Strategic Risk Management for Development NGOs: The Case of a Grant-maker

by Ricardo Wilson-Grau

Introduction

The global environment in which nongovernmental organizations (NGOs)[1] operate is changing quickly, as is the very nature of the risk management function and the process for making decisions about risk. These changes affect not only NGOs and the public that is served, but also the organizations that fund them. Keeping pace with changes in the overall economic, political, and cultural environment in risk management practice and in leading thinkers' understanding of risk is vitally important to every NGO's success in carrying out its mission and accomplishing its long-term goals. That is, managing risk is a strategic challenge today.

Recent advances in the global understanding and management of risk open opportunities for grant-making NGOs to improve their process of funding NGO grantees. The grantor can enhance its own and its grantees' performance by applying sound, consistent strategic risk management. The recipient organization will achieve more and ultimately, so too will the world these organizations strive to improve.

The first part of this article describes how strategic management of risk can make a difference to organizational operations in the fast-paced, demanding environment of development NGOs. The second part draws on the experience of a major Dutch private donor NGO to exemplify applying strategic risk management to the grant-awarding process.

Overview of NGO Strategic Risk Management

These are hard, challenging times for NGOs around the world. Whether service or social change oriented, NGOs operate in dynamic economic, political, technological, and institutional environments. For NGOs devoted to development in both the North and South, with increasing frequency, their legitimacy is questioned and accountability demanded. Stakeholders and the broader society and governments are frequently asking NGO leaders about their impact on society?

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These changes require that NGOs modify how they respond to the world and seek to shape it. Consequently, many development NGOs are altering their strategies, as the shift to rights- and results-based approaches exemplifies. Moreover, they are varying their strategies more frequently than in the past. Change, of course, has always been important in every organization's life. Indeed, for NGOs, change is absolutely essential; every NGO's mission statement commits it to improving some unacceptable aspect of the world. Change, however, brings with it uncertainty and risk.

Risk—The Simple and The Complex

The root word of risk, *risicare*, means "to dare." Daring to act audaciously is inherent to the lives of NGOs. Without taking risks, there is no innovation or social change. The nature of NGO work is to dare constantly to make decisions and act to achieve positive results, while daring to hazard bad outcomes. One of the beauties of the risk concept is its simplicity. As with anything occurring in the future, there is uncertainty about the results, desirable or undesirable; there are *consequences* of each good or bad result; and one needs to focus on the *probability* of positive and negative results. Of course, life cannot be so simple. There is an equally important and much more complex dimension to risk. Individuals, organizations, and societies are all unique. Thus, risk is rooted in specific historical contexts—from the political and psychological to the economic and environmental—that shape people's perceptions of the consequences and the probability of an uncertain event.

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Even in situations where there is a precise mathematical calculation of probabilities, people will act on their *beliefs* about the chances of good and bad results. Similarly, people take action based on their *preferences* for one result over another, even when they know precisely the potential benefits. Of course, when a judgment is about the uncertain future results of social change, the decision is especially subjective and risky.

Risk management is relatively new for NGOs. One reason is the ease NGO decision-makers have in confronting operational hazards that only one hundred years ago would have been terrifying. Insurance controls the damage caused by illness or accidents. Personnel access loans in case of personal or family emergencies. The dangers of disaster that come with all new technology are more readily mitigated than ever before, as when NGOs use virus shields and back-up systems to protect computers against electronic attack or human error.. A second reason is that applying risk management to achieving upside results, and not solely avoiding the downside ones, is a recent innovation. In today's highly competitive and unpredictable environment, NGOs not only face major opportunities and new dangers to achieve their missions, but these positive and negative risks are arising much more rapidly than in the past and are becoming more complex. They must be managed as never before. Consequently, NGO decision-makers that use strategic risk management may actively nurture success and counter threats of failure.

The Emerging Concept of Strategic Risk Management

In the last ten years, the concept of risk management has expanded from its origins in the insurance industry. It has extended into the fields of investment finance, medicine, environmental management, space science, and meteorology. Today, business and local and national governments apply risk management principles. The theory and practice has also grown from its original focus on exposure to negative risks to address positive risks as well. Building on traditional risk science, strategic risk management centers on a reinforcing, iterative process, a recycling sequence of steps for making and implementing decisions involving potential bad or good results.

- Clarifying what the organization seeks to achieve—*goals*.
- Identifying the principal opportunities and dangers that may affect achieving these goals—*uncertainties*.
- Assessing the likelihood that each opportunity or threat will materialize—*probabilities*.
- Calculating the extent of the resulting gain or loss to the organization from each opportunity or danger—magnitudes of the good or bad *consequences*.
- Weighing what the organization can do: 1) to increase the probability and the magnitude of the good consequences of each opportunity, and 2) to decrease the probability and the magnitude of the bad consequences of each danger—*risk management techniques* for each opportunity or threat.
- Deciding whether and how the organization is able to take these actions—*costs and benefits* of each technique.

This definition of risk is powerful. Instead of struggling to avoid all uncertainties—for that would be to avoid all chances of positive outcomes—an organization strives to increase the chances and size of positive outcomes while reducing the odds and magnitude of the negative outcomes. *This dual strategy is the essence of strategic risk management*. It contrasts with the narrow, negative traditional focus—merely preserving the organizations past achievements from future losses. While guarding against loss, the NGO that manages risk strategically takes carefully chosen chances, purposely mindful of the positive side of a potentially surprising future. An organization managing risk strategically dares to succeed.

A Tool for NGO Decision-makers

In recent years around the globe, NGO organizations that are committed to social change have strengthened their professional management to achieve their missions and long-term goals. NGO leaders once could safely assume that internal and external conditions with a potential major impact on their stakeholders, programs, property, income, and reputation would be stable for a year or two. No more. Currently and even more so in the future, the strategy is short term. For example, one major innovation in NGO management has been to introduce systems of strategic planning. Commonly, NGOs engage every three, four, or five years in this fundamental decision-making for achieving institutional goals. Increasingly, however, change is so rapid that managers at all levels of the organization must make decisions vital to achieving their missions outside the multi-year cycle. Now, monthly and even weekly, an NGO's entire management must adapt to and participate in incisive strategic thinking and prompt strategic action. In fact, virtually everyone in an NGO must continually understand, accept, and participate in actions sharply focused on achieving their organization's fundamental purpose and goals.

This is easier said than done. Organization-wide involvement with uncertainty can create feelings of apprehension and insecurity. Strategic risk management offers a tool to build understanding and enthusiasm for change. From the broader perspective of risk as *risicare,* an NGO's staff comes to understand that changes—some bad, some good—are not only inevitable, but the organization can thrive with these changes. Everyone comes to recognize that change, properly anticipated and wisely managed, while still posing possible dangers, is a potentially positive force. Uncertainty becomes something with an upside and a downside, something that can be managed not just by decreasing the potential for losses, but also by increasing the potential for gains.

Empowered by this broadened approach to uncertainty and change, an NGO's personnel quickly think beyond the merely negative, accident-centered, insurance-oriented concept of risk. Recognizing that changes can be positive, even surprisingly good and certainly necessary, an organization's staff can come to work with risk as an opportunity to achieve positive outcomes, daring to succeed as well as to fail.

Capacity-building Through Strategic Risk Management

Strategic risk management can enhance but never replace a development decision-maker's knowledge, field experience, cross-cultural skills, and other personal abilities. More specifically, strategic risk management enables NGOs to enhance their capacities in three areas.

Information. In management, the information function is vital. In today's "knowledge societies," decision-makers are flooded with data and ideas. The technological possibilities are a temptation to nurture a false sense of security by attempting to process all available information. Of course, managers must constantly observe, consult, read, and listen. Strategic risk management, however, offers NGO decision-makers a methodology for rapidly sifting through and selecting the most relevant information.

Action. Today, NGO managers must combine hard, in-depth analysis with fast decisions. Risk management enables a decision-maker to act even as she or he thinks. Past successes and failures are analyzed not so much to know what happened or to explain why things are as they are, but primarily to take the best decision about new activities. Exercising risk principles enables a decision-maker to identify what to change and innovate in order to maximize gains and minimize losses today, tomorrow, and in the future. For strategic decisions, certainly the search for truth must be rigorous. Strategic risk management incorporates the rational perspective of science, but the purpose is to understand in order to decide, to set objectives and make plans, but not at the expense of acting on them.

Delegation. Never before has the need for subsidiarity been greater for development NGOs. Strategic risk management facilitates delegation because risk principles are applicable at all organizational levels. Strategic risk management enables decision-makers to spread authority and responsibility upwards, downwards, and across. Everyone can be engaged in taking risks responsibly to achieve their work units' "missions" or long-term goals. Thus, for instance, in an organization where everyone uses a risk approach, senior program managers with substantial field experience will be able to delegate with greater confidence to junior staff. In addition, a quick-learning, self-critical program staff will develop faster.

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In sum, traditional and strategic risk management both emphasize a proactive attitude towards risk-taking and employ similar methods of analysis and techniques for coping with risk. All risk-taking is based on logical analysis of essential information. Risk decisions also involve strongly reasoned beliefs and preferences about the probability and the importance of the desirable and undesirable outcomes. Thus, the advantages of both traditional and strategic approaches to risk combine art and science, integrating reasoning with intuition. The fundamental difference is that traditional risk management focuses on *only* threats of loss; strategic risk management encompasses *both* opportunities for gain and threats of loss. At best, traditional risk management can only keep an organization where it now is; strategic risk management enables an organization to advance and develop its potential.

Strategic Risk Management and Grant-Making at Novib

Founded in 1956, the Netherlands Organization for International Development Co-operation (Novib/Oxfam Netherlands) is a non-governmental foundation funded by the Dutch government and public. Novib's purpose is to encourage a world community in which socio-economic contradictions between rich and poor are eradicated, the wealth of the world is more justly divided, and people and population groups can learn about and come to respect each other's cultures, and in the interest of their own development, cooperate on the basis of shared responsibility and mutual solidarity. Furthermore, Novib is a member of Oxfam International, a confederation of 12 organizations[2] working together with over 3,000 counterpart organizations in more than 100 countries to find lasting solutions to poverty, suffering and injustice. As do all the Oxfams, Novib takes a rights-based approach to achieve structural, enduring improvement in the quality of life of people. Every NGO must customize its use of strategic risk management in accordance with its mission and long-term goals, which pose special challenges for an organization that approaches grant-making from highly political and normative perspectives.[3]

Grant-making Guided by Organizational Values Rather than by Partisan Ideology

Novib works for changes in policies and their corresponding practices to modify the structures and relations of power that are obstacles to people exercising their political, civil, economic, social, and cultural rights. In every society and community, access and control of resources are structured in ways that benefit some individuals and groups and discriminate against others. Thus, the key to success of a rights based-approach to development and social justice is empowerment. Citizens and social organizations obtain the capacity to be significant actors in a process to change the structure and relations of power to benefit the many and not just a few dominant sectors. To contribute to these ends, Novib applies three institutional strategies.

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First and foremost, Novib is a donor to approximately 850 local organizations in more than 50 countries in Africa, Asia, Latin America, the former Soviet Union, and Eastern Europe. These grantees are NGOs who work directly with and for the poor and disenfranchised. The aim of this cooperation is to increase the capacity of people to exercise their individual and collective rights and to make decisions about control and use of material, human, intellectual, and financial resources. The support, however, is purely financial. Novib believes that because of the power of money, a donor-recipient partnership may be undermined if the grant-maker also attempts to provide these organizations with professional or technical assistance on ways and means to improve their performance. It can easily lead to dependence, disempowerment of the grantee, and strategic or organizational problems.

Second, Novib strives to inform Dutch public opinion. It educates the Dutch public about the non-Western world by challenging conventional images and encouraging deeper insights concerning development. Novib also tries to make the cultures of the South accessible to the Dutch public through, for example, publishing books written by southern writers. Novib promotes the personal involvement of Dutch individuals and organizations in actions such as fair trade aimed at a more equitable distribution of the world's resources. Third, with the other Oxfams, Novib defends the interests of developing countries in the political and economic power centers of the West and tries to influence policy decisions in favor of the world's poor.

Novib bases its core work of grant-making on a strongly normative approach to development as cooperation between independent social actors. Institutional autonomy, mutual accountability, consultative decision making, and transparency between donor and grantee are the four pillars of Novib's relationships of development cooperation. Novib channels well over 80 percent of its annual budget of US$170 million to fund like-minded counterpart organizations. Novib does not make grants to individuals. The average annual value of a grant is around US$150,000, and Novib is highly flexible in its funding. Grantees largely decide where Novib's donation can do them the most good. In addition, Novib strives to fund its grantees in three-year cycles and frequently, for nine or more years. In the rapidly shifting environment of international development cooperation, however, throughout each year staff increasingly face strategic choices about what grantees to fund.

In a Changing Political Environment, Novib Applies Strategic Risk Management to Appraising Grants

As is the case with NGOs around the world, Novib's stakeholders increasingly expect to know what has been achieved with their support and involvement. Furthermore, Novib now competes for funding from its principal donor, the Dutch Ministry of Development Co-operation, based on the quality of results and not solely on professional grant-making. Consequently, since 2000, Novib has given much more emphasis than before to the results it strives to achieve. To this end, Novib is applying strategic risk management in a variety of areas of operational decisions. The principal area is grant appraisal.[4]

Novib realized that if grantees and Novib itself only practice traditional risk management, then Novib's grants might be relatively safe, but the potential for more significant impact in a rapidly changing environment would be limited.

In 1980s and 1990s, the quality of the partner organization was the guarantee of positive results. Novib approached this challenge with a checklist of what it considered good grantee practice. That instrument was designed to provide a reading of the health of an organization and the quality of the project it proposed that Novib fund. Novib's rationale was that the closer a grantee was to standards of organizational excellence, the more likely the grant would be used wisely and the project successfully implemented. Solidarity, the right strategy, and excellent management continue to be important but are no longer sufficient. Novib and its grantees must demonstrate impact. Committed to this demanding task in often volatile circumstances, Novib realized that if grantees and Novib itself only practice traditional risk management, then Novib's grants might be relatively safe, but the potential for more significant impact in a rapidly changing environment would be limited. To increase the magnitude of the results, Novib understood that it must dare to manage risks strategically and not bureaucratically if it were to contribute to development. Novib decided that the emerging concept of strategic risk management would offer an especially appropriate tool for managing its grant-making. This methodology permits holistic, non-linear and dynamic analysis and decision-making about the potential for results. Consequently, from 2001 to 2003, Novib researched and developed a grant appraisal methodology grounded in risk management science. From August 2003 through February 2004, Novib field-trained over one hundred of its grant makers and managers in the new methodology.

The Appraisal Product—Judgments

In Novib, a team of two to three program officers, a financial officer, and a team secretary are responsible for the Novib portfolio in a country or region. They use an appraisal manual, the "Toolbox," to support them in formulating their risk judgments. The product—their strategic risk appraisal—is a narrative document of four to eight pages with three components.

1. The upside risks: the opportunity for cooperation

The starting point is the congruence between the positive *results* a grantee wishes to achieve and one or more strategic objectives of Novib for the country or region. The Novib team identify and interpret what the grantee wishes to achieve that will improve the quality of life of sectors affected by economic, social, and political inequality. In particular, the team explains what it believes is the potential contribution to changes in policies and practices.[5] They also identify other positive *consequences* or "added social value" of the grantee's activities.

The positive consequences are the most important but not the only element of the opportunity for co-operation and for Novib to provide funding. The amount and duration of the grant also depends on the *probability* of success. Thus, the team looks hard at the counterpart organization's resources and track record and at the environment in which it operates. It identifies the capacity that the grantee has demonstrated to achieve similar results and to manage change. Furthermore, the team takes into account favorable external social actors and factors. With this foundation, the team formulates its judgment about the probability of this organization achieving its results.

2. The downside risks: the principal dangers to success

The second component of the appraisal is the down-side risks or threats that endanger the success of the opportunity. Novib calls these "principal dangers." They are the risks in which the probability of occurrence and potential negative impact could undermine a grantee's ability to achieve the results. Equally important, the team explains how the grantee proposes to manage these "mortal" risks to success.

3. The upside-down risks: changing opportunities and dangers

Risk exposure to both positive and negative results must be managed into the future and this, of course, is the grantee's responsibility. The project proposal is essentially a plan for the management of the positive risks. The grantee informs Novib how it will manage the negative risks. Together, they agree on an agenda to monitor and review progress towards the results and the control of the principal dangers. This annual reflection analyzes how the opportunity and dangers may have changed, but also identifies new opportunities and emerging threats for the coming year. In sum, the content of the appraisal highlights the positive risks and the opportunity to contribute to significant social change. The negative risks are those that endanger success.

The Four-step Appraisal Process—Engagement and Dialogue

Novib's grant appraisal methodology is based on mutual respect between Novib and its grantees and a sound understanding of each other's expectations and needs. A program officer and the officer's team quickly confirm a promising opportunity (and weed out others). They analyze only the important obstacles to success and make decisions using judgment and reflection, as well as facts and figures, all in consultation with the grantee. The risk appraisal enables Novib staff and grantees to negotiate agreements about enhancing the opportunity to cooperate and mitigating the dangers to the success of that cooperation.

1. The pre-assessment team meeting

First, Novib communicates to all applicants that Novib supports grantees that take risks in seizing new opportunities to achieve their social change goals. Upon receiving a project proposal, one team member, usually a program officer, decides or confirms in the case of a current grantee if the project proposal meets Novib's minimum criteria.

- Fits within Novib's grant-making strategy for the country or region.
- Is compatible in terms of organizational purpose and values.
- Fulfills minimum administrative and financial standards, such as being a legally constituted NGO organization with a bank account.

If the team agrees in principle to appraise the organization and its proposal, the program officer in the lead prepares a draft appraisal for discussion by her team with the information at hand. This includes the grantee's proposal and for current grantees, evaluations, annual reports, audits, and field visit notes.

Experience to date is that key additional information is always required. For example, usually there is a lack of clarity about the intended results of the grantee's activities. In Novib's case, this is especially true concerning potential policy and practice changes. Of course, the use of a risk appraisal methodology also requires a change in mindset within the Novib team. For instance, the previous appraisal methodology was calibrated to identify problems and set conditions, not embrace positive and negative risks.

2. Visit to the grantee

Generally, not all the missing information can be obtained through correspondence. The customary emphasis by donors is on what the grantee is going to *do* with their grant. Novib's new focus on what is to be *achieved* and on the results represents a new dimension to the donor-grantee relationship and requires face-to-face dialogue. Therefore, the team crafts the questions that one or two program officers, sometimes accompanied by the financial officer, pursue during the visit to the organization. They begin with a morning or afternoon of questions and answers to gather information. The grantee's director, senior management team, and board members, occasionally, are present.

In the following day or two, the program officer (and other team members if present) completes the draft appraisal and presents it to the grantee. The grantee reads and discusses internally the appraisal before another session with the program officer(s). In the second half-day meeting, it is the grantee's turn to ask questions, correct misinformation, and comment on the analysis in the risk appraisal. They wrap up discussing how the grantee will manage the negative risks.

The visit is the central event in the appraisal process. The face-to-face critical dialogue is sharply focused on the political dimension of the cooperation—what both NGOs aim to change in society. In the first year, Novib applied the risk appraisal methodology to project proposals from almost 200 NGOs in countries with a wide range of political, economic, and cultural diversity. Around the world, grantees and Novib staff alike consistently consider this respectful, transparent discussion in a spirit of conscious risk-taking and mutual accountability to be the most valuable part of the new methodology. They are able to counter together the pressures for donors to subcontract for results and for grantees to play cat and mouse in order to preserve their institutional integrity. Grantees learn why Novib is supporting (or not funding) a project, as well as Novib's hopes for and concerns about their projects. Novib learns about the fundamental challenges the NGO counterpart faces in achieving significant social change.

3. Team discussion and decision

The program officer responsible submits to the team the appraisal and a ten to twenty page description of the grantee. The two documents—one part analysis and the other part facts and figures—complement each other. The program officer has sifted through considerable amounts of information, has analyzed that which is essential to understand the opportunity for cooperation, and made judgments about the impact and likelihood of both success and failure. All of this has been done in consultation with the NGO grantee. Therefore, the team does not repeat or simulate the process of appraisal. Instead, colleagues enrich the quality and coherence of both products.

In making their decision to fund, the team members go beyond examining the probability and the importance of potential structural, sustainable changes in the lives of people represented by the project to be funded. They strive together to strengthen, integrate, respect, and accept responsibility for Novib's and the grantee's necessarily different but convergent views.

4. Follow-up and review

The Novib methodology stipulates a review of the opportunities and dangers at least once a year. The grantee and program officer discuss the grantee's experience in the past twelve months in working towards achieving the results and managing the principal dangers and the implications for opportunities and dangers in the second year. The review also looks forward: How has the opportunity changed? Are there new opportunities that may deserve higher priority? How have the threats changed? What new action is required to manage them?

CONCLUSION

Novib discovered in strategic risk management a method to assist in making decisions about grants for social change. Thus, the methodology is politically but also result oriented. Equally important, each party's institutional autonomy is respected. There is mutual accountability, consultative decision making, and transparency between donor and grantee. Furthermore, Novib enhances its ability to demonstrate the impact of its grant-making.

NGO grant-makers and their NGO grantees have a symbiotic relationship in an uncertain world filled with both opportunities and dangers. For either to succeed, both must succeed. Thus, they have a shared interest in their own and each other's effective strategic management of risk in order to advance toward their full potential contribution to people everywhere, exercising their rights and achieving social justice and sustainable development.

Notes

[1] Also known as nonprofit, voluntary, grass-roots, community-based or civil society organizations.

[2] The current Oxfams are based in Australia, Belgium, Canada, Germany, Great Britain, Hong Kong, Ireland, Netherlands, New Zealand, Quebec, Spain, and the USA.

[3] Novib is a NGO hybrid quite common in Europe. As a private donor, it is comparable to the Ford Foundation. Since Novib receives two thirds to three-fourths of its funding from the Dutch government, it is analogous to the InterAmerican Foundation funded by the US Congress. Furthermore, as an advocacy and campaigning organization, Novib is similar to Amnesty International or Human Rights Watch. Novib is not, however, operational. It does not implement development projects.

[4] In addition to grant appraisal, Novib uses risk methodology to: 1) select countries and prioritizing themes for funding; 2) assess opportunities for cooperation with corporations and local government in campaigning, advocacy, and special projects; and 3) evaluate regional and country programs.

[5] Policy changes are modifications of formal or informal, written or unwritten political, cultural, social or religious norms that guide the actions of people, organizations, and institutions in the sphere of the state, the market as well as in civil society. Changes in practice represent a modification of what is done in society—the laws or regulations must be applied or new socio-cultural norms practiced.