Promoting Private Sector Investments in Sustainable Forestry

Initiative on Financial and Institutional Risk Mitigation and Management Strategies

Concept note
Context

While private capital is available for investments, the forest sector still lacks significant funding for the development of key areas of intervention such as forest plantations, natural forest management, small and medium forest enterprises, local and community forestry, and large-scale forest investment projects including REDD+. Underlying efficient business models can bring substantial financial returns to investors in all these activities, but many traditional investors are still reluctant to invest.

One of the barriers to more private investments is the wide range of (real and perceived) risks associated with forestry. Political, socio-economic, market, weather and climate risks are some of the reasons why investors hesitate to invest in the sector. According to FAO and GM-UNCCD (2015) more than USD 300 billion are needed per year by 2030 to achieve the land degradation neutrality target (SDG 15.3) for which the forestry sector will be a major contributor. However, in the absence of suitable risk mitigation and management strategies, it will be difficult to mobilize the scale of resources required.

While some risk mitigation and management strategies exist at the organizational level and at the biophysical level (e.g. resistant and resilient tree species, mixed cropping systems, climate change adaptation strategies), at the financial and institutional levels they are still underdeveloped. Much less attention has been paid to the identification, development and application of these strategies.

Potential financial losses at stake in the forest sector are manifold: loss of capital (trees, soil, etc.), loss of revenues from wood and non-wood forest product value chains, default payments, and market and price fluctuations are some examples of risks that require mitigation. In this context, some of the existing key risk mitigation approaches worth exploring include: credit guarantees and credit enhancement, due diligence and assurance, portfolio diversification, private sector insurance (political and commercial risks), public sector insurance (political risks), securitization as well as the development of buy-back agreements. Other important approaches for reducing financial risks include related government policies (backed-up by laws) and investment support services to private stakeholders and partnerships or platforms for standardization of investment proposals. Further, relevant examples from agriculture and other sectors could also serve as good entry points for exploration and adaptation.

However, current information on existing as well as potential financial and institutional risk mitigation and management strategies in forestry is limited. Lack of opportunities for sharing of knowledge related to successful examples within and across nations is further constraining effective expansion and adaptation of suitable strategies elsewhere. The goal of the proposed initiative, being led by FAO and other development partners, is to specifically address this policy and knowledge gap. A wide range of stakeholders with interest and experience in mobilizing private sector forestry investments will be involved for the purpose.

Objectives of the initiative

The main objectives of the proposed initiative, which will be implemented in collaboration with various development partners and private sector organizations are:

- Review, analyze and identify potential financial and institutional risk mitigation and management strategies to scale up sustainable private sector forestry investments.
- Promote global, regional and national understanding/mainstreaming of identified innovative strategies.
- Drawing on the above inputs, develop policy and technical guidance on financial and institutional risk mitigation and management.
- Disseminate the guidance through relevant outreach platforms and capacity development efforts.

How is it linked to FAO strategy?

This work programme addresses the Strategic Objective 2 (SO2) “Increase and improve provision of goods and services from agriculture, forestry and fisheries in a sustainable manner”, the SO3 “Reduce rural poverty” and the SO4 “Enable inclusive and efficient Agricultural and Food systems” of the Food and Agriculture Organization of the United Nations. The initiative will also support mainstreaming the “Principles for Responsible Investment in Agriculture and Food Systems” that were approved by the Committee on World Food Security (CFS) in 2014. The importance of risk mitigation instruments for the forest sector was highlighted during FAO Heads of Forestry Dialogues at the Regional Forestry Commission meetings and also at various other international fora. In addition, FAO, as a key player in forest and landscape finance development (FAO Forest and Landscape Restoration Mechanism; Policy advice on National Forest Funds; National Forest Financing Strategies, Investment Centre, etc.), will further strengthen its technical assistance by improving knowhow and expertise on risk mitigation strategies and mechanisms.

Potential case studies

Among possible case studies to be presented and analyzed, some indicative examples include:

- Risk guarantee mechanism of private impact funds involved in Forest and Landscape Restoration (e.g. USAID and Althelia Climate Fund)
- Partial risk guarantee mechanisms of the Initiative 20x20 (e.g. CAF)
- Political risk coverage (e.g. MIGA and EcoPlanet Bamboo)
- Layered funds as financing tools mitigating risks for institutional investors (e.g. Finance in Motion)
- Risk mitigation through investment diversification (e.g. ForestFinance)
- Special risk insurance targeting the forest industry (e.g. Munich Re)

Additional case studies will be identified in order to have a representative and diversified range of know-how and experiences. Selection of case studies will be critical in order to conduct an effective mainstreaming of lessons learned and recommendations.

Proposed programme of work

The programme of work will be composed of a series of activities covering an overall duration of two years. Following steps are planned:

- Inventory of existing and potential strategies and instruments and the development of a background paper.
- Organization of a technical workshop with experts and practitioners with experience in financial and institutional risk mitigation strategies for the forest sector to further define the scope and direction of the initiative.
- Organization of two/three regional knowledge sharing/capacity building workshops, to share information and collect best practices/policies/programmes
- Drawing on the above inputs, develop a policy and technical guidance (a policy and technical publication).
- Provide technical assistance and capacity building support for the effective design and implementation of innovative risk mitigation strategies and related instruments in specific contexts (for interested organizations/countries).
- Develop and maintain a dedicated web portal for easy access and dissemination of information on all related knowledge products and activities.

Proposed timeline

<table>
<thead>
<tr>
<th>Main activities</th>
<th>Year 1</th>
<th>Year 2</th>
</tr>
</thead>
<tbody>
<tr>
<td>Inventory of existing and potential strategies (background paper)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Organization of the technical/ expert guidance workshop</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Organization of regional knowledge sharing and capacity building workshops</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Refinement and finalization of country case studies/best practices/policies/programmes</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Development of policy and technical guidance (Policy and technical publication)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Development of a community of practice and facilitating country/organization support</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Development and maintenance of a dedicated web portal</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Advisory Committee

An advisory committee composed of representatives from international organizations and development partners will guide the initiative.

Contacts

Mr Rao Matta (FAO) Rao.Matta@fao.org
Mr Ludwig Liagre (FAO) Ludwig.Liage@fao.org