

PRIVATE SECTOR INVESTMENTS IN FORESTS: EARLY EXPERIENCES FROM INDONESIA & LAO PDR



Dr. Michael Brady
FIP Pilot Country Meeting
Kinshasa, June 2015

CONTENTS

IFC and the Forestry & Wood Products Sector

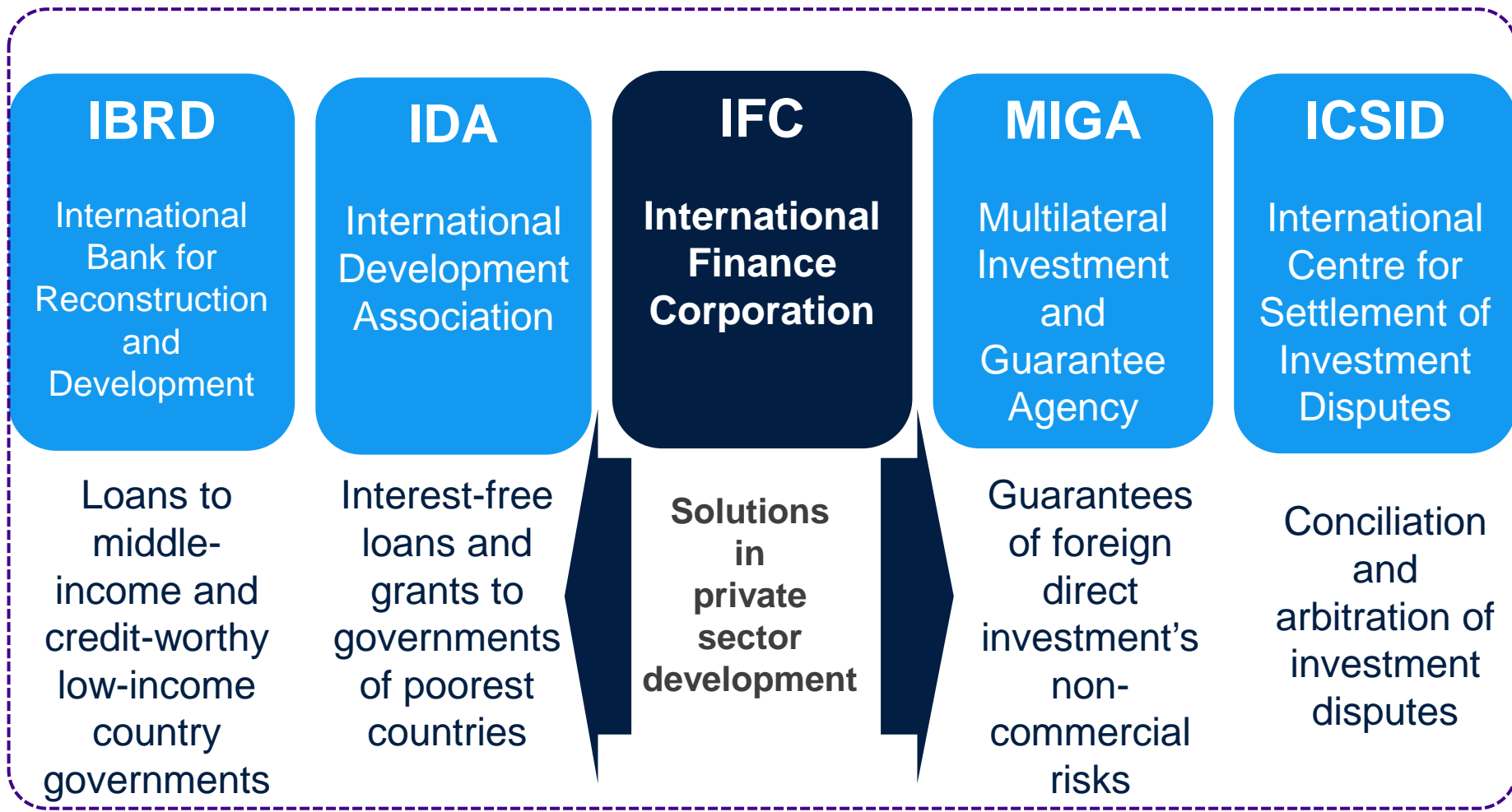
Market Barriers to Forest Sector Investments

Considerations for FIP Private Sector Engagement

Lao PDR Program Implementation

Indonesia Program Planning

IFC: A MEMBER OF THE WORLD BANK GROUP



WHAT WE DO

Integrated Solutions, Increased Impact

3 Focus
Industries:

MANUFACTURING
AGRIBUSINESS &
SERVICES

FINANCIAL INSTITUTIONS

INFRASTRUCTURE AND
NATURAL RESOURCES

3 Product
Areas:

INVESTMENT

(Debt, Equity, Trade Finance, Syndications, Securitized
Finance, Risk Management)

ADVICE

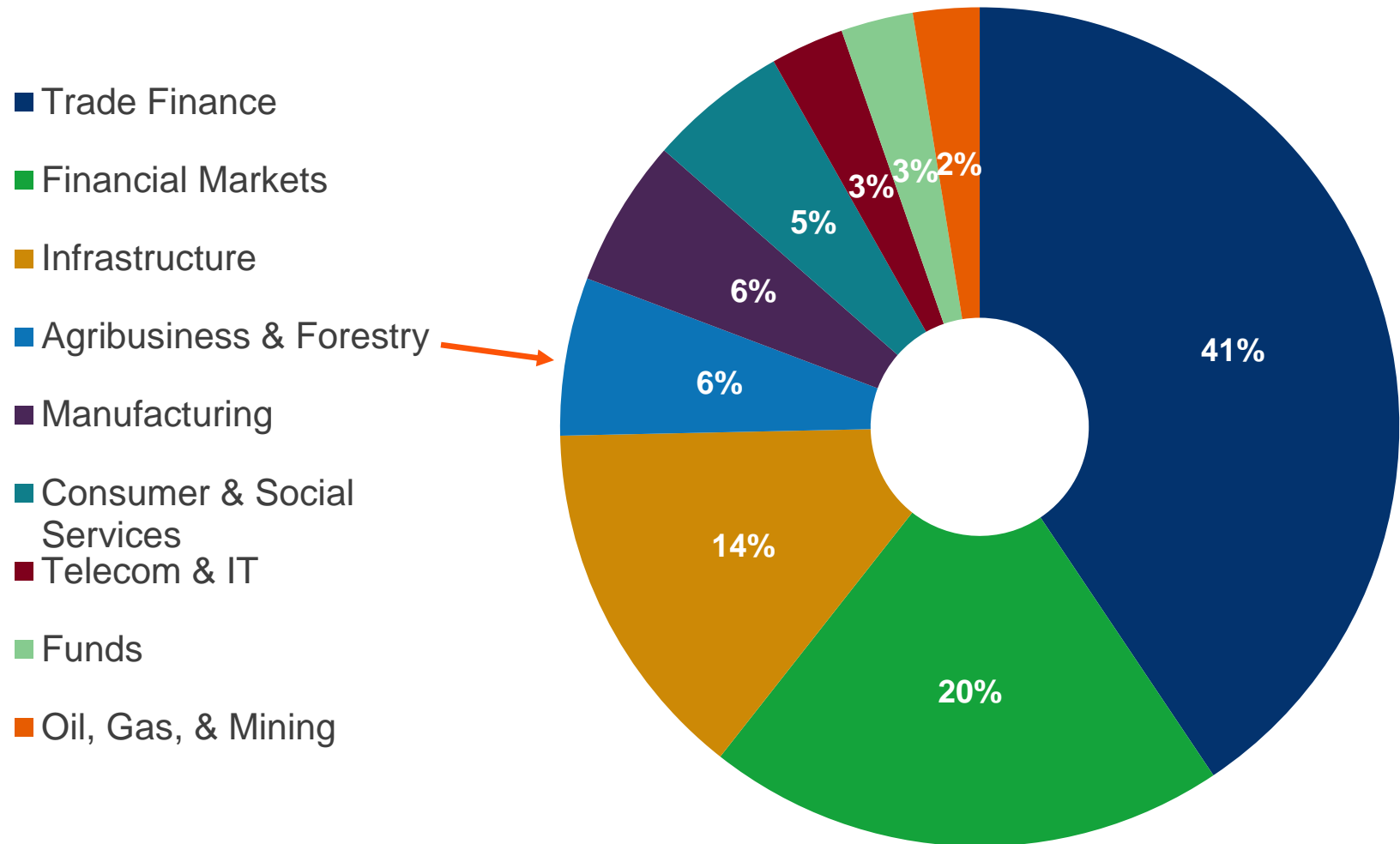
(Integrated with IFC Investment)

IFC ASSET MANAGEMENT COMPANY

(Mobilizing and Managing Capital for Investment)

INVESTMENTS BY INDUSTRY, FY14

COMMITMENTS FOR IFC'S ACCOUNT: \$17.3 BILLION



FIP IS ADDRESSING COMMON MARKET BARRIERS TO PRIVATE SECTOR FORESTRY

Mismatch between supply and demand - not enough legal, high quality, commercially available industrial roundwood available for the wood processing industry

Problems in access to forestry land and wood supplies due to lack of trust (between firms and communities) and problems around the concession allocation system, leading to insufficient investment and new planting of forest land

Lack of cashflow to complete the wood harvest cycle (for communities) – even if the business case is solid, not all communities can afford to invest with a promise of returns in 8 - 14 years' time

Lack of affordable services for community forest enterprises (CFE) around contract negotiation, general business administration and operational forest management



SME FINANCING NEEDS AND SOURCES

Needs:

- Pre harvest finance
- Inputs
- Operations
- Trade credit/export credit
- Term lending
- Infrastructure development

Sources:

- Supply chain finance involving off-taker lead firms
- Direct financing through financial intermediaries
- Other farm and off farm revenues, including PES
- Concessional loans, public grants



CONSIDERATIONS FOR FIP PRIVATE SECTOR ENGAGEMENT

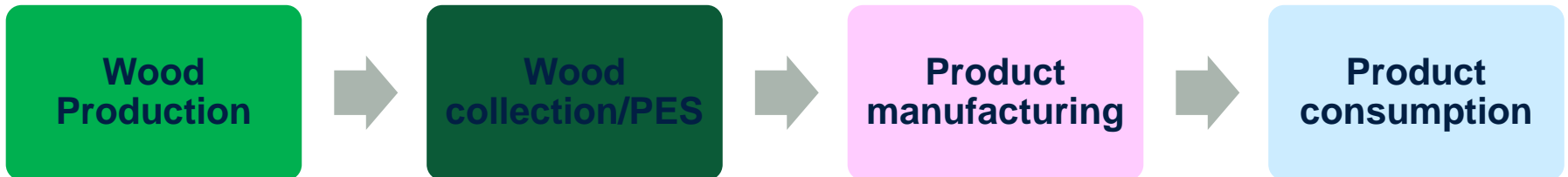
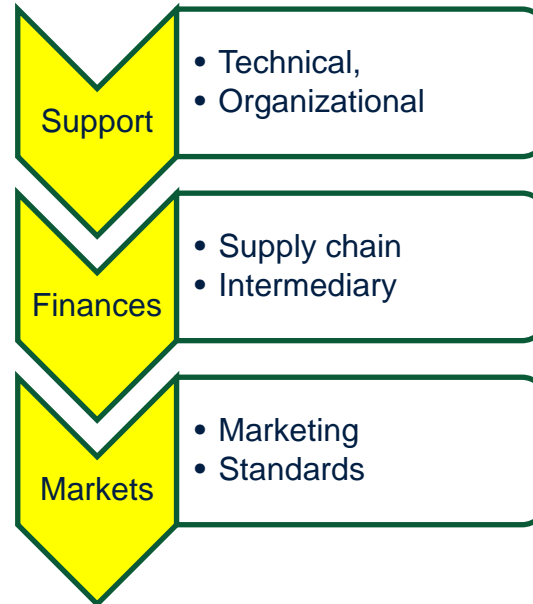
- 5-Year program framework
- Systematic survey of private sector enterprise and growth plans
- Consultation on program proposal
- Start with pilot involving 1-2 lead firms and supply chains
- Replication involving 3-4 firms
- Use IFC systems for advisory and investment services
- Collaboration with FIP pilot country agencies, other MDBs and FIP Subcommittee



IFC FIP PROGRAM APPROACH

STRENGTHENING SUPPLY CHAINS OF FOREST AND WOOD PRODUCTS SECTOR

IFC adopts a 'Lead Firm' approach when addressing supply chains, particularly in frontier sectors



LEAD FIRMS ARE ENGAGED TO AGGREGATE FORESTRY SMES TO ACHIEVE REACH AND SCALE

- Off take agreements
- Planting sites (suitability, preparation)
- Access to quality plantation inputs (seedlings, fertiliser)
- Provision of technical expertise (agriculture, pasture + forestry)
- Training
- Facilitate liaison with GoI processes
- Pursue opportunities to add value



ADVISORY SERVICES IS A KEY NEED FOR FIP INVESTMENTS WITH FORESTRY CLIENTS

Offer potential firms advisory services around FIP themes

- 1. Strategic Community Investment**
 - relationship and investments with affected communities
- 2. Develop New Supply Chains Models, Additional Supplies**
 - enhanced livelihood opportunities for communities
- 3. Forestry Extension Units**
 - promote private sector-led extension services in working with communities, FMUs
- 4. New (Financial) Partnership Models**
 - e.g., lead firm, out-grower, in-kind loans, securitization of wood growth
- 5. Enhance Client E&S Performance**
 - compliance with the requirements of financial institutions
- 6. Resource Efficiency**
 - more efficient use of energy, water, and materials



INVESTMENTS IN PRIVATE SECTOR FORESTRY REQUIRE SUBSTANTIAL ASSESSMENTS OF RISK

- Lack of interest from lead firms
- Business viability risks, including markets
- Physical and social risks
- Lack of traction with forest communities
- Negative perception of IFC's efforts by NGOs and other stakeholders



FIP PRIVATE SECTOR PROGRAM RISKS MITIGATED BY

(1) IFC Safeguard Policy

- 1 Assessment and management of environmental and social risks and impacts
- 2 Labor and working conditions
- 3 Resource efficiency and pollution prevention
- 4 Community, health, safety and security
- 5 Land acquisition and involuntary resettlement
- 6 Biodiversity conservation and sustainable management of living natural resources
- 7 Indigenous peoples
- 8 Cultural heritage

FIP PRIVATE SECTOR PROGRAM RISKS MITIGATED BY (2) IFC CLIENT ENGAGEMENT POLICIES

- Internal Due Diligence
- Politically Exposed Persons
- Environment & Social Performance Standards and Action Plan
- Public Disclosure
- Client Fee Contributions



STATUS OF PRIVATE SECTOR PROJECTS IN EAST ASIA

| Project element | Indonesia | Lao PDR |
|-----------------------------|--------------------|--------------------|
| National Investment Plan | Q4 2012 | Q4 2011 |
| Project preparation* | 2012-2015 | 2012 |
| Project approval - IFC | Q4 2015 | Q1 2013 |
| Project approval – FIP SC | Q4 2015 | Q2 2013 |
| Project pre-implementation* | Q1 2016 | Q2 2013 |
| Project implementation | Q2 2016 (1 client) | Q2 2015 (1 client) |

*Address FIP safeguards & IFC performance standards



LAO PDR PROGRAM AIM

The Program supports the development of business models for community based reforestation of degraded and underutilized land through the following activities:

1. **Establish efficient community - forestry company partnerships** through the development of comprehensive engagement models, identifying both company and farmer expected roles.
2. **Assist the Government of Lao PDR in providing land security** for the participating enterprises and communities so that they develop an asset and improve land management.
3. **Organize participating farmers into groups and build capacity** around group operation so that farmer representation improves through collectivization.
4. **Enhance farmer technical skills** with the help of companies so that farmers learn new farming techniques and improve productivity.



PROGRAM OBJECTIVES

The overall program will achieve up to:

- 15,000 hectares sustainably managed land of which at least 50% is new forest cover
- 253,270 tCO₂e per year of GHG emissions reduced
- US \$10 million investment in forestry and wood product enterprise
- 150 group contracts signed with the private sector participating in the project
- 15,000 farmers trained in farming and business practices



PROSPECTIVE CLIENTS (ADVISORY AND INVESTMENT)

The private sector FIP supports the development of business models for industrial and community based reforestation of degraded land

Lao PDR, Department of Forestry:

- Plantation Directorate, Tree Plantation Extension Division. Strengthen capacity to develop policy, regulations and administrative management of the plantation sector

Plantation Companies:

- International forest and wood product companies with industrial plantations

Wood Product Companies:

- National wood product manufacturing companies and their respective supply chains, including locally planted teak, sawmills & transporters

Public-Private Climate Change Partnership:

- National company formally engaged with GoL to develop REDD+ carbon revenues from 350,000 hectare project area



FIRST PROJECT WITH AGROFORESTRY COMPANY

Client is an international forestry and wood product company developing a multi use tree plantation with substantial community engagement in agroforestry. IFC investment to be considered following advisory services on:

1. Stakeholder Identification and Engagement Planning, including procedures for Free Prior and Informed Consent (FPIC)

- Improvement of land acquisition process
- Land compensation
- Human rights action planning
- Communication planning (internal and external)
- High conservation value (HCV) assessment and sustainability certification systems

2. Land Acquisition and Concession Licensing

- Assess the new licensing requirements as they apply to company expansion plans and recommend strategies to address them



COORDINATION BETWEEN PUBLIC AND PRIVATE SECTOR FIP PROJECTS

KEY PLANTATION ISSUES BEING ADDRESSED WITH DEPARTMENT OF FORESTRY PLANTATION DIVISION

1. Performance review of tree plantation development policy & targets
2. Plantation concession licensing
3. Effectiveness of contracting between companies and smallholders
4. Certification issues for community plantations
5. Wood supply extension and marketing



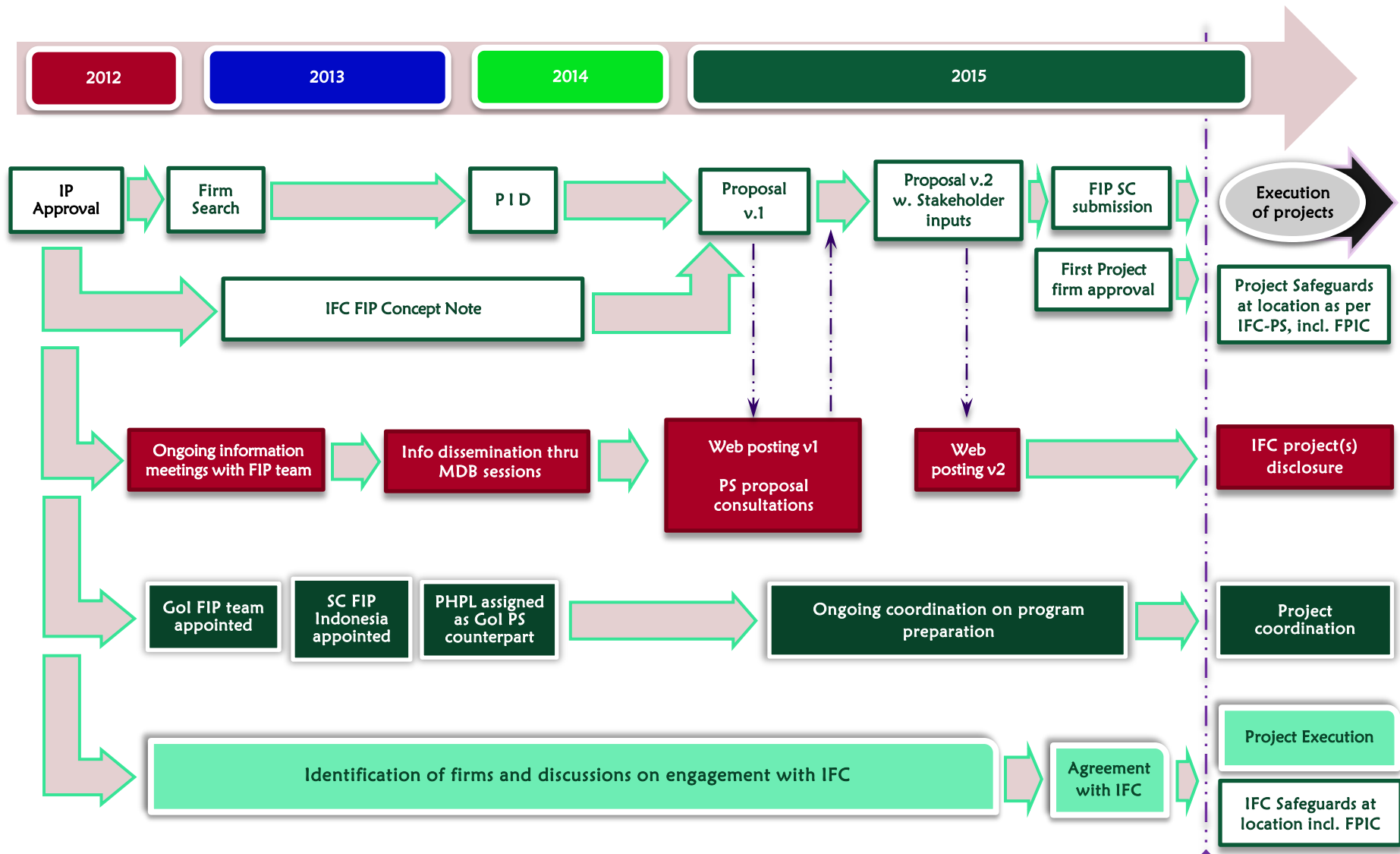
INDONESIA PROGRAM AIM AND OBJECTIVES

Partner with downstream and integrated forestry lead firms to increase planted forests, enhance wood supplies, and improve E&S performance and production efficiency

1. **Improve and expand the wood supply chain** by working with lead firms and their upstream partners on improvement of community relations, development of new product chains, and extension-type assistance on forest operations management
2. **Expand planted forests** by creating innovative partnerships with community forestry enterprises around farm and plantation management, including access to finance and markets
3. **Improve firm E&S performance and production efficiency** by providing support in implementing E&S systems and measures, and assist in developing cost savings based on resources efficiency analysis



PREPARATION OF INDONESIA PRIVATE SECTOR FIP



PID : Project Information Document
 CIF : Climate Investment Fund
 FPIC : Free Prior and Informed Consent
 IFC-PS : IFC Performance Standard

Gol : Government of Indonesia
 SC : Steering Committee
 PHPL: DG of Sustainable Management of Production Forest
 KPH : Forest Management Unit (FMU)

PROSPECTIVE CLIENTS (ADVISORY AND INVESTMENT)

1. Wood Product Factory with Community and Industrial Plantation

- Glulam and veneer products from rubber wood industry with supply chain challenges
- Biomass energy plantation and wood pellet mill development



2. Pencil Factory with Community Plantations

- FSC wood pencil slat industry and wood supply chain
- Wood pellet mill from wood waste and biomass energy plantation



3. Wood Product Factory with Community Plantations and Protection Reforestation

- Plywood industry and handicrafts with supply chain constraints
- Community plantation development with state reforestation company

4. Industrial Plantation with Conservation Set Aside

- Community engagement in conservation and outgrower scheme

5. Private Company Managing Ecosystem Restoration Concession

- Carbon credit sales



COORDINATION BETWEEN PUBLIC AND PRIVATE SECTOR FIP PROJECTS

ADDRESS SUB-NATIONAL BARRIERS IN FOREST MANAGEMENT UNITS (FMU)

1. WB program theme: Reduce national and sub-national institutional barriers to sustainable forest management and REDD+

National level:

Strengthen institutional, financial, and technical capacity and support FMU policy dialogue within the MOFOR

Sub national levels:

i) Strengthen knowledge generation with focus on participatory land-use planning processes

ii) Assist three pilot FMUs to become operational and to engage with local communities and other stakeholders.

2. IFC program theme: Strengthen the productive capacities and business skills of forest and wood product enterprises by leveraging private sector investments

Formulate guidance for FMUs to strengthen business enabling environments to attract private sector enterprise

i) Improve the viability of small and large forestry enterprises through advice and investment

ii) Build capacity in pilot FMUs to improve business enabling environment and engage with enterprise