Turning pipelines into investments: key bottlenecks in the forest and nature-based sectors

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Workshop: How to unlock nature-positive investments in your country?

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Content

- What will EDFIs invest into? The investment universe
- Key bottlenecks when investing in nature-based solutions
- Additional challenges related to EDFIs’ way of operating
- The EDFI Carbon Sinks global guarantee programme
- The role of technical assistance: examples
- What additional support for market development could catalyse

What will EDFIs invest into? The investment universe

Nature-based Solutions (NbS): **“actions to protect, sustainably manage, and restore natural or modified ecosystems, that address societal challenges effectively and adaptively, simultaneously providing human well-being and biodiversity effects” (IUCN, 2020)**

Carbon sinks: **ecosystems that absorb more CO_2 than they release (forests, oceans, soil)**

Forest product processing

Plantation forestry

Smallholder forestry & outgrower schemes

Natural forests

Climate-smart agriculture & other ecosystems

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Key bottlenecks when investing in nature-based solutions

Risks / obstacles to investors	Timber is main source of revenue	Carbon credits are main source of revenue
Land tenure insecurity (particularly in post-conflict countries / countries with agricultural reforms), complicated land-use regulations & corruption	x	x
Underdeveloped **infrastructure** (e.g. roads, ports) and supply chains (e.g. sawmills)	x	
Competition with cheap timber from **illegal logging**, no clear governmental regulations or incentives (e.g. public infrastructure projects) – particularly in SSA	x	
Limited technical forestry management skills (only few firms) / specific expertise (e.g. in cooperating with indigenous peoples)	x	(x)
Very long production cycles (i.e. **high upfront investments** with long ramp-up period until first cash flows)…	x	x
…often without the possibility of early exits	x	
Limited financial performance as compared to other investments (opportunity costs)	x	(x)
Dependency on **carbon credits as only financial return**, usually no other collateral (e.g. land assets)		x
Future price developments on the voluntary carbon market are highly uncertain		x
Many „first time“ fund managers without relevant track record		x
Natural disaster risk (e.g. fires, droughts, pests)	x	x

Additional challenges related to EDFIs' way of operating

- EDFIs provide financing to the private sector – hence, **EDFIs depend on reputable & successful private stakeholders** in partner countries!
- Private-sector focused EDFIs have **little/no influence on government policies** / regulatory frameworks / other enabling conditions in partner countries
- Some EDFIs do not receive any government funding, hence **need to be financially sustainable** → clients are usually established companies (required EDFI ticket sizes of >7m EUR → project sizes of >20m EUR)
- Some EDFIs do not count with sufficient funding to offer technical assistance to clients (very helpful to enhance developmental impacts)

The EDFI Carbon Sinks global guarantee programme - now under negotiation!

- Allocation of up to **366 million EUR** in guarantees, plus 24.78 million EUR in technical assistance
- Managed by EDFI MC (TA will be managed by DEG) and accessible to all European DFIs

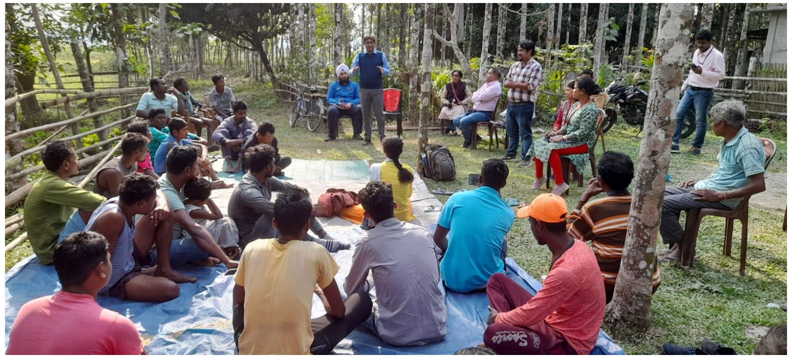
- The programme:
  - Covers all 5 sub-sectors of carbon sinks investments!
  - Contributes to the Paris Agreement and has numerous co-benefits: **biodiversity** protection, **adaptation** to climate change (resilient ecosystems), enhanced **livelihoods** for local communities, and others
  - Allows EDFIs to conduct **more investments**, and invest with **larger tickets**
  - Allows EDFIs to invest in project types that were (up to now) out-of-range due to their **high risks** (e.g. carbon credit funds and projects)…
  - ….and in countries/regions with more **challenging investment environments**
  - Serves the mobilisation of additional investments from the private sector / other sources (> 8 bn. EUR)

Overall, the programme aims to significantly strengthen and further develop private sector engagement in the NbS market!

The role of Technical Assistance: examples

- TA in the NbS sector can include:
  - support to companies and funds in establishing their environmental & social risk management systems / compliance with IFC performance standards
  - **feasibility studies**, for example:
    - potential of carbon credit certification
    - outgrower schemes with forestry companies
    - supplementary business models, such as eco tourism
  - implementation of **pilot projects** to test new approaches / methodologies
  - support to "new" carbon credit fund managers in navigating the voluntary carbon market
  - development of **instruments and tools** to increase (impact) performance

Case I: Agroforestry feasibility study with Aavishkaar Capital for their first carbon credit fund



Case II: E&S app with forestry fund Arbaro

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What an additional blending programme – beyond the guarantee programme – could catalyse

- Key challenges that can be addressed by a complementary blending programme:
  - The carbon sinks market is still nascent and in **need of further innovations** / new methodologies / proof of concept to scale projects
  - Many **market players are "new"** and need to build their track records / need help strengthening their business models or navigating the carbon market
  - **Pipelines are limited** for certain regions/countries (e.g. SSA, NEAR)

- EDFIs (via EDFI MC) are considering applying for EU blending to be able to implement a market development facility:
  - "CarbonFI" would be an **origination & market development facility**
  - Target investments:
    - i) **early-stage** projects / companies or funds in need of support to become "investable" / build track record
    - ii) particularly **innovative approaches** that show up-scaling potential (e.g. piloting new methodologies)
  - Goals:
    - i) **build pipeline** → successful projects "graduate" into EFSD+ guarantee programme
    - ii) play a role in **shaping the NbS market** through innovation
    - iii) build up **know-how** and experience in this nascent sector

- Set-up / structure, instruments and further details still under discussion!