CIF CLIMATE INVESTMENT FUNDS

Investing in the future

Meeting of the SCF Trust Fund Committee

Washington D.C. (Virtual)

Friday, June 25, 2021

SCF RISK REPORT

SUMMARY

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SCF/TFC.15/4
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PROPOSED DECISION

The SCF Trust Fund Committee reviewed the document, SCF/TFC.15/4, *SCF Risk Report*, and welcomes the progress that has been made in advancing the work of SCF.

The SCF Trust Fund Committee requests the CIF Administrative Unit to continue to identify, assess, monitor and report the key risk exposures to the program.

1 Introduction

1. CIF recipient countries continue to struggle due to the ongoing global and local economic challenges posed by the COVID-19 pandemic (the pandemic), and this is also impacting projects currently under implementation as well as projects in the CIF's programs' pipelines.
2. Developing countries including some CIF recipients, were already heavily indebted coming into the pandemic and face acute fiscal and monetary constraints to buffering their real economies from the adverse effects of travel restrictions, lock downs and social distancing measures put in place to limit the pandemic. Additionally, the risk remains heightened of governments in developing countries recalibrating their budgetary priorities away from funding climate-related projects as they focus on addressing the effects of the pandemic on their economies and fiscal sustainability.
3. All CIF programs continue to face heightened credit, market and operational risks due to the impacts of the pandemic. More specifically, the CIF Administrative Unit has observed numerous impacts of the pandemic on CIF projects' implementation, and CIF recipients' financial strength.

   - **Delays in project implementation:** Travel restrictions and lockdowns have impeded and continue to impede the ability of consultants to get to project locations, workers to perform the necessary works to implement projects, and stakeholders to engage. Supply chain disruptions are delaying or preventing the procurement of essential equipment and supplies. Much of the time, only certain aspects of a project are delayed without causing an extension in the overall implementation timeline, however, in many cases, extensions of up to 24 months and/or project restructurings are required. In rare cases (so far) projects have been cancelled altogether. Target dates for funding approvals have also been extended. For reflow-generating projects, these factors in turn delay disbursements and the timing within which reflows from these projects will be realized.

   - **Economic impacts:** The pandemic has depressed economic activity in most countries globally, with magnified effects in certain countries which are dependent on more vulnerable industries (e.g. travel and tourism). This has substantially weakened the fiscal strength of many countries, damaged the financial strength of many of CIF private sector recipients and industries, and created great financial uncertainty.

     Credit rating agencies have downgraded many of CIF's publicly rated recipients, citing the pandemic as a contributing factor. Consequently, for CIF public sector loan recipients, the expected losses implied by their credit ratings has increased. However, given CIF's experience to date with public sector borrowers (i.e. no defaults have been reported on CIF's public sector loans despite the fact that several of CIF's borrowers have defaulted on obligations to various bondholders) the CIF Administrative Unit believes that these credit rating downgrades are less of a concern than the risk of public sector funding recipients focusing their resources and efforts away from climate-related priorities in order to deal with the fallout from the pandemic in other areas.

     Additionally, the economic uncertainty resulting from the pandemic has had a chilling effect on the appetite for green finance in the private sector. Financial Intermediaries

(FI) are reporting sharp declines or even a complete cessation of green finance lending for mitigation finance, including renewable energy and energy efficiency due to the current economic uncertainties attributed to the pandemic. Some projects involving power purchase agreements (PPA) with either privates from retail or tourism sectors or public utilities are suffering from delays in construction, with various private investors deciding to retain cash rather than approve investments. Such projects are also experiencing payment delays via PPAs due to the economic slowdowns.

4. Additional potential impacts include:

    a. Increased demand for more concessionality by MDBs and funding recipients for pipeline projects, including requests to convert non-grant financing instruments into grants; and

    b. Altered timing of repayments from loan recipients due to loan restructurings to allow for longer grace periods and maturities.

5. On the brighter side, vaccines have now been developed and are being distributed to combat the pandemic. The CIF Administrative Unit anticipates that some of the impacts on project implementation will abate as COVID-19 vaccines become more widely available. Implementation delays due to travel restrictions, lockdowns and supply chain disruptions should decline. However, the rollout of vaccine distribution and administration has been very slow in most developing countries, and, for this reason, although the CIF Administrative Unit expects these implementation delays to improve, they will likely persist for at least the next 24 months.

6. In the meantime, improvements will depend on the frequency and severity of pandemic surges in recipient countries, as well as vaccines' efficacy against newer strains of the virus as these strains continue to develop.

7. The CIF Administrative Unit expects the economic impacts and impacts on the credit quality and financial strength of funding recipients to persist for longer. In the past, individual public sector recipients have had to refocus their budgetary priorities away from climate-related initiatives in response to more localized natural disasters. The pandemic has been global in nature, and the CIF Administrative Unit believes there is a risk of more widespread budgetary recalibrations to address the impacts. The decline in private sector appetite for green finance is likely to persist well beyond the next 24 months.

2 Assessment of key risk exposures — FIP

8. The following matrix summarizes FIP's key risk exposures.

Summary Risk Matrix - FIP			
Risk	**Likelihood**	**Severity**	**Risk Score**
Implementation Risk	Likely	Moderate	High
Currency Risk	Likely	Moderate	High
Resource Availability Risk	Possible	Minimal	Low
Credit Risk	Possible	Moderate	Medium

9. Implementation risk for FIP remained **High**, as four out of 42 MDB Board-approved projects representing USD 65 million (9 percent) of program funding have been flagged for this risk. The program's implementation risk score has been **High** for the past three reporting cycles, and **Medium** for the four reporting cycles prior to that.

10. Although the appreciation in the GBP caused the unrealized decline in the value of FIP's uncashed promissory notes decreased to USD 21 million from USD 33 million as reported FIP's exposure to currency risk remains **High**. GBP 131 million promissory notes remain outstanding. The program's currency risk score has been **High** for the past seven reporting cycles.

11. Resource availability risk remains **Low** as FIP now has a surplus in both grant and capital resources. The program's resource availability risk score was **Low** in the last reporting cycle and **Medium** in the cycle before that, and had been **High** for the prior four reporting cycles.

12. Expected losses associated with committed loan portfolio are USD 24 million and the credit risk associated with the program remains **Medium**.

3 Assessment of key risk exposures — PPCR

13. The following matrix summarizes PPCR's key risk exposures.

Summary Risk Matrix - PPCR			
Risk	**Likelihood**	**Severity**	**Risk Score**
Implementation Risk	Possible	Minimal	Low
Credit Risk	Possible	Severe	High

14. Implementation risk for PPCR decreased significantly from **High** to **Low**, as 1 out of 65 projects representing USD 10 million of MDB-approved program funding was flagged for this risk. The program's implementation risk score had been **High** for the prior six reporting cycles.

15. Expected losses associated with committed loan portfolio are USD 66 million and the credit risk associated with the program remains **High**.

4 Assessment of key risk exposures—SREP

16. The following matrix summarizes SREP's key risk exposures.

Summary Risk Matrix - SREP			
Risk	**Likelihood**	**Severity**	**Risk Score**
Implementation Risk	Likely	Severe	High
Currency Risk	Likely	Moderate	High
Resource Availability Risk - Sealed and Reserve Pipelines	Possible	Moderate	Medium
Resource Availability Risk - Sealed Pipeline Only	Unikely	Minimal	Low
Credit Risk	Likely	Moderate	High

17. SREP's risk score for implementation risk increased and remains **High**. Seven projects out of 46 projects representing USD 106 million (14 percent) of program funding flagged for this risk. The program's implementation risk exposure was also **High** as of the last reporting cycle, and has fluctuated between **Low** and **Medium** for the five reporting cycles before that.
18. Currency risk for SREP remains **High** as GBP 94 million promissory notes remain outstanding and have declined in value to USD 18 million. The program's exposure to currency risk via promissory notes has been **High** for the last five reporting cycles.
19. SREP's risk of being unable to fund all projects in the combined sealed and reserve pipelines declined to **Medium**, however there is **Low** risk that SREP will be unable to fund the projects in its sealed pipeline. The program's resource availability risk exposure for the combined sealed and reserve pipelines has been **High** for the last six reporting cycles.
20. Expected losses associated with committed loan portfolio are USD 25 million and the credit risk associated with the program remains **High**.