# Incentivizing the Involvement of the Private Sector in REDD+

A review of early experiences and lessons learned in the Forest Investment Program

This document is based on consultations carried out in four (Burkina Faso, Democratic Republic of Congo, Indonesia, and Peru) of the eight countries receiving pilot support from the Forest Investment Program, a targeted program of the Climate Investment Funds, as well as desk reviews of public and other documentation from the programming process in all eight pilot countries.

## THE FOREST INVESTMENT PROGRAM

**Key lessons:**

- The Forest Investment Program's greatest value-added, in terms of incentivizing private sector involvement in REDD+, is its ability to invest in and finance advisory services in support of private sector activities.

The Forest Investment Program (FIP) is one of three strategic programs of the Climate Investment Funds (CIF). FIP provides developing countries with scaled-up financing to plan and implement readiness reforms and public and private investments, identified through national REDD+ readiness or equivalent strategies, while taking into account opportunities to help adapt to the impacts of climate change on forest ecosystems and to contribute to multiple benefits such as biodiversity conservation, protection of the rights of indigenous peoples groups and local communities, poverty reduction and rural livelihood enhancements. Projects supported under a country's FIP investment plan will pilot and scale-up replicable models for REDD+ interventions that improve forest management and reduce pressure on forest ecosystems.

FIP financing is channelled through the five multilateral development banks (MDBs) to public sector initiatives (as grants, concessional loans, and guarantees) and to the private sector (as grants, concessional loans/equity, and guarantees, with rates determined on a case-by-case basis following a principle of minimum concessionality[1]) to complement large-scale investments and leverage additional financial resources, including from the private sector.

FIP is unique among the four global multilateral REDD+ initiatives in its level of engagement with the private sector. The three other global initiatives are the UN-REDD Programme, the Forest Carbon Partnership Facility (FCPF), and the Global Environment Facility's SFM/REDD+ program. The framework/program documents of each initiative mandate the consultation of all relevant stakeholder groups in the process of developing national REDD+ policies and activities, with the private sector generally identified as one of those groups[2]. Most initiatives, including the FIP, go further and recognize the important role of the private sector both as a potential source of finance for REDD+ investments and as a group to target with information and REDD+ incentives, since deforestation and forest degradation can often result from decisions made by private sector actors.

[1] Climate Investment Funds (2010) FIP Investment Criteria and Financing Modalities

[2] UN-REDD Programme (2008) Framework Document; Forest Carbon Partnership Facility (2008) Information Memorandum; Global Environment Facility (2010) GEF-5 Programming Document

However, currently, only the FIP explicitly provides financing to invest in and provide advisory services in support of private sector activities that reduce emissions from deforestation and forest degradation and/or increase forest conservation, sustainable forest management, and the enhancement of forest carbon stocks.

Such REDD+ activities could include, among others, forest conservation, agroforestry, afforestation, reforestation, assisted natural regeneration, landscape fire management, improved agro-silvo-pastoral management, improved forest management (including reduced-impact logging, increased harvest rotation lengths, and forest pest management), increased efficiency of timber and wood processing, improved bio-energy production from forestry, and deployment of bio-energy appliances with increased end-use efficiency. Some of these activities can directly reduce deforestation and forest degradation and enhance forest carbon stocks, while others can reduce pressure on forests by providing markets and producers with an alternative and sustainable supply of products.

## THE PRIVATE SECTOR

**Key lessons:**

- The private sector is a heterogeneous stakeholder group, but actors from each subgroup are already playing a positive role in national REDD+ processes.
- Private actors in the real sector and financial sector will be targeted with FIP advisory services and investments, since transformation of their behaviour towards SFM and enhancement of forest carbon stocks, and away from deforestation and forest degradation, has a very large potential impact.
- Corporate social and environmental responsibility initiatives, philanthropic organizations, carbon developers, and private consultants already partner with and provide essential services to other public and private FIP stakeholders in support of REDD+ activities, and they are likely to continue their engagement through the implementation of FIP investments.

The private sector stakeholders that are involved in national REDD+ processes in FIP pilot countries are not homogenous. As with other development processes, their impacts and contributions will differ depending on their sector, type and size[3]. Private sector actors are already using various entry points in national REDD+ processes to get involved in the design and implementation of REDD+ activities.

One important segment of the private sector that could have a critical influence on the future of REDD+ is real sector companies. This group includes forestry companies and businesses across forest-product supply chains as well as agribusiness, mining, and energy companies operating in and around forests. Informal, small- and medium-sized producers, and community-based enterprises make up an important segment of the real sector. Eco-tourism companies, which may operate in forests, also fall in this category. Another important group is the financial sector-- private banks, investors, and financial intermediaries that provide loans and capital to the real sector.

Other for-profit and non-profit private actors provide financing as part of their corporate social and environmental responsibility (CSR) or philanthropy. A large for-profit multinational company is using its CSR investment fund to finance a forest carbon project in DRC that will generate carbon credits which it will use to voluntarily offset its own emissions. The project is a model that the DRC Government has learned from and plans to scale up with FIP investments. In Peru, a non-profit private foundation is co-financing seconded positions in a government agency that is responsible for aspects of the country's REDD+ strategy, including participation in their FIP inter-ministerial committee.

[3] Organization for Economic Co-operation and Development (2011) The Role of the Private Sector in the Context of Aid Effectiveness

Still others engage in carbon project development and finance. In Indonesia, a private company that has been engaged in the country's FIP investment planning consultations over the past two years is developing carbon finance projects that aim to reduce emissions from peat lands and generate carbon credits for sale on the voluntary carbon markets. In the Congo Basin Forest Fund example from DRC mentioned below, the implementing entity (a private company) is co-financing the pilot project and has already used forest carbon finance to develop projects that are now operating and producing credits.

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Private for-profit companies provide technical services to REDD+ stakeholders, including public, private, and non-governmental organizations. For example, the Government of DRC has selected a private company to be the implementing agency of a Congo Basin Forest Fund grant for a REDD+ pilot project. The explicit rationale was that the company has proven experience implementing forest carbon projects in the country[4]. The same private company has been actively involved in DRC's FIP preparation process. In Peru, an indigenous peoples organization has hired private consultants to advise them as they engage in the FIP investment plan consultations and other REDD+ processes. The Government of Peru has hired private consultants to assist with the preparation of their FCPF and FIP documents.

As indicated above, CSR initiatives, philanthropic organizations, carbon developers, and private consultants already provide essential services to both public and private actors engaged in REDD+ activities. Actors in these groups will very likely, through their own business interest, be engaged in the design and implementation of FIP projects.

Moving forward, the real challenge of the FIP will be to influence, through advisory services and market and financial incentives, the business behaviors of private actors in the real and financial sectors towards investing in sustainable management of forests and enhancement of forest carbon stocks, and away from activities that lead to deforestation and forest degradation.

## FIP-PRIVATE SECTOR PARTNERSHIP

**Key lessons:**

- The private sector is both an important potential source of finance for REDD+ investments and a group to target with REDD+ incentives.
- The FIP intends to leverage private sector financing with its own pilot-scale public financing and thereby scale up its impact.

The reasons for partnering with the private sector in REDD+ have been explored in other publications[5], but in the FIP's case its commitment to working with the private sector is a central component of its mandate. As mentioned above, the FIP recognizes the key role of the private sector both as an important potential source of finance for REDD+ investments and as a group to target with REDD+ incentives.

The intention to leverage private sector financing with FIP resources and thereby scale up the impact of limited, pilot-scale public funding is explicit in the FIP's foundational documents[6] .

[4] African Development Bank(2011) South Kwamouth REDD Agroforestry Pilot Project – Project Appraisal Report
[5] United Nations Environment Programme (2011) REDDy Set Grow. UNEP Finance Initiative
[6] Climate Investment Funds (2009) Design Document for the Forest Investment Program, A Targeted Program under the SCF Trust Fund

It is accepted that the scale of financing needed to achieve the REDD+ impacts called for by the international community is simply beyond the capacity of public sector budgets and thus requires significant private sector finance[7]. The FIP is testing the private sector's appetite for REDD+ investments in places and at scales previously untested, and will build the collective knowledge and experience of private sector, government and MDB partners to inform future measures.

## MAIN INCENTIVES FOR PRIVATE SECTOR ENGAGEMENT IN REDD+

With such a large and diverse group of actors, it is challenging to identify the particular set of incentives that will consistently elicit private sector engagement in REDD+. In practice, the FIP partners in each country consult with private sector actors during the investment plan preparation phase, in order to identify their constraints, capacities, and motivations and design programs to address them, as discussed in a later section. Private sector actors may perceive REDD+ as a business opportunity, a regulatory risk, and/or an instrument to help manage risks[8].

### *Business opportunities*

**Key lessons:**

- Demonstrating and enhancing the profitability of forests and their sustainable management is essential to incentivizing private sector engagement and achieving the goals of REDD+.
- Through the provision of advisory services and finance, FIP will help create opportunities for the private sector to improve both production and management and to access new markets and finance.

Demonstrating and enhancing the profitability of forests and their sustainable management is essential to incentivizing private sector engagement and achieving the goals of REDD+. As one private sector FIP stakeholder put it, "the forest that pays is the forest that stays." If forests are not valued highly enough by the private sector in financial terms, forest conversion to other more profitable land uses, such as agricultural production, and the use of destructive, inefficient, low-cost forestry and agricultural practices will remain financially attractive to private actors. Another stakeholder explained that, "without clear positive benefits, compared to business as usual, the private sector will be reluctant to implement REDD+ activities."

Hundreds of millions of households and numerous profitable industries benefit from the ecosystem goods and services that forests generate, including timber, fuel wood, arable soil, water, carbon sequestration and storage, biodiversity, and others. Despite the value of this natural capital, markets and policy frameworks have failed to monetize forest ecosystem goods and services and take into account the long-term costs of activities that degrade them, such as deforestation and unsustainable forest use and management. REDD+ aims to realign markets and policy frameworks to appropriately value ecosystem services, especially carbon sequestration and storage; the FIP will help create new business opportunities for the private sector to capture some of that value.

The most effective incentives for the private sector to engage in REDD+ activities are the business opportunities to improve production and management, access markets, and access finance. Yet there are clearly constraints to private sector engagement in REDD+ activities, otherwise they would be standard practices in industry. FIP will help to address these constraints by providing private sector partners with targeted advisory services and financing.

Private sector actors, particularly in the forestry and agricultural sectors, are well placed to implement a number of REDD+ activities that can be integrated with existing operations and core business models centered on the production and trade of forest products and other commodities. A non-exhaustive list of potential private sector REDD+ activities was provided in the introductory section of this document.

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[7] Center for International Forestry Research (2008) Financing REDD: Linking Country Needs and Financing Sources
[8] UK Department for International Development (2010) Engaging the Private Sector in the Potential Generation of REDD+ Carbon Credits

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On the production side of the value chain, these REDD+ activities can help companies diversify, improve predictability, reduce operational risk, and enhance the longer-term sustainability of their operations. On the marketing and sales side, REDD+ activities can also provide a means for the private sector to respond to high and growing demand for forestry and agricultural products in domestic markets, and to a shift in demand in developed countries' premium markets favoring "forest friendly" products (for example, certified wood). FIP will provide advisory services to support private sector actors in the transition to new business practices and to help them capture the benefits noted above.

FIP will also help companies finance the costs of implementing REDD+ activities. Private sector, government, and MDB representatives, across the visited FIP countries (Burkina Faso, DRC, Indonesia and Peru), noted that the private sector cannot access financing for REDD+ activities from domestic financial institutions and that there is limited financing available from the government and bilateral and multilateral donors. In one country with a large forest industry, it was noted that banks rarely make loans for anything but equipment. The FIP will help to address these constraints and fill the gap in the absence of local financing as, in addition to direct financing of private sector activities, the FIP will work with financial intermediaries such as domestic banks to on-lend FIP financing as targeted lines of credit.

FIP will also assist the private sector with accessing emerging REDD+ financing mechanisms. Forest carbon markets offer a limited, but growing opportunity to attract financing for private sector REDD+ activities[9], as do ecotourism and payment for ecosystem services (PES) systems. In most FIP countries, PES systems do not exist or are only operational at the pilot stage; FIP public sector interventions are being designed to expand such opportunities. Where these opportunities do exist, but only a small number of private sector actors have experience with these mechanisms, FIP advisory services will be an important component of investments.

## *Managing regulatory risks*

**Key lessons:**

- Engagement of the private sector in FIP may have spill over benefits in terms of enhancing private sector engagement in other national REDD+ processes, including policy development.

For private sector actors engaged in activities that directly or indirectly cause deforestation and forest degradation, REDD+ is also seen as a risk. They are particularly concerned that the government, in order to meet REDD+ targets, will implement regulations that will adversely affect their businesses, for example, moratoriums on forest land concessions. Regulation is an incentive that could be used to compel private sector actors to engage in REDD+, but it is beyond the scope of what the FIP is designed to do. This highlights a real challenge for FIP, since regulatory aspects of REDD+ policies have not been defined in most FIP pilot countries, nor have institutional frameworks for their implementation. As a result, companies are uncertain about whether to make investments, and if so, which types and how soon.

One way for the private sector to manage regulatory risk is to engage directly in national REDD+ policy dialogues. In some countries, FIP is seen as having early success in raising REDD+ awareness among private sector actors, especially through industry associations that are more typically engaged in policy processes and play a strategic role in disseminating information to their members.

[9] Ecosystem Marketplace (2012) State of the Forest Carbon Markets 2012: Leveraging the Landscape

This could have a positive spillover effect on national REDD+ policy dialogues, where in the past private sector engagement has been limited, and more generally increase private sector awareness and understanding of REDD+ policy developments. However, such spillover effects are difficult to measure and attribute, especially at this early stage.

## *Managing social and environmental risks*

**Key lessons:**

- The private sector expects FIP investments to have a positive social and environmental impact.
- The private sector also sees the FIP as an opportunity to reduce social and environmental risks of forestry investments, particularly in areas with unresolved land conflicts.
- The Dedicated Grant Mechanism, in combination with other public policies and actions supported by FIP, could provide an opportunity to address land tenure issues which pose an underlying risk that constrains private sector investment in REDD+ activities.

Businesses also see REDD+, including the FIP, as an opportunity to manage risks, particularly as they relate to social and environmental issues, including the legality of their wood supply. Large companies with brand exposure, including in the financial sector, are under increasing pressure from shareholders, customers, regulators, and civil society organizations to conduct their business in a socially and environmentally responsible way. The upside for large exposed companies to engage in REDD+ investments lies in the positive social and environmental impacts that they can generate and communicate to their constituents, and the transparency and accountability that come with documentation of management practices, such as are required for certification programs. These measures can help to enhance their public image and protect their reputation, in addition to the production and marketing benefits mentioned above.

The need to manage social and environmental risks is even more real for companies operating in countries with ongoing land reform movements and where overlapping claims on forest lands and resources have not been resolved. Companies are sometimes operating in areas where mutually agreed land use maps do not exist, which can be a large source of uncertainty. When indigenous peoples, local communities, and civil society groups perceive that private sector activities are infringing upon their land rights, ensuing conflicts can have a direct impact on a company's profits and public image.

While resolving these conflicts on a national scale is beyond what limited FIP financing can achieve, there is scope for FIP investments, including through the Dedicated Grant Mechanism for Indigenous Peoples and Local Communities, to help clarify land tenure issues in areas where complimentary REDD+ investments are being made, including private sector investments. The private sector has indicated that they appreciate this aspect of the FIP design, as have indigenous peoples organizations and other interested stakeholders.

Across the board, FIP pilot countries have taken a participatory approach to their investment planning and related consultation processes. This has brought private sector representatives and representatives of all other stakeholder groups, including indigenous peoples, to the same table. In countries where the FIP is moving into implementation, the opportunities to take action on common interests identified through the consultation process are promising.

## *Lowering costs*

**Key lessons:**

- Access to finance for upfront investment, start-up capital and associated capital and transaction costs are major barriers to the engagement of small- and medium-sized enterprises (SMEs) and community-based enterprises in REDD+.
- National development banks and private domestic banks can play a similar role as intermediaries for FIP finance aimed at incentivizing REDD+ investments by SMEs and community-based enterprises, but both sets of actors need capacity building to lower risks and promote sustainability.

For the private sector, moving from unsustainable (or un-certified) to sustainable practices generally comes at a cost. At the very least, there are upfront investment or transaction costs, such as for training, permits and local authorizations, new equipment, accessing different sources of finance, or third-party verification (in the case of certification and carbon credits). At most, private actors could incur substantial opportunity costs from avoided utilization of forest and forest land resources.

Whether such costs are a significant barrier will depend on the specific business context as well as the time horizon for expected returns (i.e. short, medium, or long term). For example, in FIP consultations, small- and medium-sized producers have indicated that they are working with limited capital and access to affordable credit, which makes it difficult to make any upfront investments unless the payback period is very short. The opportunity cost of avoided utilization and the high hurdle rate would also be significant disincentives for making REDD+ investments. For larger businesses with working capital and established credit histories, a longer payback period may be more acceptable, if given the opportunity to borrow FIP finance with concessional terms, gain access to new markets, or expand market-share in certified products that command a price premium.

MDBs and governments are cognizant of these cost concerns and have taken them into account in the elaboration of FIP investments targeting the private sector. IFC, for example, can invest directly in medium or large companies through its existing financing and operational modalities, ensuring the application of the principle of least concessionality[10]. Small- and medium-sized enterprises (SMEs) are difficult for IFC to invest in directly -- it typically provides financing for SMEs through financial intermediaries. IFC's experience in providing energy efficiency financing to SMEs through local banks is serving as a model for FIP financing of SMEs in the forestry sector.

The IDB has flexibility in dealing with different private sector clients. The Multilateral Investment Fund (MIF) of the IDB for instance, is acting as a development laboratory - experimenting, pioneering, and taking risks in order to build and support successful micro and SME business models. The MIF works through technical assistance grants, equity investments, and lending as well as through combinations of these tools when both capacity building and risk sharing finance are needed for success. It is the largest international technical assistance provider to the private sector in Latin America and the Caribbean and always works with local, mostly private partners to help fund and execute projects, including with civil society organizations, industry associations, foundations, universities, cooperatives, companies, and financial institutions.

Similarly to IFC, IDB is also partnering with financial intermediaries, including a national development bank, private sector microfinance institutions, and pro-poor banks. These on-the-ground financial intermediaries are typically better positioned to assess smaller deals and establish creditworthiness of local actors.

[10] This means that FIP finance will be offered on a project-by-project basis with the very minimum level of concessionality needed to close each deal, rather than using standard financing terms across all private sector projects. This principle is applied to avoid using public finance inefficiently, over-subsidizing projects, and crowding-out commercially available financing.

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Both IFC and IDB are designing interventions to deal with structural barriers that prevent SMEs and community-based enterprises from accessing finance for REDD+ investments, namely lack of conventional collateral. They are also including technical assistance or advisory services as part of the package to build the capacity of private sector actors of all sizes, including financial institutions, to develop and assess business plans for REDD+ investments. Until these interventions move to implementation, it will be hard to know whether financial intermediaries can provide deal terms and structures that lower the cost of REDD+ for SMEs so as to enhance their engagement in a sustainable manner beyond the lifetime of the FIP.

Financial costs are not the only obstacles. Private sector actors in some countries have expressed the view that the transaction costs associated with accessing government finance for private SFM activities are high ("too much bureaucracy"). Some prefer to access finance through the MDBs, but even with MDBs there is a perception that the financing is hard to get because of extensive due diligence requirements ("too many rules", "time consuming"). Governments have identified broader challenges for private sector engagement in their national contexts, including lack of enabling business environments and the inability of domestic companies to meet high MDB environmental and social standards.

The combination of weak business environment, lack of capacity in the private sector on social and environmental practices, and MDB due diligence requirements may well continue to pose challenges for engaging the private sector in FIP and other REDD+ initiatives. Private sector actors, governments, and MDBs will need to work together in good faith to foster mutually realistic expectations and nurture the political will needed to make these potentially catalytic investments. Private sector actors will need to be both patient and responsive and, once programs have been approved, MDBs and governments will need to work harder and faster to complete their reviews and issue their disbursements[11].

## PRIVATE SECTOR ENGAGEMENT IN THE FIP INVESTMENT PLANNING PROCESS

**Key lessons:**

- MDBs and governments have been successful in identifying, informing and consulting with private sector stakeholders as part of the process for developing the FIP investment plans.
- Private sector engagement tools for information-sharing and consultation include sharing print and electronic documents, one-on-one meetings, meetings with multi-stakeholder platforms, meetings and workshops organized in partnership with business associations and producers unions, and field visits.
- The process-oriented, and often lengthy, nature of FIP investment plan development is not aligned with private sector culture or expectations.

In most FIP countries, MDBs and governments have engaged with private sector actors from the beginning of the FIP investment planning process. The private sector stakeholder engagement process can be thought of as having four non-discrete phases: stakeholder identification, information sharing, consultation, and partnership building.

[11] Climate Investment Funds (2012) FIP Pilot Countries Meeting, April 2012. DRC Challenges in Implementing the IP and Lao PDR's Successes and Challenges in the FIP Process.

Non-discrete in this case refers to the fact that activities in the different phases were carried out as part of a process, with phases overlapping at times and adaptations made as feedback was received. It should also be noted that private sector engagement was not carried out in isolation. Although specific engagements were targeted to the private sector audience, private sector actors also attended national and regional engagements for all interested stakeholder groups.

In the stakeholder identification phase, MDBs and governments compiled lists of contacts, leveraging MDBs' extensive national and global private sector networks, government contacts, and private sector associations. For example, in Indonesia, IFC was able to draw on contacts with partners in its Indonesia Sustainable Forestry program and Global Forestry and Wood Products group, as well as the member list of the Indonesian Forestry Industry Association, among others. The objective in each country was to cast a wide net and ensure that different interest groups within the private sector would be adequately represented in the initial phases. As additional private sector stakeholders were identified later in the process, they would be integrated into subsequent engagement activities.

In the next phase of engagement, these networks were activated using direct e-mail and telephone correspondence to invite private sector stakeholders to information-sharing events at the national and regional levels. This strategy was enhanced by public posting of documents and meeting dates through online media such as CIF and government websites as well as through news media. In Indonesia, participants in a national workshop "expressed appreciation for the efforts of the joint mission for posting relevant documents on the CIF and [National Forestry Council – a multi-stakeholder platform -] web sites[12]." Public posting of documents was also carried out prior to Indonesia's first joint mission.

With stakeholder identification and information sharing well under way, the consultation phase was begun. As per the FIP Operational Guidelines, government-led scoping and joint missions were organized, with MDBs playing a supporting role. The purpose of scoping and joint missions, from a private sector engagement perspective, were for MDBs and governments to assess and verify the specific barriers to private sector REDD+ investment, seek stakeholder feedback on appropriate private and public sector interventions, and ultimately seek consensus on proposed investments to be included in the country's FIP investment plan.

The consultation phase did not start and end with joint mission meetings, nor did the information-sharing phase end when the consultation phase began. These phases of the private sector stakeholder engagement process used the same set of engagement tools or mechanisms, including sharing print and electronic documents, one-on-one meetings, meetings with multi-stakeholder platforms, meetings and workshops organized in partnership with business associations and producers unions and, in some countries, even field visits to sites where SMEs and community-based enterprises operate. In the case of multi-stakeholder platforms, the FIP process benefitted from pre-existing capacities and institutional mechanisms established by governments in partnership with other multilateral and bilateral REDD+ initiatives such as the UN-REDD Programme and Forest Carbon Partnership Facility (FCPF). For example, in DRC, FIP was channeled through the technical coordination group established for the development of the country's REDD+ Readiness Strategy, co-financed by the UN-REDD Programme and FCPF.


To get a sense of the scope and number of these engagements, one only needs to review the country programming documentation submitted to date, including joint mission reports and investment plans themselves. DRC's investment plan notes, "… more than 30 meetings of the [technical coordination group] were held, involving more than 160 people, including over 50 representatives from the private sector (28 companies, 6 banks, 2 private sector representative organizations)."

[12] Climate Investment Funds (2011) Indonesia' Second Joint Mission Completion Report

In Indonesia, specific group meetings targeted at private sector stakeholders were held in June, July (attended by 28 private sector representatives), and December 2011 (16 private sector representatives), in addition to multi-stakeholder meetings and less formal meetings. This documentation cannot capture the full extent of engagement, since much of day-to-day business is carried out over e-mail and telephone.

Although it was observed during country missions conducted for this Learning Product that private sector actors in Burkina Faso, DRC, Indonesia and Peru have different levels of awareness and understanding of the FIP (some did not seem to know about the FIP, but knew about REDD+), there were no concerns or complaints voiced that the private sector had not been well engaged in those countries. Some, especially representatives of producers organizations did express that "there is a difference between participation in meetings and participation in implementation," with the latter referring to on-the-ground activities and impact. A commonly expressed frustration in several FIP countries was that the time period of consultations and investment plan development was too long. The other critique of the engagement process was that there were "too many meetings."

In one country where the government and MDBs had sacrificed speed in order to build consensus with civil society and indigenous peoples on aspects of the consultation process and investment plan, private sector actors even suggested that the country move forward in a two track process, whereby the private sector components could move forward to seek endorsement while the government and civil society reach agreement on the public sector investments. Even with such an arrangement, MDBs involved in the consultations indicated that the gestation time that would follow endorsement before FIP financing to the private sector would actually begin flowing could reasonably be estimated to be six months. This was not a mainstream proposal that the government or MDBs gave serious consideration to, but it highlights the high level and urgency of demand expressed by the private sector and points to a broader challenge of managing trade-offs in speed and depth of the consultation process.

Now, as private sector project proposals begin to make their way through FIP and MDB decision-making bodies for those countries with endorsed investment plans, MDBs and governments are poised to begin the process of seeking formal proposals from the private sector, conducting due diligence on proposals, and designing and structuring investments[13]. In other words, private sector engagement is moving to the partnership building phase of implementation.

## CROSS-SECTORAL PRIVATE SECTOR PARTICIPATION IN THE FIP

**Key lessons:**

- Inter-ministerial collaboration in REDD+ decision-making may lead to cross-sectoral private sector participation.
- However, the ministries collaborating on the FIP tend to cover a limited number of sectors (e.g., environment, forestry, agriculture, finance), and participation of private sector actors outside those sectors is not common.

In FIP pilot countries, national inter-ministerial councils with authority over REDD+ strategy have included Ministries of Finance, Development, Environment, Agriculture, Forestry, Energy, Mining, Transport, and others. This is rational, since each of these Ministries is responsible for policies, plans, and programs or projects that have the potential to make an impact on forests, particularly in the context of REDD+. These Ministries also have working relationships with the broad spectrum of private sector actors that are working or financing activities in and around forest areas or in related value chains, and therefore hold a strategic position in terms of their capabilities to enhance private sector engagement in REDD+.

While national councils are primarily serving efforts to develop National REDD+ Strategies, the FIP investment planning processes in most countries have been driven by a smaller subset of inter-ministerial collaborators and focal points.

[13] For those projects being managed by the private sector arms of the MDBs, FIP financing must be approved before they can begin identifying and reviewing individual investments.

Each of the pilot countries visited has put in place an inter-ministerial body, most commonly consisting of the Ministries of Environment, Forestry, Agriculture, and Finance, with decision- making and coordination responsibilities over their FIP investment plans. In this context, FIP has already made an impact by bringing government stakeholders in these sectors together in effective ways, overcoming some institutional difficulties stemming from overlapping authorities over forest and land resources.

In the countries visited, it was also observed that a cross-sectoral group of private sector stakeholders under the purviews of Ministries of Environment, Forestry, Agriculture, and Finance is engaging in the FIP process and learning about its incentives for REDD+ investment. These stakeholders range from small producers in the African shea, livestock, and charcoal industries, to large industrial forestry companies in Asia and Latin America, and financial institutions worldwide. This suggests that the scope of inter-ministerial or cross-sectoral collaboration on the government side may be having a positive influence on the sectoral mix of private sector collaborators. MDB personnel assigned to the FIP also tend to be from the sectors that correspond with the collaborating Ministries, which could be enhancing this effect, since they are also responsible for engaging their private sector networks in the FIP process.

It is notable that Ministries of Energy, Mining, and Transport are not among the members of the FIP inter-ministerial committee in any pilot country. The in-country meetings conducted with stakeholders for the purposes of this Learning Product included no representatives from these sectors, neither from governments, MDBs, nor the private sector, aside from charcoal producers. Although some countries' FIP investment plans do recognize their importance, and allow for their participation, without the involvement of corresponding government institutions and MDB personnel, it seems unlikely that private actors from these sectors will be engaged in FIP implementation, despite the potential opportunities.

The direct and indirect linkages between the construction of linear infrastructure, typical of site development in these sectors, and deforestation and forest degradation are well documented and can be modeled. It seems plausible that with REDD+ incentives, mining, energy, or transport companies could be convinced to implement best management practices that reduce above-ground impacts on forest ecosystems. For example, an alternative road or pipeline routing that was previously considered infeasible when evaluated in an environmental impact assessment for a new facility located in forest lands might become feasible once REDD+ financing is factored in.

It may already be too late to fully explore this potential in most FIP countries, given that new stakeholder engagement efforts would be required after the investment plans have already been elaborated and that such investments might not fit well into national REDD+ strategies. It may also be that countries have assessed the potential impact of such investments compared to investments in the agriculture or forestry sector and determined that they do not warrant the same level of priority. In either case, other efforts or incentives targeting private sector actors in these sectors may be warranted, such as regulation or public-private partnerships.

## STAKEHOLDER VIEWS ON PRIVATE SECTOR INVOLVEMENT IN THE FIP

### *Private sector*

**Key lessons:**

- Private sector actors need to be educated about MDB and government policies, including financial, environmental, and social criteria, and be given reasonable or conservative estimates regarding the time it may take to move from business development to disbursement.

Given the focus in the early stages of REDD+ on capacity-building and investment, and the promise of results-based payments down the road, private sector actors have expressed their willingness and even eagerness to take advantage of REDD+ incentives, particularly FIP financing – so long as it does not bring down their bottom line. In some cases, private sector actors have had a misperception that FIP money is "cheap". MDBs have had to educate the private sector regarding the principle of least concessionality.

Private sector actors have also emphasized fast delivery of finance as an important criteria for scaling up their involvement in FIP and REDD+ more broadly. This is perhaps premature since, in country level consultations, it has been apparent that many private sector actors lack a full awareness of the financial, social and environmental criteria for multilateral direct investments.

Information-sharing and capacity-building with the private sector, particularly in regards to social and environmental standards, should be emphasized in the short term in order to promote upfront compliance with MDB and national requirements, reduce delays for lack of completeness, and mitigate the risk of frustrations on both sides down the road. Private sector actors who have no experience applying for MDB financing or are known to have low levels of capacity should be given conservative estimates regarding the time and effort it may take to move from business development to disbursement.

### *Pilot country governments*

**Key lessons:**

- With knowledge and experience gained from engaging with the private sector, and/or a clear mandate to do so, government officials will prioritize investments in private sector REDD+ activities, in an effort to attract private co-financing.
- Multilateral finance for private sector REDD+ investment can be channelled through governments or MDBs' private sector arms, depending on the preference of governments and the type of investment.
- Governments do not necessarily want multilateral finance for private sector REDD+ investments to be channelled through their institutions.

Pilot country government focal points responsible for the investment planning process are from public agencies. They tend to be most familiar with public interests, institutions, programs, and persons and less familiar with private sector instruments, investment structures, associated needs for financing, and incentives. Early in the process, some perceived private sector REDD+ investments to be riskier and less effective than public investments. In deciding how to allocate limited financing to different priorities, some expressed reservations about allocating funds for private sector initiatives, perceiving it as a reduction in funds available for public sector priorities.

However, as evidenced in all investment plans endorsed to date by the inclusion of private sector projects, where financing is channeled to the private sector either through the private sector arms of MDBs or through the public sector arms of the MDBs and then government agencies, governments have come to understand the potentially valuable and complementary roles such initiatives could play in transforming markets. Learning has been assisted by MDB efforts to share knowledge and raise awareness as well as government engagement with private sector stakeholders during investment plan consultations. In general, pilot country governments now recognize the potential benefits of using public funds, including the FIP, to invest in and leverage private financing for private sector REDD+ activities. In fact, they continue to express interest in learning about successful models of private sector engagement in REDD+[14].



Countries differ in their definition of the private sector (small/community producers vs. large producers; carbon financiers vs. rights-holders) and in their preferred model for channelling FIP financing to the private sector. Some may prefer to have the private sector arms of the MDBs provide FIP financing directly to the private sector. In one country, the rationale for this was to leverage the MDB's comparative advantage and technical expertise and reduce administrative burden on government agencies. Ghana, Indonesia, Lao PDR, and Mexico included private sector components like this in their endorsed investment plans. An alternative is to channel FIP financing for the private sector through government institutions, including national development banks. Some countries with this preference believe it will ensure that FIP private sector investments align with national REDD+ goals and strategies and build on existing capacities. Brazil, Burkina Faso, DRC, and Mexico included projects that channel finance to the private sector through public institutions in their endorsed investment plans.

## *Contributor countries*

Key lessons:

- Contributor countries are interested in the FIP's potential to leverage private sector finance with public funds.
- Contributor countries see the FIP's level of engagement with the private sector as potentially transformative and a source of future lesson learning.

Major contributors to the FIP and other bilateral and multilateral REDD+ initiatives have emphasized that one of the FIP's greatest potentials in terms of transformational impact and lesson learning may come from its partnership with the private sector. At a time when contributor countries' budgets are constrained, they are eager to see how the FIP can use limited public finance to leverage private investment. This message is consistently expressed in various forums and at different levels, including FIP Sub-Committee meetings and national consultations. Contributors have noted the lower levels of private sector engagement in other REDD+ initiatives, particularly those active in the national REDD+ policy arena, and are hoping that FIP's investment plan and project-level engagement will spill over into broader national dialogues. Some have noted complementarity between their capacity-building programs, for example in Forest Law Enforcement, Governance and Trade (FLEG-T), and potential FIP investments with the private sector.

[14] Climate Investment Funds (2012) FIP Pilot Countries Meeting Report

## *Indigenous peoples organizations and civil society organizations*

**Key lessons:**

- The status of tenure, security of rights, and history of social and environmental conflicts with the private sector, in each country influences the extent to which IPOs and CSOs find FIP private sector financing acceptable.
- In countries with histories of social and environmental conflicts between private companies and indigenous/civil society groups, often related to overlapping claims on forest lands and resources, mistrust can be a pervasive influence on REDD+ processes.
- In FIP consultations, IPOs and CSOs in more than one country have emphasized that public finance should not be used to subsidize private sector forest exploitation and commodity production or reward concessionaires with poor social and environmental track records.
- The Dedicated Grant Mechanism will provide an opportunity to reduce competition for FIP financing between the private sector and indigenous peoples and local communities.
- Despite stipulations on what private sector actors or activities should and should not be financed by the FIP, IPOs and CSOs in these countries have not unilaterally opposed the inclusion of private sector programs in FIP investment plans.

Indigenous peoples organizations (IPOs) and civil society organizations (CSOs) view FIP private sector financing differently from country to country, depending on their context, constituency, and negotiating positions in the broader investment planning process. The status of tenure, security of rights, and history of social and environmental conflicts with the private sector, in each country shape the attitude of these stakeholders toward the possibility of FIP private sector financing.

In unique cases, such as in Mexico, land reform and distribution have resulted in clear and secure tenure for indigenous peoples and local communities, and many small- and medium- sized private sector forestry enterprises are actually indigenous or community enterprises. Mexico was not one of the countries visited for this Learning Product, but, based on public documentation, it does not appear that Mexican IPOs or CSOs objected to the allocation of FIP finance to private sector activities.

In several FIP countries, IPOs and CSOs are actively advocating for changes to public policies that they believe will improve the status of tenure and security of rights for forest-dependent indigenous peoples and local communities. In some of these same countries, there are histories of social and environmental conflict between large private companies and indigenous/civil society groups, often related to overlapping claims to forest lands and resources. Where this combination of factors exists, there tends to be a high background level of mistrust which can be a pervasive influence on REDD+ processes.

IPOs' and CSOs' discomfort with private sector involvement in REDD+ is amplified in countries where stakeholders have had negative experiences with private actors in the specific context of forest carbon markets. For example, an IPO stakeholder engaged in the FIP process reported that "carbon cowboys" have approached indigenous peoples and local communities and obtained leases and carbon rights on unfair terms.

In FIP consultations, IPOs and CSOs in more than one country have emphasized that public finance should not be used to subsidize private sector forest exploitation and commodity production or reward concessionaires with poor social and environmental track records. They have also suggested that FIP financing would be better spent if passed on to non-profit organizations, including IPOs, for activities such as land titling and registration, community forestry and general development[15] .

[15] Asociación Interetnica de Desarrollo de la Selva Peruana (AIDESEP) (2012) Carta No. 097-2012-AIDESEP

MDBs have social and environmental policies, often referred to as safeguards, or Performance Standards in the case of IFC[16], that apply to all MDB financed projects and prevent the use of resources to finance private companies with poor social and environmental track records. In regards to the second concern, the MDBs' business modalities have not traditionally allowed them to provide direct financing to non-profit organizations in the same way as with the private sector. However, in the process of setting up the USD 50 million FIP Dedicated Grant Mechanism (DGM) for Indigenous Peoples and Local Communities, MDBs will create such modalities and begin to test models for the kinds of partnerships and activities these groups envision or desire. It is not clear whether this will alleviate the longer term tensions between the private sector, indigenous peoples, and civil society organizations where they persist, particularly given the smaller scale of financing available through the DGM, but at the very minimum it could reduce short- to medium-term competition among these different stakeholder groups for limited FIP resources.

Despite these and other stipulations on what private sector actors or activities should and should not be financed by the FIP, IPOs and CSOs in these countries have not unilaterally opposed the inclusion of private sector programs in their countries' FIP investment plans. This may be a product of their country context and constituency. For example, in countries like Mexico, many of the target beneficiaries of FIP-financed private sector programs are indigenous and community enterprises. It may also relate to negotiating positions in the broader investment planning process. For example, in one country, a coalition of IPOs and CSOs were initially opposed to the public sector taking any loan financing offered by the FIP. In consultation with these groups, the private sector, and MDBs, the government decided to allocate the entire loan portion of its FIP financing to the private sector through the private sector arm of an MDB. In achieving their bottom line of "no FIP loans to the public sector", these groups did not oppose the allocation of FIP loan financing going to the private sector, albeit with some conditions[17].

## EXPECTED CHALLENGES AND OPPORTUNITIES

As previously noted, FIP is unique among the four main multilateral REDD+ initiatives in that it has the mandate to finance private sector REDD+ investments and leverage private co-financing. Without this important mandate, MDBs and pilot country governments probably would not have achieved the level of private sector engagement that they have so far. Lessons learned documents from other multilateral REDD+ initiatives without such a mandate indicate that private sector engagement is an ongoing challenge[18].

With FIP financing for engaging the private sector in hand, MDBs and governments have had an answer to the inevitable and crucial question that arises in private sector consultations – "What's in it for me?" That is a key advantage that the FIP and its partner institutions have leveraged and should continue to leverage moving forward.

MDBs and governments still have challenges ahead. For example, they will need to clearly and convincingly answer the inevitable follow up question – "What exactly do I have to do to receive private sector FIP financing?" The capacity challenges noted in this report are real, and many potential partners may not have experience accessing finance from MDB and government programs. They will likely face difficulties meeting MDB social and environmental performance or creditworthiness criteria, and MDB support for companies to build that capacity will be essential.

It should be noted that, as of the date of publication, only two project proposals aimed at channeling FIP financing to the private sector have been submitted to and approved by the FIP Sub-Committee[19] .

[16] International Finance Corportaion (2012) IFC Performance Standards on Environmental and Social Sustainability
[17] Huma, BIC, debtWatch Indonesia, ELAW Indonesia, AMAN, Solidaritas Perempuan, KPSHK, Forest Peoples Programme, IESR, Greenpeace, Walhi, AKSI, Ulu Foundation, Sawit Watch (2012) Comments and Recommendations on the Forestry Investment Program/Plan Document.
[18] UN-REDD Programme Strategy 2011-2015; UN-REDD Programme (2011) Lessons Learned, Asia Pacific.
[19] "Financing Low Carbon Strategies in Forest Landscapes" project, approved on 4 September 2012, will provide financing to SMEs and community-based enterprises via a national development bank. "Support for Forest Related Micro, Small, and Medium-sized Enterprises (MSMEs) in Ejidos" project, approved on March 4th 2013, will provide technical assistance and micro credit to SME and community based enterprises through the Multilateral Investment Fund – IDB's private sector arm.

Both are IDB projects targeted to support SMEs and community-based enterprises in Mexico with technical assistance and financing. One is being channeled through IDB's private sector arm and the other through an IDB public sector project working with a national development bank as a financial intermediary. FIP private sector programs of both types are still in the design phase in other FIP countries and, for those being managed by the private sector arms of the MDBs, FIP financing must be approved before they can begin formally identifying and reviewing individual investments.

As programs become more concrete, governments and MDBs need to target the private sector in more concerted communications efforts. Any criteria developed for qualifying activities for financing will need to be communicated in a timely manner to potential partners, or risk losing their good faith. Communications products that clearly spell out what private sector activities are eligible for FIP financing, with illustrative examples for different sectors (forestry, agriculture, etc), could be developed jointly by MDBs and the CIF Administrative Unit. Of course, each MDB would be free to tailor and translate the products to their particular country contexts and languages. In either case, the responsibility for widely disseminating this information to private sector constituents would largely rest with MDB country offices and governments.

A significant challenge facing partners in most FIP countries is the lack of previous experience financing private sector REDD+ activities. It may be necessary to draw on experiences and lessons from smaller initiatives and international knowledge centers, such as the World Bank's BioCarbon Fund, and voluntary REDD+ carbon standards organizations, such as the Verified Carbon Standard and the Climate, Community and Biodiversity Alliance. These potential knowledge partners are well placed to share experiences and lessons learned and set realistic expectations for the challenges that private sector REDD+ projects are likely to face.


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With the first approved FIP private sector investments just underway, lessons learned have mostly drawn from private sector experience to date in the four pilot countries' investment planning process in which different stakeholder groups have been engaged and, through consultation, expressed their aspirations, needs, and concerns. Moving forward to implementation, private sector projects supported by the FIP will provide a unique and valuable source of new experience. The CIF AU, MDBs, and governments will continue private sector engagement and ensure that the new lessons are documented and shared with the broader international community.