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Independent observer of the Global Fund

it's Time to Soften the Comprehensive Funding Policy

The Global Fund board looks all set for a difficult discussion about Round 5 next week. What are the factors?

First, precedent: Until the last board meeting, the Fund has always launched a new round of grants every second board meeting – that is, every eight months. According to that schedule, the board should have agreed in June to launch Round 5 two months ago. If, at next week's meeting, the board delays Round 5 until some unspecified future time, it will anger many, particularly the 52 countries that the board encouraged to improve and resubmit their Round 4 proposals in the next Round. (Those proposals alone had a 2-year value of $980 m.)

Second, capacity: As quoted in this issue of GFO, the US says “We do not believe the Fund currently has the capacity to support another round of grants”, yet Brad Herbert, the Fund's Chief of Operations, says “it's a board decision when and how we initiate a Round 5. But the Secretariat will have no problem implementing it”. And in July, Richard Feachem told GFO, “One of the strongest messages to emerge at the Partnership Forum was the urgent need to launch Round 5 immediately following the board meeting in Arusha in November. While recognizing the need for financial prudence, I fully support this call.”

Third, money: The Fund calculates that if pledges for 2005 are approximately what they will be for 2004, there will be about $400 m. available for Round 5 grants next year (significantly less than the Round 4 cost of about $1,000 m.). Tht's true. But a continuation of those assumptions into 2006 shows that the Fund will then be $1,100 m. short of cash in 2006, because the cost of renewing Round 1-4 grants really escalates that year.

The “precedent” factor says the Fund should belatedly agree this month to launch Round 5 in January, one year after Round 4. The “capacity” factor says the same, if one accepts Herbert's analysis. But the “money” factor seems to say No – hold on to any cash generated in 2005 in order to help cover the 2006 renewals. To put it another way: as things stand, the Fund can’t really afford Round 5 until 2007.

However, all this assumes that the Fund continues to follow its current financial rules, known as the Comprehensive Funding Policy. This policy says that before a 2-year (Phase 1) or a 3-year (Phase 2) grant agreement is signed, the Fund must put the entire cost in the bank, and that money cannot be used for any other purpose. The money then sits idle for up to 3.5 years.

As a result, by some time in 2006 the Fund will have about $3 billion in the bank to cover Round 1-4 commitments. Those who wish to apply in the next Round will be told “There are billions in the bank, but we can’t launch a new Round.” And potential donors will be told “There are billions in the bank, but we desperately need more money.” This situation is not only un-productive, it is counter-productive. It harms the Fund.

The Comprehensive Funding Policy is a conservative approach that was perfectly appropriate when the Fund was new. But the Fund is now approaching its third birthday, and it’s now both possible and appropriate to soften the policy.

A comparison with the private sector is instructive. If a billion dollar corporation signs multiple contractual obligations (e.g. property leases, employment contracts) that commit it to pay money over three years, the CEO would be fired if he insisted on placing all the required money in the bank at the start of the three years. Good financial planning would say that the percentage of the contractual obligation that is locked up in the bank should decrease as the corporation matures, i.e. as it is able to develop estimates of likely future revenue.

Time is short, because the Global Fund board has engaged in its own form of denial by never seriously discussing resource mobilization challenges.

At its meeting this month, the board should commission an urgent study of the financial consequences of the Comprehensive Funding Policy, and of changes that the Board might make to that policy. The study should be completed in time for board committees to review it prior to the March 2005 Replenishment Conference and the April 2005 Board meeting.

The study should be carried out by a major financial services firm. It should examine what is typically done when major corporations, and major inter-governmental institutions, sign obligations to make payments over multiple years. In particular, it should examine what factors determine the percentages of those future obligations that those institutions believe must be locked up “in the bank”.

The study should end with recommendations for what the Global Fund’s evolving policy on this should be as the Fund matures yet further.

One path that the Fund currently faces is for next week’s board meeting to commission this study and to agree on a January launch of Round 5; for the April board meeting to agree, based on the study, that a portion of the money that will otherwise be locked up in the bank to cover future obligations can be used to fund Round 5; and then for the July board meeting to approve Round 5 grants worth a billion dollars.

The other path forward is for the board to put aside the vision set out by Kofi Annan, and to turn the Fund into a modest-sized agency preoccupied over the next two or three years with no more than raising and disbursing money to complete grants that have already been started.

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