CLIMATE INVESTMENT FUNDS

FIP/SC.12/7
May 26, 2014

Meeting of the FIP Sub-Committee
Montego Bay, Jamaica
June 28, 2014

Agenda Item 6

OPTIONS FOR THE USE OF POTENTIAL NEW FUNDS UNDER THE FIP

PROPOSED DECISION

The FIP Sub-Committee reviewed document, FIP/SC.12/7, *Options for the Use of Potential New Funds under the FIP,* and welcomes the proposed options.

The Sub-Committee agrees that the following should be pursued should additional funds be made available to the CIF…

[i. *Option 1*: Selection of new FIP pilot countries.]

[ii. *Option 2*: A dedicated set-aside of funds to address emerging issues related to REDD+ and/or close strategic gaps identified in the FIP portfolio, including a second round incentivizing innovative private sector investments.]

[iii. *Option 3*: Additional resources to existing FIP pilot countries.]

[iv. *Option 4*: Expansion of FIP activities to all SCF countries in support of synergies between mitigation and adaptation/resilience measures as they relate to forest landscapes and REDD+, including innovative private sector projects.]

The Sub-Committee requests the CIF Administrative Unit, to keep it informed of the availability of new resources so the Sub-Committee can agree if and when it is appropriate to expedite the implementation of any option.

I. INTRODUCTION

1. At its meeting in October 2013, the FIP Sub-Committee reviewed document FIP/SC.11/7, *Approaches and Criteria for Considering Potential New Pilot Countries,* and agreed that it is not selecting new countries under the Forest Investment Program at this stage and that it is not asking for any expression of interest or new investment plans.

2. The Sub-Committee welcomed a broader discussion of how funding could be used effectively should new funds become available.

3. The CIF Administrative Unit, in collaboration with the MDB Committee, was invited to prepare a paper exploring possibilities for the use of additional funds, should they become available under the FIP, for consideration at the next Sub-Committee meeting.

II. OPTIONS FOR THE USE OF POTENTIAL NEW FUNDS UNDER THE FIP

4. Consistent with the decision by the Sub-Committee in October 2013, the CIF Administrative Unit, in collaboration with the MDB Committee has prepared four prioritized options for the use of new funds, should they become available under the FIP:

> Option 1: Selection of new FIP pilot countries.
>
> Option 2: A dedicated set-aside of funds to address emerging issues related to REDD+ and/or close strategic gaps identified in the FIP portfolio, including a second round incentivizing innovative private sector investments.
>
> Option 3: Additional resources to existing FIP pilot countries.
>
> Option 4: Expansion of FIP activities to all SCF countries in support of synergies between mitigation and adaptation/resilience measures as they relate to forest landscapes and REDD+, including innovative private sector projects.

5. Each option will depend on the amount of new resources available to the FIP. The Sub-Committee may decide to choose one option or it may conclude that a combination of options should be piloted.

6. Each proposed option will promote investment activities which are consistent with the *FIP Design Document*[1].

Option 1: Selection of new FIP pilots

7. As of March 2014, 39 additional countries have expressed interest in participating in the FIP, 21 of which are countries participating in the readiness programs supported by the FCPF and the UN-REDD Programme.

---

[1] https://www.climateinvestmentfunds.org/cif/sites/climateinvestmentfunds.org/files/FIP_Design_Document_July_final.pdf

8. A recent in-depth study on the "Link between REDD+ Readiness and Implementation in FIP Pilot Countries" (document FIP/SC.11/6) concluded that the level of readiness drives the speed and types of FIP investments for meeting REDD+ goals and objectives at the country level. The study also emphasizes that FIP finance can provide an important bridge between REDD+ readiness and results-based finance. Hence, collaboration between REDD+ finance initiatives at the country level is of crucial importance for successfully addressing the drivers of deforestation and forest degradation.

9. Considering the interest of additional countries to participate in the FIP and the main findings of the study, option 1 proposes the expansion of the FIP to include new pilot countries. Specifically, it is suggested that a closer and more strategic link be established with the FCPF Readiness Fund and UN-REDD Programme by allowing countries which are supported in their readiness work under the FCPF and/or UN-REDD Programme to be eligible for accessing FIP funding. Annex 1 provides a list of countries currently participating in the FCPF Readiness Fund and the UN-REDD Programme[2].

10. New countries would be able to benefit from lessons gained from the programming and implementation process in existing FIP pilot countries. Hence, there is significant potential for South-South learning and broadening the *FIP Community of Practice*.

11. To implement this option, a new selection process would be needed. It is suggested that a process similar to the selection process being followed to identify additional SREP countries may usefully be explored (*Criteria and Process for Selecting New Pilot Countries under the SREP*[3], 2014).

12. The CIF Administrative Unit would invite eligible countries participating in the FCPF or UN-REDD Programme to submit an expression of interest in participating in the PPCR based on a template to be prepared by the CIF Administrative Unit in collaboration with the MDBs and approved by the Sub-Committee.

13. An expert group would be established to review the expressions of interest and recommend new countries, using selection criteria agreed by the FIP Sub-Committee.

14. The FIP Sub-Committee would invite the expert group to recommend up to [10] new countries that could benefit from the FIP while contributing to the overall programmatic objectives of FIP. Depending on the amount of available additional resources, the FIP Sub-Committee would then select a number of countries and invite them to prepare a full FIP investment plan. Preparatory grant resources would be provided. For the current set of FIP pilot countries, preparatory grant resources in the amount of USD 250,000 per pilot were provided to develop the investment plans.

---

[2] FIP pilot countries have been omitted in this list as they are already participating in the FIP.

[3] https://www.climateinvestmentfunds.org/cif/sites/climateinvestmentfunds.org/files/Criteria%20for%20new%20SREP%20pilot%20countries_final_2-26-2014.pdf

15. Once new countries are selected, programming of FIP resources will follow approved FIP policies, guidelines and procedures (see *FIP Investment Criteria and Financing Modalities,* the *FIP Operational Guidelines* and the *FIP Results Framework.*

16. To pilot the strategic link between REDD+ readiness and implementation; and demonstrate its validity in at least 3 additional countries, USD 200-300 million in new FIP resources should be made available.

Option 2: A dedicated set-aside of funds to address emerging issues related to REDD+ and/or close strategic gaps identified in the FIP portfolio, including a second round incentivizing innovative private sector investments in the current FIP pilot countries

17. With all eight FIP investment plans endorsed, analytical work on the FIP portfolio and the updates provided by the eight countries has shown that the projects and programs under endorsed investment plans address a range of aspects of the REDD+ agenda. While the current investment plans have a strong focus on community-based forest management and capacity development, countries could also benefit from additional funding for work in other areas. These could include, for example, enhancement of relevant co-benefits from REDD+ activities, such as biodiversity conversation and sustainable wood/renewable energy supply or innovative private sector activities.

18. Under this option, it is proposed that resources be made available on a competitive basis for exploring emerging issues in REDD+ or addressing gaps identified through the regular FIP portfolio analysis and annual/biennial country-level meetings reflecting on progress with the implementation of FIP investment plans. Consideration could be given to theme-based calls for proposals, depending on available resources in areas such as:

a) enhancing biodiversity considerations in REDD+ by, e.g., conserving and rehabilitating habitat connectivity across landscapes to reduce the negative impacts of fragmentation on biodiversity;

b) supporting innovative direct private sector investments, including developing sustainable supply chains for commodities relevant to REDD+ (annex 2 lists some ideas which could be further developed); advisory services and financial intermediaries;

c) forest and landscape certification;

d) supporting REDD+ relevant policy reforms;

e) investing in coastal vegetation management and conservation (e.g. mangroves, peat lands and wetlands); or

f) linking sustainable management of forests and wood-based energy supply or climate-smart buildings.

19. For this option, it is proposed to build on experience of a competitive allocation of resources under the FIP private sector set-aside and invite the FIP pilot countries to submit project concepts through the MDBs based on a specific call for proposals.

20. If this option is pursued further, the FIP Sub-Committee could decide for each round the specific opportunities or gaps to be addressed. A strategic gap analysis of the portfolio against the REDD+ potential would help the Sub-Committee to inform that decision. In addition, information on new REDD+ relevant opportunities may be discussed, e.g. using wood substitutes for fossil fuel, and steel and cement in the building industry[4].

21. The CIF Administrative Unit and the MDBs may suggest to the FIP Sub-Committee new procedures or modifications to the procedures for the FIP private sector set-aside depending upon the theme or gap to be addressed.

22. The allocation of additional FIP resources through this option would be competitive. The option would need a mix of grant and credit resources, depending on the objective of the call for proposals and related identified gaps and tools and instruments to address them.

23. To generate sufficient interest in accessing resources under this option, at least USD 100 million in new FIP resources should be made available.

Option 3: Allocation of additional resources to existing FIP Pilot Countries

24. Over the past years, FIP pilot countries have expressed the need for additional resources to address their REDD+ priorities. Recognizing that the needs of all the pilot countries far exceed the available FIP funding, additional financing could be made available to pilot countries[5].

25. Under this option additional FIP funds would be made available to all pilot countries to augment their initial FIP allocations, depending on the available amount of additional resources. Lessons from the allocation of additional resources to PPCR pilots has shown that if additional resources per pilot are less than USD 10 million, the additional resources will likely be programmed as additional to planned or ongoing investments.

26. The use of the additional FIP resources would contribute to enhancing the impact from FIP investments; e.g. by scaling up good practices in REDD+; addressing additional drivers of deforestation and forest degradation; or emphasizing the forest landscape approach, including restoration and rotational forest stand management.

27. FIP pilot countries would be required to set out an indicative program for the use of any additional resources. A country receiving an additional allocation would be expected to work with the MDBs to agree on the use of the additional funds following similar procedures to those used to prepare the initial investment plan, recognizing that the procedures may be greatly

---

[4] Using wood substitutes could save 14 to 31% of global CO_2 emissions and 12 to 19% of global fossil fuel consumption by using 34 to 100% of the world's sustainable wood growth. (Oliver, 2014)

[5] In November 2012, the PPCR Sub-Committee allocated additional PPCR resources to PPCR countries. The allocation ranged between 5-10 million per pilot country. Most resources were added to planned or ongoing PPCR investments.

simplified since the country will be able to build upon the preparatory work undertaken to prepare the original FIP investment plan.

28. Project or program preparation and implementation would follow agreed CIF and MDB procedures.

29. The implementation of this option would require a mix of grant and credit resources.

30. Considering that an objective of the FIP is to provide funding for scaled-up investments that can initiate transformational change, and taking into account the transactions costs to program and implement the additional investments, a minimum additional allocation should be agreed (e.g. USD 10 million). Hence, a minimum allocation of USD 80 million would allow one additional project in each pilot country.

31. Burkina Faso, DR Congo, Ghana and Lao PDR as countries in high debt distress, are not be eligible to receive FIP credits for public sector projects, and grant funding will need to be available for these countries.

Option 4: The expansion of FIP activities to all SCF countries in support of exploring synergies between mitigation and adaptation/resilience measures as they relate to REDD+, including innovative private sector projects

32. Activities related to reducing emissions from deforestation and forest degradation and managing forests and landscapes sustainably may have multiple benefits, including the increased resilience of forest ecosystems to the impacts of climate variability and change. In addition, in many low-income and vulnerable countries, drivers for deforestation and forest degradation are often linked to unsustainable wood harvesting for energy use (wood fuel, incl. charcoal and wood pellets). Providing access to energy and efficient energy alternatives would benefit local communities in terms of health (black carbon), reducing the pressure on women to collect firewood and reduce emissions mainly from forest degradation.

33. Resilience measures or energy-based investments using an integrated approach considering the larger land use context, can contribute to significant GHG emission reductions and biodiversity conservation (e.g. maintaining trees in the agricultural landscape, enhancing soil carbon and below-ground biodiversity, avoid forest degradation and related species loss).

34. Under this option, it is proposed that FIP resources be made available not only to existing FIP pilot countries but also for countries participating in the Pilot Program for Climate Resilience (PPCR) or the Program for Scaling-up Renewable Energy in Low-Income Countries (SREP).

i. *PPCR*: The majority of PPCR investments are in the agricultural sector with the objective to ensure food security by increasing the resilience of agricultural systems to the impacts of climate variability and change. These investments and others such as disaster risk management projects using a watershed approach have also the potential to contribute to GHG emission reductions and enhance biodiversity, especially in landscapes with forests and trees. Managing these landscapes for multiple benefits (food security, resilience and mitigation) is the core of climate-smart agriculture. So far, this potential has not been tapped in the PPCR.

ii. *SREP*: Investments in SREP focus on improving access to energy and providing renewable energy alternatives to rural communities in low-income countries. One energy source for rural community is wood fuel, often harvested from adjacent forests or trees in the wider landscape. Substituting fuel wood for another renewable energy source or providing access to the grid can contribute significantly to GHG emission reductions and other co-benefits such as health and biodiversity conservation. So far, this link is underrepresented in the SREP portfolio.

35. Examples of potential activities in PPCR and SREP countries support of REDD+ objectives under this option may include:

a) reforestation/afforestation activities (e.g. community woodlots; recovery of highly degraded lands);

b) integrated landscape management to address dynamics in the wider landscape (e.g agroforestry);

c) integrating forest conservation and management as a resilience measure in coastal zone management plans (e.g. mangrove forests vs. Sea walls);

d) creating bio-corridors to link forest fragments and allow species affected by the impacts of climate change or other pressures to migrate; or

e) enhance access to renewable energy in rural communities dependent on wood energy.

36. Examples of potential activities in all SCF countries in support of REDD+ objectives under this option may include investments, via equity and quasi-equity, in private sector agroforestry projects that allow for the implementation of profitable economical models while providing positive benefits for local populations and the environment.

37. Recognizing the particular capacity of private equity funds in the development of private enterprises in the agroforestry and forestry sectors given the nature of such enterprises, the time it takes for them to be established, mature and deliver value to their shareholders and surrounding communities, some MDBs are exploring innovative opportunities of supplying Patient Capital in the form of indirect equity and quasi-equity investments with a long time horizon. Annex 2 presents an example of a relevant investment opportunity that AfDB can implement on the short-term that could leverage other sources of private sector investments with FIP support.

38. For this option, it is proposed to communicate the opportunity to FIP, PPCR and SREP pilot countries, develop simple outreach material which clarifies the minimum set of conditions that would need to be in place to access additional FIP resources through this option. Procedures for implementation would follow standard FIP project approval procedures.

39. The allocation of additional FIP resources through this option could be on an ongoing basis linked to the identification of market opportunities or competitive. The option would need a mix of grant and credit resources.

Annex 1: Countries participating in the FCPF Readiness Fund and UN-REDD Programme[6] (excluding current FIP pilot countries)

1	Argentina	23	Liberia
2	Bangladesh	24	Madagascar
3	Bolivia	25	Mozambique
4	Bhutan	26	Nepal
5	Cambodia	27	Nicaragua
6	Cameroon	28	Nigeria
7	Chile	29	Pakistan
8	Colombia	30	Panama
9	Congo, Republic of	31	Papua New Guinea
10	Central African Republic	32	Philippines
11	Costa Rica	33	Paraguay
12	Côte d'Ivoire	34	Suriname
13	Dominican Republic	35	Solomon Islands
14	Ecuador	36	Sri Lanka
15	El Salvador	37	Tanzania
16	Ethiopia	38	Thailand
17	Fiji	39	Togo
18	Gabon	40	Uganda
19	Guatemala	41	Vanuatu
20	Guyana	42	Vietnam
21	Honduras	43	Zambia
22	Kenya		

[6] As of May 2014.

Annex 2: Patient Capital for Sustainable Agroforestry Private Sector Projects (Submitted by AfDB)

AfDB is exploring the possibility of providing Patient Capital to Agroforestry projects in SCF countries, through an investment vehicle (the Fund) with a final targeted size of USD 135 million which will invest in profitable agroforestry projects with high environmental and social impacts.

The Fund would invest, via equity and quasi-equity, in 10 to 15 agroforestry projects across SCF pilot countries in Sub-Saharan Africa[7] and Latin America, allowing the implementation of profitable economical models while providing positive benefits for the local populations and the environment.

The targeted projects integrate environmental, social as well as economic aspects of sustainable development. Specifically, the combination of trees and other woody plants with agricultural crops or animal husbandry contribute to:

(i) Soil improvement, erosion-control, water availability and favorable micro-climatic conditions

(ii) The production of timber, firewood as well as tree crops (fruit and nuts), thus avoiding deforestation in adjacent forest areas

(iii) Higher productivity and profitability

(iv) Resilience in relation to changing climatic conditions

(v) The potential for tradable environmental credits (including carbon credits)

(vi) Social development, local entrepreneurship and employment

(vii) Long-term viability of the local economy and livelihood of local communities

Investors supplying patient capital in the form of equity investments with a long time horizon are uniquely well placed to provide the capital that is required to establish and grow such businesses. Patient capital does not require short-term interest payments, which reduces pressure on the enterprises that benefit from investment. The interests of equity investors are closely aligned with those of the other shareholders of the targeted enterprises themselves. Equity investors are therefore incentivised to add value to such businesses and work in close partnership with other shareholders to ensure the success of the business. Equity investors typically add value by ensuring effective governance, high ethical and Environmental, Social and Governance standards, well developed strategies, and capacity building at enterprise and community level. Agroforestry is an attractive strategy because it creates a strong and diversified platform

[7] As per AfDB's rules and procedures, any financial resources implemented by AfDB as part of this transaction would need to be domiciled in Africa and utilized, at the portfolio level, only for the benefit of African projects.

for the development of forestry sector businesses, whilst also paying attention to the need for agricultural production. Smallholders benefit from an income diversification supported by an investor with a long time horizon.

The Fund has a strong climate change mitigation impact through afforestation / reforestation and avoided deforestation & degradation (estimated to be around 15 $MtCO_2$ over the 12 year lifetime of the fund) thanks to the development of state of the art agroforestry techniques. It has developed a robust Environmental & Social Management System that provide clear safeguards regarding issues such as livelihoods, land tenure or biodiversity conservation. These safeguards would be assessed against AfDB's safeguards to ensure alignment.

The Fund focuses on the development of out-grower schemes with the potential for creating substantial income growth and livelihood improvements for smallholder farmers and will develop and upscale existing small-scale agroforestry initiatives.