for their intended purpose (and not prematurely raided for non-qualifying expenditures). This limits their use in low-income/ Fragile and Conflict Affected Situations.
- Retains all of the risk, meaning that the entire cost is borne by the holder of the fund.
- Funds are often (but not always) disbursed on verification of the hazard; when this is the case, funds are used for response and recovery, rather than for anticipatory purposes.
- Triggers can be difficult to develop/enforce and often are not based on objective criteria.
- Money can be used up if funds are not purely for disasters and/or there is more than one disaster during the fiscal period.

#### Best suited:

**Low risk layer, e.g. frequent low-impact events such as annual flooding or localised drought or conflict.**

#### Key considerations for SRSP

##### Contingency budget:

- Deciding whether a share should be earmarked for disasters (and therefore guaranteed should the event occur), and/or channelled through social protection, means less flexibility for the government to use the contingency budget at its discretion. For example, it may be more politically advantageous to use the budget in geographic areas where the SRSP system does not cover, or another sector or budget line entirely.
- Placing money in a contingency budget means that governments can spend funds at their own discretion without parliament checking, which (if large enough) can undermine fiscal discipline. There becomes a point at which this mechanism becomes too opaque, despite the flexibility it lends. Ex-post audits can be conducted, but this not always mandatory (or not always done) in many countries.

##### Dedicated disaster funds:

- Dedicated disaster funds typically require strong PFM discipline to ensure that funds are spent as intended, with a high degree of transparency. Several issues arise when establishing such funds, including but not limited to: how to manage unused funds; who can spend the funds; how procurement will be managed; and whether idle fund should be invested. Regardless of the choices made, good practice dictates the importance of funds remaining on-budget and that the standard transparency requirements, dictated in PFM law, remain in place (as for the use of any public funds) – this is not always the case.
- Deciding who will manage such a funds (and who will have access to the funds) is an important consideration and will likely depend on a variety of factors (e.g. level of decentralisation, power-sharing arrangements, the ability to create new entities, etc.)

## Further reading and resources

- Department of Budget Management (Government of the Philippines), 2017. Technical notes on the 2017 Proposed National Budget, [link](#).
- Department of Budget Management (Government of the Philippines), 2018. Calamity and Quick Response Funds, [link](#).
- Government of the Philippines, 2012. National Disaster Risk Reduction and Management Plan 2011–2028. World Bank, 2016. [link](#).
- Peru: A comprehensive strategy for financial protection against natural disasters, [link](#).
- IMF, 2018. How to Manage the Fiscal Costs of Natural Disasters, [link](#).

## 5.1.2 Instrument type: triggered contingent finance – humanitarian pooled funds

### Description:

Triggered contingent funding, similar to parametric insurance, uses objective triggers and allows governments and other actors to receive funding from a pre-arranged fund that can be released in advance of the shock to incentivise risk reduction activities (early action financing), or based on a forecasted event (forecast-based financing), or when the shock hits. This financing can be divided into two types: grants (with no expectation to be repaid); and loans (see next box on triggered finance for loans). This box focuses on the former and their use in humanitarian pooled funds, the next box on the latter, as offered through IFIs to governments.

Humanitarian pooled funds allow governments and private donors to pool their grant contributions into common, un-earmarked funds to deliver assistance in emergencies. There are two types of pooled funds: global (such as UN OCHA's Central Emergency Response Fund (CERF), or the Red Cross Red Crescent Disaster Relief Emergency Fund (DREF)), which can cover emergencies anywhere in the world; and CBPFs such as the 18 managed by the UN, which support the highest-priority projects set out in Humanitarian Response Plans. While they represent only a relatively small portion of global humanitarian funding (between 5% and 6.6% of total international humanitarian assistance since 2010 (Development Initiatives, 2020)), they are important in supporting timely delivery and improving the overall coordination of response. In total, the UN's CERF and CBPFs allotted over US\$ 1.6 billion in assistance in 2020.

A growing area of investment for humanitarian pooled funds is anticipatory action. As noted in Section 5, anticipatory action broadly includes interrelated investments in preparedness, surveillance, early warning early action, and forecast-based action (Levine *et al.*, 2020). Global humanitarian pooled funds such as the IFRC's DREF and, increasingly, the CERF are allotting triggered contingent financing to anticipatory actions at country level. This approach works to overcome the delays inherent in ex-post humanitarian funding and is often linked to pre-agreed response plans (the Red Cross has called them 'Early Action Protocols') and delivery channels prior to a shock. While currently in place for more frequent, low-severity shocks, with more experimentation large humanitarian funds could develop triggers for different types of shock.

### Country examples:

#### Early action:

- In 2017, CERF was one of the first responders in 2017 to warning signs of famine in northeast Nigeria, South Sudan, and Somalia, and by end of August 2017 had released US\$ 106 million to support critical response and life-saving activities prioritised by the humanitarian partners on the ground. CERF also provided a US\$ 22 million loan to the FAO to bridge a cash flow shortfall, which threatened the FAO's ability to continue its drought response in Somalia. With this timely and highly cost-effective support, the FAO was able to scale up life-saving activities and launch an unprecedented campaign to avert famine.
- In 2018, CERF worked closely with field colleagues to analyse drought and food security forecasts in the Sahel and advised Resident and Humanitarian Coordinators in the highest risk countries on how to access CERF funding. A total of US\$ 30 million was allocated to Mauritania, Mali, Burkina Faso, and Chad between March and June 2018. This enabled partners to bolster communities' resilience through animal health and cash transfers to safeguard livelihoods.

#### Anticipatory action:

- CERF is currently piloting this approach in five pilot countries (Somalia, Chad, Ethiopia, and Malawi (drought), and Bangladesh (flooding)).

- The IFRC's DREF currently has 38 Early Action Protocols at country level approved or under development, and recently undertook analysis to understand how to expand the number of Early Action Protocols which could be put in place with better financial management of the pool.<sup>20</sup>

Advantages	Disadvantages
<ul style="list-style-type: none"> <li>• Funding can be released before the impacts of a shock are felt, or before a shock turns into a disaster.</li> <li>• Flexible: they can respond to need and can scale quickly.</li> <li>• Funding released based on objective preconditions and triggers, and with contingency plans in place so response actions are implemented quickly with the potential to coordinate across response actors.</li> <li>• Pools resources from different donors, reducing overheads, earmarking, and bureaucracy, and increasing flexibility and timeliness.</li> <li>• Increasingly integrating DRF and anticipatory action principles.</li> <li>• When used for anticipatory action, less costly than traditional humanitarian response.</li> <li>• Does not have to be repaid, helping countries avoid further indebtedness and longer-term economic downturns.</li> <li>• Not subject to some of the donor preconditions of bilateral humanitarian aid.</li> <li>• Helps support underfunded and forgotten crises and activities.</li> </ul>	<ul style="list-style-type: none"> <li>• The majority of funds are allocated due to a conventional process linked to appeals which come after a shock has become a crisis.</li> <li>• Funding released based on objective preconditions and triggers, which is not always appreciated by those who like to retain decision making control.</li> <li>• Not mainstreamed within government planning processes, therefore limiting the ability to plan the response and recovery, as they in practice have no or limited control over the timing, the amount of funds received, or what the funds can be used for (despite pre-approved contingency planning).</li> <li>• Typically used to supplement humanitarian agencies as a pre-cursor to regular response financing; more coordination is needed to align with government-led systems.</li> <li>• Can be costly (in comparison to using pre-established systems).</li> <li>• Issues of 'acting in vain' (triggering support for a shock that does not materialise as forecast).</li> <li>• Risk of funds not being released if trigger is incorrectly set.</li> <li>• Requires a high degree of technical input and investment (especially at the outset).</li> <li>• Triggers are not always perceived as reliable (or are not always entirely objective).</li> <li>• The ability to connect to social protection programmes such as social assistance is not yet known (untested).</li> <li>• Upfront costs of developing triggers and risk analysis.</li> </ul>

**Best suited:**  
**Frequent, low-severity shocks, or those that exceed the capacity of national actors. Also, as a pre-cursor to larger shock responsive efforts.**

### Key considerations for SRSP

- Triggered contingent financing is growing in use with many humanitarian organisations undertaking pilots with strong outcomes. Much of this experimentation is being done outside SRSP systems. The next step will be taking this approach to scale and using SRSP systems as 'money-out' conduits to avoid potential duplication in beneficiaries reached or systems utilised.
- Typically used to better automatise humanitarian funding; however, could be adopted by government for funding efficiencies. It would then become a risk retention instrument.
- Can easily be combined with other financing instruments which may be better suited to more severe shocks with the key being to encourage coordination across triggers and instruments.

### Further reading and resources

- Use of the International Federation of the Red Cross Red Crescent's DREF for forecast-based financing, [link](#).
- CERF's plans to pilot anticipatory action measures using DRF triggers, [link](#).

<sup>20</sup> See link for more details on the DREF and Early Action Protocols: [www.disasterprotection.org/financing-forecast-based-early-action-protocols](http://www.disasterprotection.org/financing-forecast-based-early-action-protocols)

## Box 7: Proposed re-structuring of CERF for anticipatory action

Based on a systemic review and ongoing pilots in five countries, OCHA is currently reviewing the structure of CERF to integrate an anticipatory action approach under its rapid response window, in addition to the pre-existing early response and regular response approaches that CERF already supports. As OCHA notes, although an anticipatory approach would be housed under the CERF rapid response window, it will represent a distinct way of accessing CERF funding, as compared with early response and response. Funding requests will be based on forecasts of humanitarian need, with thresholds for action and implementation strategies agreed in advance of a shock and in line with national and agency contingency plans.



Sources: CERF and Anticipatory Action (2019) - [link](#), CERF - Anticipatory Action Update (2020) - [link](#)

### 5.1.3 Instrument type: triggered contingent finance – credit lines

#### Description:

Lines of contingent credit are pre-arranged loans which can be drawn down rapidly after pre-identified shocks. The terms of the line of credit are agreed beforehand to avoid lengthy negotiations and delays in the midst of a crisis. Arrangements are contract specific, but both hard (e.g. the intensity of a hurricane) and soft triggers (e.g. the declaration of an emergency) can be and are used. In general, contingent credit lines have approval criteria in place which generally cover an adequate macroeconomic framework, and a DRM policy or programme in preparation or in place. Some credit lines will require prior agreement on what funds can be used for – for example, the relevant programmes that will be protected during the shock. The funds can be drawn down at any point once the trigger event(s) materialises. Contingency credit lines have typically been offered by international organisations such as the World Bank (CAT-DDO), the Inter-American Development Bank (Contingent Credit Facility for Natural Disaster Emergencies), the IMF, and the Japan International Cooperation Agency (Stand-by Emergency Credit for Urgent Recovery); they can also be offered by commercial lenders.

#### Country examples:

- The World Bank offer IDA CAT-DDOs to all IDA-eligible countries if they meet the eligibility criteria: (i) the existence of an adequate macroeconomic policy; and (ii) the preparation, or existence, of a satisfactory DRM programme that addresses natural disasters. Countries are able to borrow up to a limit of US\$ 250 million or 0.5% of GDP (whichever is lower). Prior to introducing such mechanisms, countries typically need to meet around six prior actions (e.g. DRF strategy, DRM reform, etc.). Triggers are typically associated with the country declaring a state of emergency, and funds can be received within 72 hours. Kenya agreed the World Bank's first IDA CAT-DDO in 2018, totalling US\$ 200 million. The CAT-DDO was introduced alongside a World Bank policy programme which supports the Government of Kenya to achieve set targets which centre around strengthen resilience to climate and disaster risk in the urban and water sectors, mainstreaming DRM into development planning and public investment, and increasing the transparency of government interventions for climate adaptation and mitigation. The CAT-DDO has been fully disbursed; in the first instance, US\$ 70 million was disbursed to support severe flooding in 2019, and a further US\$ 130 million was drawn down to support the COVID-19 response.
- Cook Islands: In 2016, the Asian Development Bank provided a policy-based loan of NZ\$ 13.95 million (about US\$ 10 million) from its ordinary capital resources to fund a contingent disaster financing facility in the Cook Islands. Eligibility to access the policy-based loan is linked to the achievement of prior and continuing actions to strengthen disaster resilience. The loan funds were initially available for a three-year period (and subsequently extended to a second phase in November 2019) and are drawable as needed if a state of disaster is declared by the government, as defined by its 2007 Disaster Risk Management Act. The funds can be used flexibly to support the short-term post-disaster activities that the government deems necessary. Only a single withdrawal may be requested per disaster event, and the request should be received by the Asian Development Bank within 90 days



of the declaration of a state of disaster or emergency. The country has not experienced a major disaster to trigger a disbursement of the loan; it therefore remains unknown how long disbursement would take.

Advantages	Disadvantages
<ul style="list-style-type: none"> <li>• Can be cheap, particularly for mid-frequency shocks. Contingent lines of credit are typically offered by development banks, often at below-market-rates.</li> <li>• Quick: the World Bank CAT-DDOs typically disburse within two to three days of the request being made.</li> <li>• Encourages forward planning (i.e. action plans on who and how money will be allocated and spent).</li> <li>• Can incentivise proactive actions to reduce risk, particularly if linked to the country meeting certain DRM and resilience conditions, including scalable social protection systems.</li> </ul>	<ul style="list-style-type: none"> <li>• Adds to a country's debt burden; the fund must be repaid and therefore reduces the future fiscal space.</li> <li>• Access is generally dependent on the current stock of public debt, macro-fiscal conditions, and the ability to access international credit markets; this may rule out a number of at-risk countries.</li> <li>• Current low (but growing) uptake of CAT-DDOs. If a country's window to credit is fixed in size, countries are likely to prefer direct credit over contingent credit (since it is guaranteed).</li> <li>• As credit lines are agreed in advance, they will be subject to greater political economy constraints compared to ex-post credit. For instance, ex-ante credit will typically need to be approved by a national parliament, and if the country is suffering debt problems, many may be against these types of arrangements. During a disaster, many of the normal processes are bypassed in order to respond, creating potentially less scrutiny.</li> <li>• Conditions are imposed for some contingent credit lines. While conditions are generally linked to DRM and improving resilience (often through the support of a programme), they do act as a barrier to some countries in terms of access. For example, prior actions for such instruments may be that the country needs to introduce a DRF strategy or start to track climate and disaster-related expenditure; these are often complex reforms for governments to introduce, even with support.</li> </ul>

**Best suited:**

**Mid-risk layer, e.g. higher magnitude events, such as widespread flooding or hurricane, which occur less frequently but cause damage that exhausts the resources of national contingencies.**

**Key considerations for SRSP**

- Availability of such funds. COVID-19 has demonstrated that they can be deployed extremely quickly, but COVID-19 is unprecedented and a similar level of borrowing is unlikely to be made available (at such a pace) for natural disasters at a national level.
- Funds need to enter into the PFM system, not just the SRSP system, requiring a country's PFM system to flex to allow this sudden inflow of cash. The worst-case scenario would be money sitting in the national treasury but delays in money being transferred to the SRSP oversight ministry.
- Limited transparency requirements and some discretion on where the money is used. There is no requirement for them to be used to prioritise poor and vulnerable people, nor those impacted by shocks. Donors do not track the use of funds, nor require government to do so (though internal PFM systems may require this).

**Further reading and resources**

- Clarke, D., and O. Mahul, 2011. Disaster Risk Financing and Contingent Credit: A Dynamic Analysis, [link](#).
- Office of Evaluation and Oversight, 2016. Contingency Lending Instruments, [link](#).
- World Bank, 2018. IDA Catastrophe Deferred Drawdown, [link](#).
- World Bank, 2018. Disaster Risk Management Development Policy Credit with a Catastrophe Deferred Drawdown Option (CAT-DDO) (P161562), [link](#).
- World Bank, 2020. Faster Access to Better Financing for Emergency Response and Resilience in Kenya, [link](#).

## 5.1.4 Instrument type: parametric risk transfer instruments

### Description:

Parametric risk transfer solutions are pre-agreed financing arrangements where a third party agrees to assume the costs associated with the occurrence of a certain event. Insurance is a classic example, with an insurance company agreeing against payment ('premiums') to disburse a certain amount of money (e.g. the cost of a lost harvest) in the event of a pre-agreed occurrence (e.g. a drought). Other examples of risk transfer solutions include catastrophe bonds and other financial derivatives (e.g. index-based livestock insurance). Coverage through risk transfer solutions can be purchased by individual persons ('micro-level'), groups ('meso-level'), or governments ('macro-level'). Of these, in the context of SRSP, where social protection systems are usually operated and paid for by national governments, macro-level solutions tend to be most relevant. However, so far there is limited experience with using risk transfer for social protection purposes. It should be noted that risk transfer solutions, compared to other financing options, can be expensive. They tend to become cost-effective only for the least frequent, most severe risks, such as catastrophic droughts, floods, or storms.

### Country examples:

- Mexico was the first country in 2003 to introduce macro-level crop and livestock index insurance products (under the Component for the Attention of Natural Disasters programme). Through this, regional governments purchase insurance against natural disasters on behalf of small and marginal producers. When drought conditions are detected in a particular area, the respective regional government receives an insurance pay-out, which it then distributes to the producers affected (World Bank, 2012).
- ARC: This is a sovereign risk pool owned by African Union member states that has been active since 2014. Member states can purchase mutual insurance cover from ARC. Initially, offered insurance products covered only drought, but the portfolio is growing, with e.g. tropical cyclones and floods being added to the risks covered. In order to be eligible, the purchasing member state must present a contingency plan that outlines how it would use a potential pay-out. The contingency plan should cover emergency response actions for the most vulnerable populations affected by the shock and needs to be approved by an ARC technical committee. Many member states that have purchased ARC insurance have included the scale-up of safety nets as one of the uses of a potential pay-out in their contingency plans. As per their respective plans, in the event of an ARC pay-out, these countries would channel the resources received to affected populations via existing national social safety nets. However, evidence as to whether triggered funding has actually been channelled to social safety nets through ARC contingency plans is still lacking.
- Index-based livestock insurance in Kenya and Ethiopia: the Government of Kenya (through the Kenya Livestock Insurance Program) and the Ethiopian regional Government of the Somali Region (the Satellite Index Insurance for Pastoralists in Ethiopia programme, with support from the WFP) have purchased drought insurance cover from local companies for SRSP purposes. Drought conditions in pastoralist rangeland areas are monitored by satellite. When a drought is detected, pre-registered vulnerable pastoralists in the affected area receive a pay-out from the insurance company into their mobile money bank account (Fava et al., 2020).

### Advantages

- Can be cheaper than other financing alternatives, particularly for extreme shocks as the market is competitive.
- Parametric insurance can pay out very quickly, in days or weeks. Because it is triggered by the specific event, there is no need to assess impact or undertake damage observation. It allows implementers to plan, and in the best example, incentivises joint-planning e.g. ARC Replica.<sup>21</sup>
- Supports fiscal discipline – funds cannot be 'raided' early.

### Disadvantages

- Can be expensive for frequent shocks.
- Can be vulnerable to political criticism and 'regret' if no pay-out.
- Usually aligned to financial impact of shock (i.e. how much a government needs to re-build), rather than driven by the needs of beneficiaries or poverty reduction.
- Requires risk literacy and capacity to ensure value for money. Some countries have had problems with the way triggers or the price of premiums are set.
- Trade-off between the cost of premiums and the frequency or scale of pay-out.

<sup>21</sup> ARC Replica offers international organisations the opportunity to purchase coverage that replicates the insurance policy purchased by a national government through ARC. This extends coverage to additional households, reached through government or international partner programmes, thereby also enabling humanitarian actors to access market risk capital to cover costs related to humanitarian action in specific countries (Hobson, 2020).

- Helps countries to transfer risk off their balance sheet, shifting some of the burden of sudden and heavy losses from a severe event to other actors.
- Can clarify how risk is owned, and therefore who is responsible for what risk.

**Best suited:**

**High-severity, less frequent events, e.g. shocks occurring less than every five to 10 years, such as severe droughts, hurricanes, or earthquakes.**

**Key considerations for SRSP**

- Parametric insurance can act as commitment device as decisions on who will pay for what after a shock is pre-arranged, with the SRSP delivering the 'money-out' system to delivery funds quickly to beneficiaries.
- Existing risk pools, such as ARC, show that there is an appetite from the private sector to provide affordable DRF for at-risk countries.
- Not all insurance is provided by the private market. Mutual and co-operative insurance options provide credible options to manage risk and would be in scope for countries to buy in order to provide additional financing for specific risks, which could then be channelled through SRSP systems.
- Parametric insurance, as a standalone product, does not always incentivise good risk management. Conversely, indemnity-based insurance, where you must prove loss or harm to receive a pay-out, does encourage steps to manage risk before it is transferred (e.g. locking your car when it is unattended reduces the likelihood of it being stolen). However, there are several challenges surrounding implementing indemnity-based insurance in countries that lack strong insurance regulations and where evaluating losses is challenging. Both options would be available to SRSP systems, and parametric products can build trust in insurance to implement indemnity schemes later.
- There is a significant appetite from donors to support governments buying parametric insurance products to support SRSP, with a growing body of evidence of how it can be done effectively to support development outcomes. However, there is very limited evidence of parametric insurance being effectively linked to and channelled through SRSP.

**Further reading and resources**

- Swiss Re, 2021. What is parametric insurance? [link](#).
- Clarke & Dercon, 2019. Beyond Banking: Crisis Risk Finance And Development Insurance In IDA19 - Discussion Paper. [link](#).
- World Bank, 2016. What Is Disaster Risk Finance (DRF)? [link](#).
- World Bank, 2017. Index insurance is having a development impact where it's needed most. [link](#).
- The African Risk Capacity, 2021. [link](#)

**5.1.5 Instrument type: catastrophe bonds**

**Description:**

Catastrophe bonds (cat bonds) are financing instruments that transfer catastrophe and natural disaster risks from a sponsor (the insurance buyer) to global capital markets. They involve insurance securitisation – the transfer of a specific set of underwriting risks that cedents such as insurers or governments (and now humanitarian agencies such as the Danish Red Cross) are exposed to through the creation and issuance of risk-linked financial securities.

Capital markets investors take on the risk of a catastrophic event happening in the future (usually within a three-to-five-year timeframe), in exchange for a return on investment that they deem suitable for such a risk level. Simply put, cat bonds equate to a financial bet on whether an extreme climate-related event such as a severe drought, earthquake, or hurricane will happen or not. If this event does not occur, the investors in the cat bond receive their investment capital back, plus the interest paid to them by the buyer for holding the risk during the life of the bond. If the event does occur, they can lose up to all of their money. Hence, the interest rates paid to investors tend to be high to compensate for this.

Originally introduced in the 1990s, total issuance since surpassed US\$ 100 billion at the beginning of 2020. Cat bonds generally have higher fixed costs associated with them than insurance; as a result, they are more suitable for the transfer of significant risks that have the potential to materially impact the financial stability of the sponsor.

The average commercial cat bond size ranges from US\$ 50 million to US\$ 300 million. They are not commonly used to cover smaller losses from more frequently occurring shocks, for example annual losses due to cyclical floods.

**Country examples:**

- After many years in the making the Government of The Philippines introduced a US\$ 225 million cat bond to protect against earthquake and tropical cyclones. It was issued by the World Bank's International Bank for Reconstruction and Development (IBRD) in November 2019 and was the first cat bond to be sponsored by an Asian sovereign, plus the first cat bond listed on the Singapore Exchange. This DRF instrument provides timely post-disaster financing for the government's emergency responses to these two types of hazard if the earthquake or tropical cyclone breaches the modelled loss triggers, i.e. if projected impacts caused by the cyclone or earthquake amount to more than the pre-agreed threshold. The cat bond sits alongside a number of other financing plans that the Government of the Philippines has put in place to comprehensively manage disasters under its National Disaster Risk Reduction and Management Plan 2011–2028.
- The world's first cat bond covering volcanic eruption risk has recently been brought to market (March 2021) in a private placement worth US\$ 3 million, sponsored by the Danish Red Cross. The cat bond covers 10 volcanoes across three continents where an eruption poses a humanitarian threat to 700,000 or more people living within a 60 km radius of each volcano. The trigger for pay-outs has been designed by Mitiga Solutions, with expertise in predicting natural hazards, and uses an innovative model to anticipate the trajectory of an ash cloud using prevailing winds. In this way, immediate humanitarian needs after the eruption occurs can be assessed more accurately and potential impacts can be predicted more effectively. Timely humanitarian funding is released when the cat bond triggers (the parametric trigger has three ash plume thresholds), and can therefore be used in a more targeted and impactful way. This is innovative for a number of reasons: specific geological risk is covered across multiple countries (usually, international cat bonds cover insurers' portfolios); it is unusual for a humanitarian agency such as the Danish Red Cross to be the sponsoring entity; the structuring agent Replexus has used its private Insurance-Linked Securities (ILS) blockchain platform to settle the cat bond securities, thereby reducing the settlement costs associated with 'traditional' cat bonds. This blockchain platform also allows investors to hold the securities on their own computer servers, further reducing costs.

Advantages	Disadvantages
<ul style="list-style-type: none"> <li>• Can be a cost-effective way of managing large-scale shocks at sovereign level in developing countries, by transferring some catastrophic risk off country balance sheets.</li> <li>• If triggers are parametric in nature and based on pre-agreed thresholds (for example, earthquake magnitude or wind speed), they can pay out quickly to the sponsoring entity in order to fund timely and effective disaster responses.</li> <li>• Cat bonds can support budgetary pre-planning and fiscal discipline, plus complement other aspects of a sponsor's comprehensive risk management programme (such as long-term disaster risk reduction).</li> <li>• They offer multi-year funding (a typical duration of three to five years), thereby increasing the visibility of financing and supporting longer-term planning than annual insurance policies.</li> <li>• These instruments can prompt clarification about who owns what risk and how exactly sponsors will use the proceeds to respond to disasters and protect their vulnerable populations and economic assets.</li> </ul>	<ul style="list-style-type: none"> <li>• Higher fixed costs associated with the structuring and issuance can make them expensive for frequent shocks.</li> <li>• Trade-off between model customisation to align with specific risks and higher development and transaction costs involved.</li> <li>• There is always a risk that modelled loss using parametric triggers does not mirror the realities of a disaster on the ground, thereby exposing cat bond stakeholders to criticism and public distrust.</li> <li>• Due to their use at the sovereign level to manage the mainly financial impacts of disasters, they tend to focus on and enable the 'money-in' side of a transaction, i.e. access to finance. They do not incentivise accountability for the 'money-out' side, i.e. ensuring that funds are disbursed to those most vulnerable people and communities affected disproportionately by disasters.</li> <li>• Complex structuring requires a level of financial and risk literacy that enables thorough cost-benefit analysis by sponsors. When analysed in isolation and without comprehensive understanding, issuance can happen for the wrong reasons and systemic problems in disaster response may not end up being solved.</li> </ul>

**Best suited:**

**High-severity, low-frequency events with economic and human impacts that would otherwise overwhelm a sponsor's capacity to respond to shocks occurring typically within a five-year period, such as earthquakes, hurricanes, or tropical cyclones. Given the high transaction costs (and effort), catastrophe**

**bonds are best suited where a significant amount of money (often hundreds of millions) is required if the event occurs.**

### Key considerations for SRSP

- Cat bonds can be useful tools in managing disaster risk, where the potential magnitude of a future catastrophe cannot be borne by the sponsoring entity, be that a national government, insurance company, or humanitarian agency. They have not been used to fund SRSP since they are tightly regulated, sophisticated insurance instruments which require substantial upfront investment.
- Practically, a cat bond would most likely be a sovereign-level instrument whereby some of the proceeds would be used to surge the SRSP system, especially if the system has low population coverage because typically the transaction size is in the hundreds of millions.
- Triggers for the release of funds can be parametric in nature and can be designed to meet the specific financing needs and disaster relief trajectory of single or multiple events affecting a particular country or region.
- Pre-arranged financing like this can create a clear line of sight to the cashflows involved. If a triggering event happens, cashflows can be used for quicker and often anticipatory responses to disasters, in order to save more lives. It does not, however, guarantee accountability for and transparency of cashflows to vulnerable people.
- There is significant investor appetite for cat bonds that represent diversification of investors' overall portfolios risk levels; however, their suitability as a DRF tool should be guided by several factors that will be unique to every country or a sponsor's own requirements. These can include trade-offs between higher transaction costs and longer time horizons than other financing options, or the often lengthy timeframes to bring cat bonds to market and their potential positive impact on the delivery of long-term policy and development agendas.
- With the purpose and structure of cat bonds currently evolving, there is future scope to integrate and incentivise other critical aspects of comprehensive DRM, for example increased investment in SRSP delivery systems, risk reduction activities, and resilience building, but this is resource intensive and requires collaboration across many parts of government.

### Further reading and resources

- Artemis. What is a catastrophe bond, [link](#).
- Wright, A., 2020. Adaptation finance takes off as Catastrophe Bonds top \$100 billion, Global Center on Adaptation, [link](#).
- Carayannopoulos, P., Kovacs, P., and Leadbetter, D., 2003. Insurance Securitization Catastrophic event exposure and the role of insurance linked securities in addressing risk, [link](#).
- Sheehan, M., 2020. Total cat bond issuance surpasses \$100bn: Aon Securities, [link](#).
- Evans, S., 2021. First volcanic eruption cat bond issued for the Danish Red Cross, [link](#).
- Sheehan, M., 2021. Danish Red Cross launches first volcano cat bond, [link](#).
- Artemis Catastrophe Bond and Insurance-linked Securities Deal Directory, [link](#).
- Evans, S., 2020. Philippines Gov requests cat bond loss calculation for typhoon Goni, [link](#).
- REbound, 2017. A guide for public sector resilience bond sponsorship, [link](#).

## 5.2 Ex-post instruments

These are instruments and financing approaches that are arranged and agreed once a shock has occurred. Depending on the instrument or financing approach and the scale of the shock, they can be slow to mobilise and insufficient in size to meet the needs of those affected. Typically, they do not take into account money-in and money-out considerations.

### 5.2.1 Instrument type: budget reallocations

#### Description:

A common solution for cash-strapped governments in the midst of a crisis is to reconfigure the state budget, diverting existing funds away from public services and ongoing public projects and towards disaster response



efforts. The process for reconfiguring the budget differs across countries, with different rules on how far ministries can change the composition of spending without seeking approval from the ministry of finance and subsequently the legislature. In the first instance, virements are utilised – in-year movements of budgetary resources between line ministries, programmes, policy areas, expenditure categories, or line items. Every country will have different rules for how and whether these movements happen and how large they can be, yet across all countries, virements do not require parliamentary approval (if they are within the pre-agreed limits and do not fundamentally change the composition of expenditure appropriated by the legislature) and cannot increase the overall ceiling.

Once a country has exhausted the limits of its virement policy, a government may seek to make larger reallocations which will require a supplementary budget in most countries – an additional budget which overrides the original budget. These typically require legislative approval; therefore, the only limits imposed in term of the scale of the reallocations are linked largely to the power of the legislature. If a supplementary budget increases the overall ceiling, additional financing instruments will be required to finance the additional spending: budget reallocations cannot cover the additional spending.

More recently, some donors have established their own financing procedures during disasters, meaning that they can reallocate their own funding within and across programmes, in order to respond to a crisis.

#### Country examples:

- Example of virements rules: In Sweden and Finland, no virements are allowed. In the UK, virements are allowed between programmes under one line ministry, but virements cannot occur across ministries. In South Africa, movements are also allowed between programmes (under one ministry), but they are capped to 8% of the original budget allocation. Ministries typically cannot move money from capital to recurrent through virements; however, some countries suspend this clause during emergencies.
- Fiji: The 1993 cyclone Kina led the Fiji government to launch a rehabilitation programme equivalent to 5.3% of total expenditure. However, the government was intent on containing expenditure and so total expenditure was only 0.5% higher than originally budgeted; the government opted to undertake large-scale budget reallocations. Recurrent operating expenditure increased, while capital expenditure fell by 75% of the original allocation, with a large number of rural development and roads projects suspended in order to finance rehabilitation efforts.

#### International examples:

- Contingency Emergency Response Component: Run by the World Bank, this is a financing mechanism available to governments to allow rapid reallocation of uncommitted funds from World Bank-financed projects to other urgent needs during a disaster. A Contingency Emergency Response Component is typically embedded within a project but with zero funds allocated to it. Once activated, funds can be mobilised very quickly (as long as the project still has uncommitted resources available).

Advantages	Disadvantages
<ul style="list-style-type: none"> <li>• Relatively easy to implement (depending on the flexibility and rules of a country's PFM system).</li> <li>• Relatively quick to implement, particularly if implemented in a top-down manner (i.e. by the finance ministry without wide consultation).</li> <li>• Often there are areas of public spending that are no longer viable during a disaster; therefore, some financing can be reallocated very easily, with limited associated costs (e.g. travel expenses in the COVID-19 crisis since travel in most countries is much more limited).</li> <li>• Government in the driving seat of making fiscal decisions.</li> </ul>	<ul style="list-style-type: none"> <li>• Many of the disadvantages are related to the potential cost of budget reallocations as a financing instrument. Presently, the cost is unknown, but anecdotal evidence suggests that governments typically cut investment projects and operations and maintenance budgets. Cutting these areas can be very costly for development.</li> <li>• The cost of this instrument greatly depends on what areas government opts to cut, and what would have been the benefits of the projects that were cut, which will now not materialise, or materialise much later than planned.</li> <li>• Limited transparency: budget reallocations are poorly documented, making scrutiny (and cost estimates) difficult.</li> <li>• Potential high negative impact on non-disaster-affected sectors.</li> <li>• There are limits to how much a government can reallocate its budget; many costs, such as wages or pension payments, cannot be considered discretionary (at least in the short-term).</li> </ul>

**Best suited:**

**Budget reallocations are typically a first port of call for governments, utilised as a stopgap between accessing additional financing. Budget reallocations are, however, not a sustainable long-term option for financing disaster response, particularly if disasters are frequent and more predictable (e.g. droughts). The government will eventually run out of projects to postpone and ultimately the development of the country will be severely hindered.**

**Key considerations for SRSP**

- Understanding the relative cost of this instrument is very difficult as it depends on where governments decide to reallocate from, and how efficient they are at conducting this practice. Furthermore, there are often costs associated with pausing or stopping capital projects as contracts have already been signed with the associated terms and conditions. The opportunity costs of ex-ante instruments are better documented, in the sense that there is an understanding of the relative costs of loans, bonds, etc., and then the opportunity to compare them.
- When in the fiscal year the disaster strikes will impact how flexible this mechanism is. Towards the initial part of the fiscal year, it is difficult for ministries to identify areas of potential underspend; towards the later part of the fiscal year, there may be little space to cut the slack or cancel projects.
- These will generally be used in the first instance (though contingency funds can also be accessed first, if they have not yet been depleted), but if DRF financing can be used to replenish funds, the adverse effects may be lessened.
- In countries with a high degree of donor spending within their budget (e.g. a number of the Pacific islands), their capacity to utilise budget reallocations is substantially reduced.
- It requires the government to prioritise investment in the SRSP system over any other department which may be responsible for responding to a shock or disaster. It would follow that if a social protection system is underfunded by the government in normal circumstances, it may be an unlikely recipient of additional funds.

**Further reading and resources**

- CDP, 2020. The opportunity cost of COVID-19 emergency expenditure reallocation, [link](#).
- Benson & Clay, 2004. Understanding the Economic and Financial Impacts of Natural Disasters, [link](#).
- World Bank, 2021. Factsheet: World Bank's Response to COVID-19 (Coronavirus) In Latin America & Caribbean, [link](#).

**5.2.2 Instrument type: post-disaster borrowing****Description:**

Governments can opt to finance additional expenditure pressures following a disaster through taking on additional debt; all arrangements are made following the disaster. Post-disaster borrowing can take many forms, including access to crisis windows offered by development banks, issuing bonds, or other commercial (or concessional) borrowing.

**Country examples:**

- The World Bank's Crisis Response Window provides IDA countries with rapid credit to allow them to respond to the impact of severe natural disasters, public health emergencies, and economic crises, but this credit can also be accessed at an earlier juncture to slower-onset crises, namely disease outbreaks and food insecurity. Following a request for funding, a post-disaster needs assessment is typically conducted. Funds are disbursed within six months, on average; however, analysis from the CDP concluded that to date the average time from crisis to first disbursement from IDA's Crisis Response Window has been 398 days (analysis was pre-COVID-19).
- The IMF's Rapid Credit Facility and Rapid Financing Instrument provide rapid financial assistance to countries facing an urgent balance of payments need. Both can be used for various reasons, including economic shocks, natural disasters, and emergencies resulting from fragility. The Rapid Credit Facility provides credit on more concessional terms to low-income countries and does not impose ex-post conditionality. For the Rapid Financing Instrument, the requesting country is required to cooperate with the IMF to make efforts to solve its balance of payments difficulties and to describe the general economic policies that it proposes to follow. Prior actions may be required where warranted. Access is based on an assessment of the country's balance of payments need, its capacity to repay, the member's outstanding Fund credit, and its record of using Fund resources in the past. More than 90 countries have drawn down Rapid Credit Facility and Rapid Financing Instrument credit from the IMF

following the COVID-19 pandemic (the only rapid options highlighted here). As part of the COVID-19-related rapid arrangements, borrowing countries have committed to undertake governance measures to promote accountable and transparent use of these resources. Typically, financing can be agreed and disbursed in one week.

- Asian Development Bank Emergency Assistance Loans: The Disaster and Emergency Assistance Policy provides immediate short-term transitional assistance following a disaster (in conjunction with humanitarian assistance) usually for a period of two to three years. These rapid loans have low thresholds for eligibility and are provided to countries to mitigate immediate losses from shocks and restore critical services (for example key infrastructure or services) after emergencies. The Emergency Assistance Loan process sets a maximum of 12-week disbursement to countries.

#### Advantages

- Often a welcomed last resort for many countries, particularly if disasters are highly infrequent.
- Depending on the country's income status, these loans can be highly concessional.

#### Disadvantages

- Without pre-agreed plans in place, post-disaster credit may be slow to arrange and subsequently disburse to beneficiaries, depending on the source. Crisis windows may be slightly faster, while issuing debt could take up to nine months.
- It adds to country's debt burden; funds must be repaid, therefore reducing future fiscal space.
- Access is generally dependent on macro-fiscal conditions and the ability to access international credit markets.
- It is potentially costly, particularly if interest rates increase following disasters (although evidence is inconclusive); they can be highly concessional but need to be balanced with a country's overall debt burden.

#### Best suited:

**Unpredictable and infrequent disasters, regardless of scale.**

#### Key considerations for SRSP

- As with budget reallocation, it requires a government to borrow with the intention to invest in the SRSP system; this is a political decision when funds may be scarce.
- Additional borrowing may be advantageous if the SRSP is delivering a public good, e.g. works programmes.

#### Further reading and resources

- World Bank Independent Evaluation Group, 2019. IDA's Crisis Response Window: Lessons from IEF Evaluations, [link](#).
- [www.preventionweb.net/news/view/65963](http://www.preventionweb.net/news/view/65963).
- IMF, 2021. COVID-19 Financial Assistance and Debt Service Relief, [link](#).
- CDP dataset of IMF instruments (rapid and regular), [link](#).
- ADB emergency assistance loans, [link](#).

## Box 8: Future global fund for social protection – useful for financing SRSP?

### What is it?

The creation of a global social protection fund has been put forward by a coalition of actors, including the UN Special Rapporteur on extreme poverty and human rights, along with a network of NGOs (the Global Coalition for Social Protection Floors) and the French labour ministry. The proposal is for a dedicated financing mechanism to address the gap between domestically available resources and the cost of providing national social protection floors, in line with SDG 1.3, a gap costed prior to COVID-19 by the ILO for all 134 developing countries at US\$ 527 billion per annum, or the equivalent of 1.6% of the GDP of these countries. Updating estimates to take the COVID-19 pandemic into account show that developing countries would need to invest an additional US\$ 1.2 trillion – equivalent to 3.8% of their GDP – to close the financing gap, and that the gap for low-income countries is US\$ 78 billion, equivalent to 15.9% of their GDP. By way of comparison, the total official development assistance from OECD countries amounted to 152 billion USD in 2019 (OHCHR, 2020).

### How will it be financed?

According to the International Trade Union Confederation (ITUC), the fund could be financed through a mixture of Official Development Assistance (ODA), increasing corporation taxes, such as through a tax on financial transactions, which could potentially generate US\$ 15–75 billion per year, as well as a currency transaction taxes (US\$ 40 billion per year), a 0.42% tax on the total net worth of 2,208 billionaires (US\$ 37.8 billion), and putting an end to tax avoidance strategies (US\$ 100–240 billion per year), as well as through contributions from international financial institutions and other funds for urgent action concerning cash transfers and food distribution. There is also the capacity for conditionality on debt relief or cancellation and SDR liquidity swaps (ITUC, 2020).

### How will it be governed?

The current concept put forward by the Global Coalition for Social Protection Floors (though other suggestions are to be forthcoming shortly) suggests that governments will have the final say over which social protection programmes will be supported by the fund. Donor and recipient states will therefore be represented in the governance structures. However, adhering to the principles of accountability, it will also include 'organizations representing affected populations'.

### What are the advantages and disadvantages of such a fund for shock responsive social protection?

The advantage of such a fund is that it could mobilise resources and enable predictable financing, which would enable low-income countries to invest in the provision of social protection floors, coordinate and promote the development of social protection floors, and strengthen international cooperation in the sector. For a shock-responsive approach, if the right types of finance were in place it would incentivise actors to follow a common set of principles to improve coherent action. It is interesting to note in that regard that two of three proposed dimensions of the fund's mandate include shock responsiveness:

- Technical support to introduce or complete social protection floors and to develop their preparedness to sustain and expand in times of crisis.
- Co-financing of social protection floor transfers in times of crisis (e.g. natural disasters, reception of large numbers of refugees, economic crisis, etc.).

However, the disadvantages of such an approach include concerns that the fund would require additional financing to cover all the administrative costs of creating and running a new international institution, that participation in the fund would incur additional opportunity costs on the part of lower-income country governments, and that it would shift financing decision making away from country-level discourses and ownership.

Such a vertical sectoral approach could incentivise better cooperation at the national level, in terms of developing joint strategies/plans behind which the fund could provide more streamlined financing, instead of multiple donors and agencies approaching national governments with different approaches and programmes. However, the reverse is also true: it risks perpetuating sectoral fragmentation and competition both domestically and also among the development partners, rather than promoting integrated cross-sectoral planning and effective PFM.

As with SRSP, specific expertise and agreement would be needed to structure the shock responsiveness financing and programming components and principles of the fund correctly, to ensure funds could be triggered and arrive in a timely and predictable manner, and would complement (and not detract) from efforts in-country. The fund plans to cover very minimal benefits, meaning additional interventions may be needed to meet humanitarian standards, requiring potentially high levels of coordination. While it targets the poor, a principle for SRSP as well, other groups such as informal workers stand to miss out.

Likewise, it is not clear which contingencies the supported social protection programmes would cover, and whether these would be prioritised towards vulnerable groups, such as women and child-headed households; this would depend on the priorities of national governments. Lastly, there will likely be issues with eligibility as access to social assistance is generally defined by citizenship, which usually excludes forcibly displaced or migrant workers.

The example of the Green Climate Fund rejection of Ethiopia's proposal mentioned in Box 6 above is also instructive: unless members of the board hold a shared understanding of the objectives of the fund, proposals and funding requests could risk getting bogged down in bureaucracy and disagreement, or worse still, debates over what constitutes 'routine' versus 'shock responsive' social protection, and which should take priority. Currently, the proposal is asking for a large amount of funding for only 10 countries, which may not always align with those most in need or best suited to a SRSP approach.

*Source: OHCHR, 2020; Global Coalition on Social Protection Floors, 2020; ITUC, 2020; McCord et al., 2021.*

## 6. Reflections and recommendations for improving financing for shock responsive social protection

**This paper has attempted to outline in more detail the different aspects of SRSP financing**, from understanding context and downstream delivery (the 'money-out' aspects), then reviewing and introducing new financial sources and instruments for SRSP (the 'money-in' aspects). While by no means comprehensive, these sections have aimed to delve deeper into what financing for SRSP actually is (an under-discussed topic in the global literature), and the principles that underlie it.

**This section now summarises and elaborates on some of the main reflections, findings, and recommendations for improving financing for SRSP in the future.** They are split into two groups – those recommendations that look at the big picture, and those that focus on technical specifics.

### 6.1 Big picture focus

1. **Disasters are political, and so are the decisions about financing them.** When introducing risk financing instruments, governments have an array of decision points and considerations, including fiscal constraints and political will. Shifting from a more ex-post to ex-ante business model poses big questions about who owns the risk and who pays for it, with governments taking more ownership over time. DRF processes of quantifying risk and allocating responsibility help highlight both the extent of need and the most appropriate response, but also the extent of a problem. While it may represent value for money, such approaches can move the locus of power away from traditional decision makers towards objective and automated processes, and can meet with resistance due to perceived opportunity costs (losing out on investments today for those that yield returns only in the longer term) (Hobson, 2020). Governments in many countries therefore may need a more convincing business case to invest and deepen ownership of shock responsive approaches.

Demonstrating the value for money of such investments is key, but SRSP will also need to be presented as part of a broader package of risk management options that look to complement, not entirely replace, existing response mechanisms, and demonstrate how risk finance linked to SRSP can ensure that benefits actually reach the poorest (currently many DRF mechanisms do not have this explicit link, or focus on protecting government assets).

2. **Risk finance can be used to leverage policy and programmatic reform, but actors must speak with one voice.** While there is a wealth of ongoing SRSP initiatives on the ground, governmental reform can often lag behind, and prioritisation of SRSP can remain relatively weak, especially in terms of policy and fiscal planning and PFM. Likewise, general donor and international partner enthusiasm for SRSP is



not yet being translated into coordinated action in many settings. More efforts are needed to support systematic reform in areas of relevance to SRSP, such as anticipatory action, shock-based seasonal planning, delivery architecture, and aligning and leveraging investments across sectors in fragile contexts, as well as governmental reform in key areas around institutional and policy reform, PFM, the fiscal space, etc. Without this concerted and inclusive effort, prioritisation of SRSP (and its financing) may remain low in countries that could benefit from it most, also limiting governments' capacity to meet the prerequisites for risk financing. Alternatively, a rush towards introducing different risk financing instruments and approaches could further fragment efforts to manage and respond to covariate shocks coherently.

Consideration could be given to working between the principal donors in the shock responsive and adaptive agendas to introduce a broad set of requests to key government counterparts to incentivise multi-year institutional and fiscal reforms to advance SRSP, matched by common commitments from donors. Disaster risk finance strategies are a key vehicle for such advocacy.

- 3. For the sake of sustainability, a balance of investments is necessary to both reduce and transfer risk.** Reducing the size of the risks to be transferred also reduces the cost of transferring the risk (Hobson, 2020). Without investing in risk reduction and prevention, interventions can become more efficient at responding to shocks, but not necessarily more effective in reducing risk and caseloads over time. Doing more of the same (such as extending social protection floors or investing in resilience programmes) will help, but is not necessarily enough on its own. Likewise, DRF is one necessary component for SRSP to function effectively, but not the only one: it is not feasible in all contexts, and risk transfer should only be used where it is cost-efficient.

This paper has noted that SRSP is fundamentally about achieving interconnections across sectors and financial instruments to create a more comprehensive, efficient, and integrated risk management framework, which in most countries does not exist. Again, this often comes down to questions of politics and coordination, rather than technicalities such as which financial instruments to use. Investing in coordination – and ensuring a broader set of actors are around the table when deciding on SRSP financing options – remains critical.

- 4. Climate finance, especially adaptation finance, has the significant potential to fund SRSP, yet faces a series of barriers to doing so.** As shown in Box 5, some successful country projects (e.g. in the Philippines) offer examples of how global climate adaptation finance can be channelled to funding to SRSP. Loss and damage finance could also provide a relevant funding source for SRSP, but there does not yet exist a dedicated source of financing for loss and damage overall, and clarification is needed on how developing countries could access funding for loss and damage through existing mechanisms such as the GCF (Raju et al., 2021). Tools such as catastrophe modelling, parametric insurance, and anticipatory action all have a clear climate adaptation focus, and beneficiaries reached through SRSP tend to be those worst affected by climate change and climate-related disasters. However, stronger advocacy is clearly needed around the use of climate funds to support routine and shock responsive social protection.

We propose more efforts are invested in advocating for the potential of climate finance to be used to 'shock proof' social protection systems and programmes, while also using social protection to deliver adaptation, mitigation, and risk management dividends. This can include governments utilising the potential of Nationally Determined Contributions for climate-proofing the social protection sector, or utilising unearmarked climate finance in the form of general budget support linked to broader climate policy reforms to finance SRSP. This will also require the integration of better metrics and key performance indicators into social protection programmes (in terms of monitoring and mitigating climate risk, and demonstrating how social protection addresses climate risk for the most vulnerable). More broadly, the global climate funds and their boards need to resolve how and whether climate finance can be used to support routine protection and SRSP through their guidance and decision-making processes, as well as the technical assistance and advice the global funds provide. The 2021 United Nations Climate Change Conference (COP26) and the momentum created by the COVID-19 crisis offer significant opportunities to advocate for such as shift in thinking towards the use of climate finance for social protection (Aleksandrova, 2021).

- 5. There is a need to review and enhance the role that humanitarian actors and financing instruments can play in financing SRSP.** Currently, several dual mandate agencies, the IFRC and international NGOs known for leading humanitarian response are also funding SRSP initiatives of various kinds. Meanwhile, there is growing approval of the use of humanitarian financing instruments, such as pooled funds for anticipatory action and forecast-based action (Pichon, 2019). Risk pooling instruments,

such as ARC, offer humanitarian agencies the opportunity to ‘replicate’ their coverage to reach additional households, enabling humanitarian actors to access market risk capital to cover costs related to humanitarian action in specific countries (Hobson, 2020). Parametric insurance instruments are now being tested to finance anticipatory action to support preparedness for shocks, an area central to the mandate of humanitarian actors. Yet discussions around linking this all to existing social protection systems and programmes, and the role of humanitarian actors and financing mechanisms in this picture, remain in many cases unclear. Likewise, while risk financing hinges on contingency planning, this does not necessarily mean all SRSP initiatives across humanitarian and development partners are following the same contingency plans; this is complicating efforts to coordinate action.

6. **Increase investment in approaches to financing SRSP that that are responsive to gender equality and social inclusion (GESI) issues** - addressing the right ‘money-out’ parameters means ensuring that resources get delivered not only in a timely manner, but in an equitable way as well, differentiated to peoples’ inter-sectional needs. Increased investment is necessary across components of the system to ensure responses a) reach women, girls and diverse groups, and b) contribute to longer-term empowerment and transformative objectives (beyond the immediate shock response)<sup>22</sup>. This can include investment in areas such as data gathering (collection and analysis with a focus on age, gender and disability), programme linkages and coordination to GESI-responsive programming (e.g. linkages to essential health services), tailored outreach and communications, accountability and feedback mechanisms, programme delivery to reach marginalised populations, and investment in staff capacity and expertise. This can be further advanced by investing in local organisations<sup>23</sup> led by or representative of women, persons with disability etc., to help ensure SRSP resources are channelled directly to women, girls and diverse groups as part of shock response.
7. **Further research needs to be undertaken into expanding financial protection strategies from climate- and weather-induced covariate shocks to cover other complex risks, including interconnections with other shock responsive systems beyond social protection such as health.** While in theory the principles of DRF and SRSP mentioned at the outset of Section 3 can apply to different types of shocks, they have not yet been applied to contexts of conflict or forced displacement. More evidence is needed on how to finance SRSP in fragile and conflict-affected situations, and how to align financial instruments, sources, and actors, which in contexts of insecurity can be quite different. Likewise, the evidence around how social protection systems could work more closely with and learn from other shock responsive systems, such as health response systems, could be more systematically recorded and leveraged, building on the multiple lessons learned through the COVID-19 response.

## 6.2 Technical focus

8. **Risk financing mechanisms offer huge potential, but it is essential to address skills and affordability deficits.** Risk financing in the development sector is relatively new, and **technical** expertise is at a premium. A shift of expertise is needed from private enterprises and IFIs towards the public sector in key areas such as collecting, analysing, and modelling data on risk, hazards, and financial impacts, and developing DRF strategies. Too often, this expertise is not connected to those with programme implementation knowledge, another area that requires collaboration and dialogue. Likewise, the **affordability** of certain instruments, such as risk transfer, is still out of reach for many countries, which is preventing risk regional pooling mechanisms, such as ARC, from achieving scale.

The consequence is that the international community needs to consider greater subsidisation of the costs (in terms of things such as premiums but also technical expertise) of DRF and SRSP in the short term to make risk financing more affordable, demonstrate results, and enable wider uptake from governments. Crucial to this effort is translating high levels of support from donors and IFIs, as well as global initiatives such as the InsuResilience Partnership, into more tangible, country-based partnerships that link DRF to SRSP, with a focus on working through government in a contextually appropriate way over the longer term (Hobson, 2020).

9. **The range of existing financial products for SRSP should be consolidated.** Innovation in areas such as catastrophe risk modelling, the creation of parametric insurance instruments, and the convergence of

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<sup>22</sup> See [SPACE Strengthening Gender Equality and Social Inclusion \(GESI\) During the Implementation of Social Protection Responses to COVID-19](#)

<sup>23</sup> See [SPACE Programming Guidance: Embedding Localisation in the Response to COVID-19](#)

traditional reinsurance markets and broader global financial markets through instruments such as cat bonds, have revolutionised the cost-effectiveness of DRF mechanisms, and made it possible to transfer larger volumes of natural hazard risk to global markets more cheaply and more effectively (Hobson, 2020). However, the large volume of financial products can seem overwhelming, and few (if any) countries have successfully developed and sustained a coherent set of DRF instruments, including between DRF and SRSP. The number of risk financing options, and the requirements for their establishment, can seem overwhelming and inaccessible.

More investment could be made in helping country-based stakeholders scope out the full range of financial products on offer, their prerequisites and trade-offs, and how to integrate them into a longer-term vision for SRSP at organisational or national level. More country case study materials could examine the benefits, drawbacks, and entry points for financing SRSP. To date, too many case studies have served as promotional materials for specific financial instruments, but more detail is needed as to why specific financial instruments, in isolation or combination, succeed or fail. This could be coupled with a series of dialogue sessions between policymakers and practitioners to enable open and frank exchange on what works, what does not, and where opportunities lie.

- 10. DRF instruments need to be attached consistently to downstream delivery vehicles such as SRSP.** To date, successful examples of effective disaster risk finance linked to SRSP are hard to find. Examples of triggered funds from parametric insurance being delayed in centralised bureaucracies of government are not uncommon (see the example of ARC pay-outs to Niger and Senegal in 2015), with or without contingency plans in place. Where humanitarian organisations are using risk financing approaches, such as forecast-based action, to release benefits in a timely manner, they may not be working around the same contingency plans as those of government.

This means recognising coherent yet differentiated investments are needed in systems and various forms of capacity (human, financial, and material), regardless of context, levels of fragility, or the maturity of existing social protection systems. Likewise, linking to the principles outlined in Section 3 around how that SRSP is designed (in terms of inclusiveness, timeliness, cost efficiency, etc.) can significantly affect whether it delivers on SRSP goals. Government and donor interest in risk financing is high, and development partners can build on this interest by helping address these bottlenecks and ensure that a wider cross-section of stakeholders are around the table to improve accountability and delivery.

- 11. Investing in risk-aware systems, data-driven processes, and different forms of capacity for financing SRSP benefits everyone.** This forms the backbone to good risk finance and ensuring interconnections across different forms of investment in SRSP. More focus should be placed on achieving the cost-benefit returns of a sustainable and systemic approach to risk management, designed around core and commonly agreed principles. Investing in risk-aware systems and tools that can be used or interconnected to serve a wider community of actors and beneficiaries, and can address a multitude of shocks, represents a win-win for everybody. Likewise, more investment is needed to improve various outputs required for both risk finance markets to function and for SRSP programmes to better operate and target assistance. These win-win investments are crucially important at a time when fiscal space for public sector investment is already contracting.

Examples include building and improving database interoperability; improving data availability, quality, consistency, and protection for assessments of vulnerability, risk, and financial impact; and tracking financial and programme data. Likewise, this means that recognising coherent yet differentiated investments are needed in systems and various forms of capacity (human, financial, and material), regardless of context, levels of fragility, or the maturity of existing social protection systems. Financing for SRSP is a relatively new area, and suffers from definitional ambiguity and a lack of obligation to report expenditure (an issue common to tracking financing in general), with financing for SRSP falling between different sectoral sources. Further ways of tracking investment in SRSP should be explored, including through improving the labelling and tagging of SRSP project investments in major donor databases (such as the UN's FTS and the OECD's Creditor Reporting System), to help clarify the division of finance between humanitarian and social protection programmes, increase accountability, and support advocacy for investment in SRSP as part of broader 'nexus' dialogues and reform agendas.

- 12. The proposal for a global social protection fund from the angle of financing shock responsiveness needs to be reviewed.** As noted above in Box 8, the fact that the proposal for a new global fund for social protection includes shock responsiveness as part of its core mandate is welcomed. Naturally with any such proposal many questions remain outstanding. Among these is whether DRF could be considered for the global fund itself (alongside things such as ODA and financial transaction taxes), and how such shock responsive investments would be planned and managed alongside those to

extend social protection in an integrated manner. Doing more of the same (such as extending social protection floors) is not enough to meet the needs of SRSP, and discussions around finance need to avoid the dichotomy of supporting either routine or shock responsive investments in social protection wherever possible (rather than focusing on investing in systems and capacities that benefit both routine and shock responsive approaches), while noting that certain tough trade-offs in investment choices are unavoidable. Lessons from how attitudes from governing bodies for climate finance have enabled or (mostly) blocked support to SRSP are instructive but are rarely discussed (see Box 5 and Box 6).

More expertise could be provided in the current discussions around how such a fund could be designed and developed so that both the 'money-in' and 'money-out' factors mentioned above could be integrated into governance of the fund. This could also open up other avenues to finance the global fund that up to now have not been considered. The interaction between a global fund for social protection, and others such as the GCF, as well as global health funds (and whether health funds themselves have considered or built-in shock responsive mechanisms that touch on social protection), also merits discussion.

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# Annex 1: Glossary

- **Basis risk:** Basis risk is the difference between an index and the shock that the index is supposed to be a proxy for. A pay-out triggered by an index may be higher or lower than the beneficiary's losses, leading to overpayment or shortfall, respectively. Where there are differences of opinion among stakeholders over what the index is supposed to be a proxy for, the precise definition of basis risk can be contested. For example, disagreement may arise over whether an agricultural insurance product that uses a rainfall-based index covers drought-induced crop disease and pest damage (CDP, 2020).
- **Catastrophe bonds (cat bonds):** Bonds are issued by national and local governments, and other quasi-public organisations, as well as large companies, to finance investment. In exchange for the payment of the bond by the purchaser, the issuer agrees to pay the purchaser interest payments on a set schedule, and repay the principal at maturity. As such, they are a form of debt instrument. Catastrophe bonds are short-term bonds (three to five years) issued by a sponsor to investors in the capital markets. However, in contrast to normal bonds, they are 'triggered' by a catastrophe. Once triggered, the bond sponsor maintains a portion of the principal and consequently investors lose a portion of principal and interest payments. In this way, they transfer natural catastrophe risk to investors. The bond issuer will typically be a state or large infrastructure owner. Insurers, reserve funds, or risk pools might also issue catastrophe bonds as an alternative to purchasing reinsurance, to lessen their risk exposures. They can be attractive instruments to investors as cat bond risks are uncorrelated with other risks investors face (GIZ, 2019).
- **Catastrophe Deferred Draw-Down Option (CAT-DDOs):** The development policy loan with a CAT-DDO is a contingent financing line that provides immediate liquidity to countries to address shocks related to natural disasters and/or health-related events. It serves as early financing while funds from other sources such as bilateral aid or reconstruction loans are being mobilised (Yeo & Navarro-Martin, 2018). This product allows countries to borrow up to the lower of US\$ 250 million or 0.5% of GDP (IDA countries) or US\$ 500 million or 0.25% of GDP (IBRD countries) in the event of a state of emergency being declared by the country. The draw-down period for the loan is three years, renewable up to four times. The interest rate on the loan is the same as for regular IDA/IBRD loans, with no front-end fees or renewal fees (IDA countries)/0.5% front-end fee and no renewal fees (IBRD countries). The product is available only to countries that have, or are preparing, a satisfactory DRM plan, which the World Bank monitors on a periodic basis (Menan et al, 2019).
- **Contingent credit/financing:** Mainly ex-ante loan agreements, such credit provides immediate liquidity in the aftermath of a covariate shock, often at highly concessional terms (long duration with low interest rates). Ex-ante loan agreements are typically offered by multilateral development banks and IFIs. These agreements have the potential to ensure financing beyond a government's own reserve funds. The main drawbacks are: (1) the funds are often provided as budget support, so there is no guarantee that they will be used to finance ASP programmes; and (2) they are still loans and so add to the country's debt (O'Brien et al., 2018a). Contingent credit is most cost-effective for high-impact, low-frequency shocks (Bowen et al., 2020).
- **Contingent liabilities:** These are obligations to pay costs associated with a possible, but uncertain, future event. Because there is no obligation to pay unless the event occurs, contingent liabilities might not be formally listed as liabilities on an organisation's balance sheet. Contingent liabilities might be explicit or implicit:
  - Explicit contingent liabilities are contractual commitments to make certain payments if a particular event occurs – the basis of these commitments can be contracts, laws, or clear policy statements;
  - Implicit contingent liabilities are political or moral obligations to make payments, for example in the event of a crisis or a disaster – governments do not recognise these liabilities until a particular event occurs; implicit contingent liabilities are difficult to assess, let alone manage in a consistent manner, precisely because of their implicit nature (CDP, 2020).
- **Disaster:** A disaster refers to a situation when the impacts of a shock are widespread and often overwhelm local and national capacities (UNDRR, 2017).
- **Disaster risk financing (DRF):** DRF covers the system of budgetary and financial mechanisms to credibly pay for a specific risk, arranged before a potential shock. This can include paying to prevent and reduce disaster risk, as well as preparing for and responding to disasters (CDP, 2020).



- **Ex-ante financing:** This refers to financing agreed in advance of an event, which will be available to spend once an event occurs.
- **Ex-post financing:** This refers to money and cash agreed once the event has taken place.
- **Humanitarian financing:** Humanitarian financing ‘refers to the financial resources for humanitarian action spent outside the donor country ... based on what donors and organisations report as such and does not include other types of financing to address the causes and impacts of crises ... referred to as crisis-related financing’ (Development Initiatives, 2020, p. 81).
- **The International Development Association (IDA):** The IDA is the part of the World Bank that helps the world’s poorest countries. Overseen by 173 shareholder nations, the IDA aims to reduce poverty by providing zero to low-interest loans (called ‘credits’) and grants for programmes that boost economic growth, reduce inequalities, and improve people’s living conditions. IDA complements the World Bank’s original lending arm – the International Bank for Reconstruction and Development (IBRD). The IBRD was established to function as a self-sustaining business and provides loans and advice to middle-income and credit-worthy poor countries (World Bank, 2021).
- **International Financial Institution (IFI):** An IFI is a financial institution that has been established by more than one country, and hence is subject to international law. Its owners or shareholders are generally national governments, although other international institutions and other organisations occasionally figure as shareholders. In many parts of the world, IFIs (such as the World Bank, Asian Development Bank, African Development Bank, the Inter-American Development Bank, etc.) play a major role in the social and economic development programmes of nations with developing or transitional economies. This role includes advising on development projects, funding them, and assisting in their implementation. Characterised by AAA-credit ratings and a broad membership of borrowing and donor countries, each of these institutions operates independently. All, however, share the following goals and objectives: to reduce global poverty and improve people’s living conditions and standards; to support sustainable economic, social, and institutional development; and to promote regional cooperation and integration (Government of Canada, 2020 – from CDP, 2021).
- **Indicators (for early warning early action):** Indicators provide specific information on the state or condition of environmental and socio-economic systems. Indicators can be qualitative, quantitative, or a combination of both. In early warning early action, they can relate to both rapid- and slow-onset events (FAO, forthcoming).
- **Insurance:** A contract which provides a guarantee of compensation for specified loss, damage, illness, or death in return for payment of a specified premium.
- **Indemnity insurance:** A (re)insurance contract which pays out compensation worth the ultimate net loss of a specific asset. This type of insurance can be useful in protecting high-value assets such as homes, where there is a relatively narrow scope of potential loss. Insurance pay-outs are determined based on an assessment of losses after an event has occurred (InsuResilience Global Partnership, 2020 – from CDP, 2020).
- **Overseas Development Assistance (ODA):** This is defined by the OECD Development Assistance Committee as ‘government aid that promotes and specifically targets the economic development and welfare of developing countries’ (OECD, 2019 – from CDP, 2021).
- **Risk:** While there is no universal definition of risk, it is commonly understood as the potential for suffering or loss (including loss of life) that could occur in a specific time period, determined probabilistically as a function of hazard, exposure, vulnerability, and capacity (CDP, 2020).
- **Risk layering:** As regards risk retention and risk transfer instruments, a risk-layering strategy can reduce costs and improve the reliability of funding. This involves combining risk retention instruments for high-probability, low-impact events with risk transfer instruments for the lower probability, higher impact events. As a rule of thumb, an economic and pragmatic approach aims to reduce risk first, then arrange risk retention, and finally transfer risk (Centre for Disaster Protection. 2020a).
- **Risk pooling:** Risk pools are structures where a selection of organisations (typically administrative units) come together to purchase insurance. The pool effectively becomes the ‘captive insurer’ (the bespoke insurance company) for the units in question. The pool retains some of the risks itself and transfers other risks, through reinsurance, or other instruments, to third parties. The pool is able to purchase insurance more cheaply than if its members purchased it individually, as it offers a more diversified risk portfolio, and because of economies of scale and greater buyer power. Pool membership may be conditional on having

a disaster response plan. Risk pools typically use parametric triggers, allowing pay-out within one to two weeks, making them suitable instruments for providing liquidity during the response phase of a disaster (Centre for Disaster Protection, 2020a).

- **Risk retention:** This involves keeping the risk within the balance sheets, meaning that the cost of the disaster will be repaid.
- **Risk transfer:** The transfer of risk is a business agreement in which one party pays another to take responsibility for mitigating specific losses that may or may not occur. This is the underlying tenet of the insurance industry. Risks may be transferred between individuals, from individuals to insurance companies, or from insurers to reinsurers. When homeowners purchase property insurance, they are paying an insurance company to assume various specific risks associated with homeownership. When purchasing insurance, the insurer agrees to indemnify, or compensate, the policyholder up to a certain amount for a specified loss or losses in exchange for payment (Investopia, 2020). Examples include market-based insurance, reinsurance, risk pools, derivatives, and cat bonds.
- **Shock:** The word 'hazard' in DRM terminology tends to focus on climate- and weather-related events. The word 'shock' is used in this paper as a wider term that denotes the wide array of events (e.g. natural, economic, epidemiological, conflict-based, etc.) that households, governments, and humanitarian and social protection systems aim to address (TRANSFORM, 2020). It can be seen as the realisation of risk that can lead to losses or negative outcomes. Shocks can affect the individual or household (idiosyncratic) or a large number of people simultaneously (covariate).
- **Social impact bonds:** Impact bonds encourage risk reduction investment by offering a pay-for-performance contract between an 'outcome-based funder' – typically a government, donor agency, or philanthropic organisation – and private sector investors in relation to a project that has social or development objectives. Under an impact bond structure, investors will provide capital (either/both debt and equity) to a project with the outcomes-based funder committing to make repayments to investors depending on the extent to which independently verified performance targets are met. These targets place a strong incentive on the overall outcomes expected from the project, rather than just immediate project outputs. Investors will normally appoint a 'managing agent' to implement the project. The structure could be used to incentivise investments that reduce the risk that disasters pose to infrastructure, but also, for example, through boosting the adaptive capacity of individuals and communities by improving health or education outcomes, thus also reducing the risks to lives and livelihoods that disasters cause. The long timescales and substantial transaction costs involved in structuring impact bonds mean that they are most appropriate for preparedness activities typically at the community, municipal, and/or sovereign level (GIZ, 2019).
- **Thresholds / probability threshold:** Thresholds mark points that signal a warning associated with a specific indicator (see definition of 'Indicators' above). They are the value of forecast probability at which the chances of reaching the impact level are considered high enough to merit forecast-based action. The probability threshold can be defined based on comparing the risk of acting in vain, versus the risk of failing to act. The probability is agreed upon beforehand among all stakeholders. For example, action will be triggered when there is a greater than 50% chance that the defined flood water levels will be reached (IFRC/Red Cross Climate Centre, 2020). One indicator can have one or several thresholds indicating different levels of risk. Thresholds mirror the nature of their indicators and can be measured quantitatively and qualitatively (FAO, forthcoming).
- **Triggers:** A trigger is a pre-defined threshold of an index underlying a risk finance mechanism which, if exceeded, prompts a pay-out. A trigger may also leave an element of discretion to a designated party about whether or not to launch a response activity (CDP, 2020). A trigger is a pre-defined probability and magnitude of disaster risk which activates anticipatory action in a given area (FAO, forthcoming).

# Annex 2: Case study – Financing the COVID-19 response

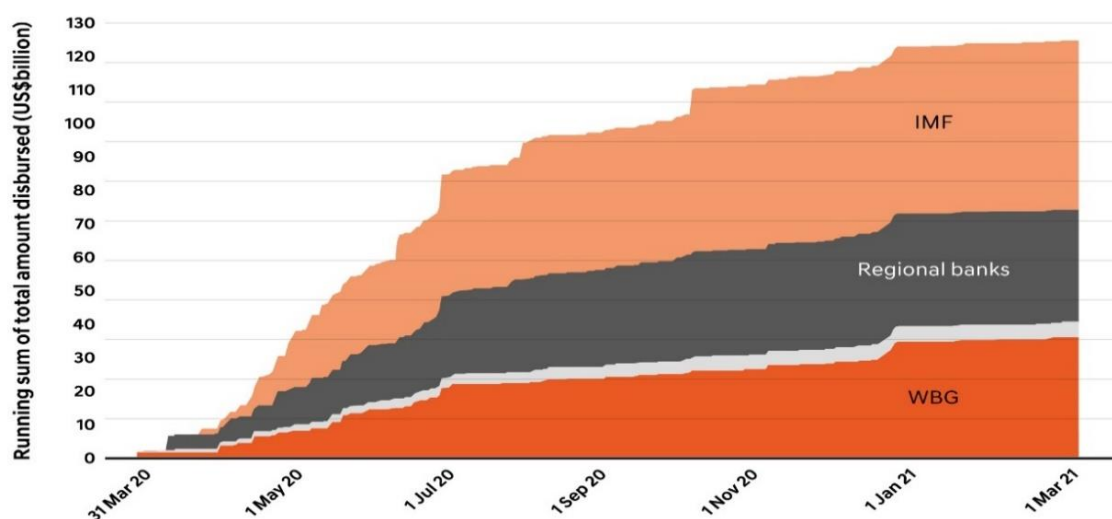
The COVID-19 pandemic increased global levels of need, compounding existing crises and creating new ones. It has presented immediate mortality and morbidity threats, and impacted on longer-term levels of poverty and food insecurity, livelihoods, health systems, and national productivity. In response, various forms of finance have been mobilised by the international community. The UN has released its COVID-19 Global Humanitarian Response Plan (GHRP), with appeals for 63 countries and an intended total of US\$ 7.3 billion; it had received US\$ 4.35 billion by December 2020 (see Figure 7 below). In addition to humanitarian needs, the UN is seeking a further US\$ 1.2 billion for the World Health Organization to address public health needs, as well as for its Framework for the Immediate Socioeconomic Response to COVID-19 in developing countries.

Humanitarian needs have never been higher, and COVID-19 is putting a significant strain on humanitarian resources. With the addition of COVID-19 requirements, total UN humanitarian funding requirements for 2020 reached US\$ 37.7 billion, 25% higher than in 2019 (Development Initiatives, 2020). For those countries in the GHRP, the scale of need varies widely, yet 34 of the 63 countries are already in protracted crisis, and nine of the 10 largest recipients of COVID-19-related assistance were also the largest recipients of routine humanitarian assistance in 2018 (Development Initiatives, 2020).

The call for financial support for COVID-19 has been answered by bilateral, multilateral, and private donors. At the end of June 2020, 20% of **all** humanitarian requirements had been met, totalling US\$ 7.5 billion, with equal amounts going to COVID-19 and non-COVID-19-related appeals (Development Initiatives, 2020). While this amount was down as an overall percentage compared to the same time in 2019 (23%), volumes disbursed in June 2020 were US\$ 578 million higher than by mid-year in 2019. In addition, total pledges made in the Global Goal summit convened by the European Commission in support of the pandemic response amounted to around US\$ 14.3 billion for COVID-19, indicating that significant funds are yet to be released or reported (Development Initiatives, 2020).

Lending has also been substantial. Total support in the form of grants and loans (concessional and non-concessional) provided by the main development finance institutions for the COVID-19 pandemic response amounted to US\$ 110.61 billion by the end of 2020 (CDP, 2021). As of mid-2020, 36% of support provided by five major development finance institutions, amounting to approximately US\$ 46.7 billion, was directed to 31 countries experiencing protracted crisis and also targeted by the GHRP. Further support to enable the use of domestic fiscal resources to respond to the pandemic has been made possible through the short-term suspension of debt repayments and through grants to cover debt repayment (for example, through the Catastrophe Containment and Relief Trust of the IMF) (Development Initiatives, 2020).

**Figure 7: Funding to COVID-19 response by institution type (2020).**



Source – CDP, 2021.

However, overall ODA resources to crisis-affected countries are set to fall, as are foreign direct investment and remittances, the latter of which make up the majority of capital inflows in many crisis-affected countries. Research from Development Initiatives based on economic forecasts made by the OECD indicates that in a worst-case scenario, revenues for countries experiencing protracted crisis may fall 7% in 2020, and that global ODA could fall from US\$ 153 billion in 2019 to US\$ 134 billion by 2021, with cuts continuing beyond 2021 as governments reassess domestic priorities (Development Initiatives, 2020). For over a third of countries in the GHRP, ODA makes up a quarter of all government expenditure, meaning cuts will be felt keenly.

Despite the COVID-19 crisis raising further questions about how aid is delivered, increasing calls to support local and national actors, available data on financing shows a retrenchment of support to traditional actors. As of June 2020, almost 75% the total international humanitarian assistance to the COVID-19 response was channelled through multilateral organisations. Of this amount, 92% went to just four agencies, with the World Health Organization joining the familiar 'big three' of UNICEF, WFP, and UNHCR (see more on the Big Three in Table 1). Less than 5% of total international humanitarian assistance during the same period was channelled through national public sector institutions (Development Initiatives, 2020).

Likewise, work from the CDP shows that almost none of the money provided for the COVID-19 response was in place in advance. For instance, in the first six months of the crisis response by IFIs, only 2% of all the funding had been pre-arranged. While a characteristic criticism of crisis response is that funding arrives too late, in the case of the COVID-19 crisis disbursement has been far quicker, with the likes of the World Bank transferring half their funds within 100 days, timing that will be hard to improve upon (Hill *et al.*, 2020). However, we note that a critical distinction in 'disbursement' has to be made between when money was provided from a donor to a client (e.g. from an IFI to a government), as opposed to when it was disbursed from the client to beneficiaries. Much less can be derived from the data in terms of the latter as opposed to the former, potentially distorting perceptions of how fast money actually reaches those who need it.

With very large numbers of individuals and businesses needing support even quicker, the only mechanisms in place to respond in many cases were pre-existing catastrophe-contingent loans such as the World Bank's CAT-DDOs, or government reallocation of existing budget lines, with longer-term implications for routine programmes. This intersected with a lack of planning that reduced the effectiveness of the response in various ways, and shows that while attention to and investment in DRF has been growing, it still makes up only a small amount of total crisis financing and is not yet an approach widely adopted by the international crisis financing system.

This situation underscores four points. First, since the vast majority of the funding was not pre-arranged, it did not become available at the beginning of the crisis when the needs were generally highest. Secondly, grants (including the grant components of concessional lending that make the cost of borrowing cheaper) can be better targeted towards the poorest countries or those at risk of poverty. For instance, only 46% of the UN's GHRP is going to countries where poverty is expected to increase the most (Hill *et al.*, 2020). Thirdly, with 93% of financing from IFIs coming in the form of loans, there is a need not only to provide more money, but also to address debt distress through debt relief. Lastly, there is the need to move away from reactive crisis response to investments in crisis management and preparedness to help improve the timing, cost, and effectiveness of humanitarian and broader SRSP actions, as part of the anticipatory action and DRF agendas (Hill *et al.*, 2020).



# Annex 3: Establishing triggers for rules-based disbursement

Any SRSP initiative should consider ahead of time when it intends to activate and deliver shock responsive support. This moment we call the 'trigger'. A trigger could be anything from someone simply deciding that the activation should happen to a fully automated, data-driven process. Assuming that policymakers want to deliver shock responsive services rapidly, reliably, and cost-effectively, they should consider the latter. The more concretely that moment is defined before it actually happens, the fewer discussions need to be had on whether or not a mechanism should be activated (in short, minimising political influence). Naturally, this type of response has the potential to be much faster. The benefits of a rules-based approach to triggering have been demonstrated extensively by the DRF literature (see e.g. World Bank, 2014).

In the world of DRF and insurance, two broad categories of triggers are being used: 'hard triggers', which are based on objective data to define a specific criterion that launches the shock response; and 'soft triggers', which leave an element of discretion to individual people or processes to decide whether or not the response should be launched:

- Hard triggers that could be used for SRSP include: measurements of the severity of a certain natural hazard, such as satellite-recorded rainfall estimates or soil moisture (for drought), the water surface extent (for floods), or wind speed (for storms); the average hazard-related damage or loss in a pre-defined area, such as the average crop yield in a certain area after the harvest; or the impact of a certain event, such as the number of refugees arriving in a certain area or the modelled number people becoming food insecure due to a drought. Soft triggers leave more discretion to a deciding party. The key benefit of hard triggers is that they can be structured to be objective, non-manipulative, and quickly available after the occurrence of a shock. At the same time, no parametric index is ever perfect: it may not account for all situations that should result in a response, or may fail to capture the situation it means to capture.
- Soft triggers are more flexible than hard triggers. For example, a committee of technical experts or policymakers may be well-placed to decide when to commit to scaling-up a national safety net. This is especially the case when the underlying landscape of shocks is complicated or unpredictable, and deciders want to maintain sufficient room to manoeuvre rather than be bound to a narrow band of triggering situations as determined by a parametric index. The challenge with soft triggers is that they can be prone to delay or politicisation.
- A useful way to make use of the advantages both of hard and soft triggers can be to use a combination of both. The primary trigger can be a hard one but be backed up by a secondary soft one. Thus, the launch of the shock response will be determined primarily by data; however, should the hard trigger fail to capture a shock or should an unforeseen situation arise, a response could still be launched via the secondary discretionary mechanism.

When structuring a SRSP trigger, decision makers should consider the following points to ensure high-quality design (Lung, 2020a):

1. Hard triggers should be based on data that is reliable, timely, resistant to manipulation, and cost-effective. Data should be objective in order to avoid potential political bias in the process; it should be timely, so as to ensure that the data is available as early as possible in order to enable effective shock response; it should be resistant to manipulation, e.g. by using data from a third party such as NASA; and it should be cost-effective, in order to be able to direct resources where they are most needed and to enable external scrutiny.
2. The trigger should also be structured so as to make sure that it enables early response. For many SRSP activities, speed is particularly important. Triggers should thus aim to define the occurrence of a shock as early as possible. Increasingly, triggers today are also structured not to detect the occurrence of a disaster but to predict such an occurrence. This has been piloted by the 'Forecast-based Financing' agenda by International Federation of the Red Cross.<sup>24</sup> In theory, such forecast-

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<sup>24</sup> [www.forecast-based-financing.org/](http://www.forecast-based-financing.org/)



based triggers could also be used to launch shock responsive activities via SRSP, but this has not yet been implemented (Costella et al., 2018).

3. Significant attention should be paid to the performance of the trigger. In other words, if a parametric index is chosen as a hard trigger, it should approximate well what it aims to approximate. Some hazards are much harder to detect or to model, and thus the quality of the triggering decision may suffer.
4. This means that the development of any parametric index should be led by an appropriate team of experts. It should also be rigorously tested before use and measures be put in place that ensure mitigation of any potential mismatches between index value and reality, as well as continuous review and improvement over time.
5. For data-driven hard triggers, there must be appropriate fail-safe mechanisms. As described above, parametric indexes are bound to be imperfect and only an approximation of reality. For this, secondary (hard or soft) triggers can offer a remedy. SRSP programme designers should also think about situations in which the data may not be recorded as planned, e.g. because a satellite is taken off-service. For these situations, it is best practice to build redundancy into the system, for example, by maintaining a backup dataset.

### Box 9: Trigger examples for shock-responsive social protection

Although the financing landscape for SRSP is still evolving, many systems have already adopted rules-based approaches to launching their shock-responsive services:

**Kenya – Hunger Safety Net Program:** The Program uses a hard trigger to launch a potential scale-out of safety net payments to additional households. The trigger is based on the Normalized Difference Vegetation Index, which is recorded by satellites and approximates the existence of pasture on the ground. Two separate absolute Vegetation Condition Index (VCI) threshold values were chosen that reflect whether a 'severe' or an 'extreme' level of drought have been reached in the observed regions. Both threshold values correspond to certain scale-up frequencies. Taken together, they have resulted in an average scale-up frequency of the Program of once every 1.6 years for targeted sub-regions (Calcutt *et al.*, 2021).

**Ethiopia – Productive Safety Net Program:** Meanwhile, the Program uses a mix of hard and soft triggers to scale out to additional beneficiaries. The program comprises a Risk Financing Mechanism which enables the rapid scaling-up of shock response services. The triggering decision is based on objective data as collected by the government early warning system. When the early warning system indicates the occurrence of a shock, a decision making process for the scale-up of the Program is started. The final decision whether the Program is scaled up, how many people are targeted and for how long, is not automatic, however: it rests with the Risk Financing Mechanism Management Committee (World Bank, 2013).

**Uganda – Northern Ugandan Social Action Fund:** The activation of the shock-responsive component of the Fund depends on a primary hard and a secondary soft trigger. As with the Kenyan Program (though constructed in a slightly different manner), the primary trigger depends on the Normalized Difference Vegetation Index. When the Index records that rangeland conditions have become too dry during the season, beneficiaries are added to the social protection programme from a pre-selected roster of vulnerable households. The secondary trigger functions as a fail-safe for the primary one. When the primary trigger is not activated, a government committee analyses the results from the annual Integrated Food Security Phase Classification. If food insecurity on this classification reaches a certain threshold in one of the target areas, the committee can decide (or not decide) to scale up the regular Fund programme (World Bank, 2018).

Finally, there is significant value in ensuring that any triggering system maintains a certain level of simplicity and transparency. Only when all concerned parties – who may often not be deeply familiar with the technical intricacies of trigger design – are familiar and comfortable with the trigger, will they accept the implications of its use. Besides, simplicity and transparency also enable external scrutiny, which can lead to constant improvement of the mechanism.

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