Forestry and Climate Change Fund

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Change Fund

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Value Creation From the Ground up

Tropical forests are vitally important eco-systems, with ecological, economic and sociocultural benefits. They harbour biodiversity, provide a regenerating stream of resources and absorb high amounts of carbon. Over the past decades, around 30% of global forest cover has been completely cleared and an additional 20% has been degraded to make space for agriculture and other human activities. Consequently, large areas of forest remain degraded and marked by human intervention. A mosaic of secondary and degraded forests (SDF) emerges between agricultural lands and primary forests.

Investing for Development SICAV launches the Forestry and Climate Change Fund (FCCF), a Fund aiming to demonstrate that sustainable forestry generates high environmental, economic and developmental value. This impact investment fund seeks to pioneer a viable business model for timber production within secondary & degraded forests. At the core of the FCCF lie long term partnerships with a climate change mitigation objective. With this, the FCCF hopes to give secondary and degraded forests economic value, to better match its ecological and social importance.

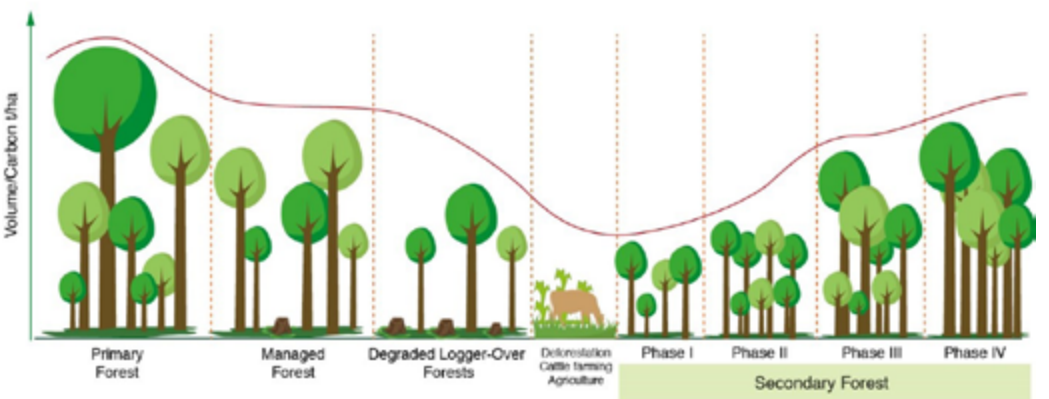
Our Mission

In order to realize this vision, FCCF:

- balances ecological and social impact with attractive long term financial returns;
- creates and disseminates knowledge on business models adapted to the specifics of secondary and degraded tropical forests
- forges lasting alliances with local communities and locally rooted entities. This supports the long-term vision by which forests find their place within economically and ecologically functioning landscapes;
- contributes internationally and in Luxembourg to growing interest in climate financing;
- considers the global significance of SDFs and seeks to expand the approach beyond Central America in the long-term.

Secondary and Degraded Forests

FIGURE 1
TRANSITION FROM DEGRADED LOGGED-OVER FOREST TO SECONDARY FOREST



Source: Defining Secondary and Degraded Forests in Central America - Working Paper, CATIE

Secondary Forests

Secondary Forests are forests regenerating through a natural succession process after very significant and/or total human or natural disturbance of the original forest. They show major difference in structure, species composition, and age profile compared to primary forests.

Degraded Forests

Degraded Forests are forests which have been harvested unsustainably. In degraded forests, the commercial timber was logged beyond the natural growth capacity of the system (logged-over). The extraction is generally done by "conventional logging", without applying the principles of reduced impact logging. Such practices leave the forest overexploited to such a degree that a gradual recovery to a forest similar to primary forest is no longer feasible.

> "The Forest Resources Assessment report 2015 found that the area of naturally regenerated forests (…) constitutes 58% of the overall global forest area." (FAO, 2015)

Figure 1 shows the forest transition curve and serves as basis to define the scope of the projects that will be considered for the secondary and degraded forests management initiative.

Economic, Environmental and Social Impact

The FCCF creates multiple layers of impact.

Economic Impact

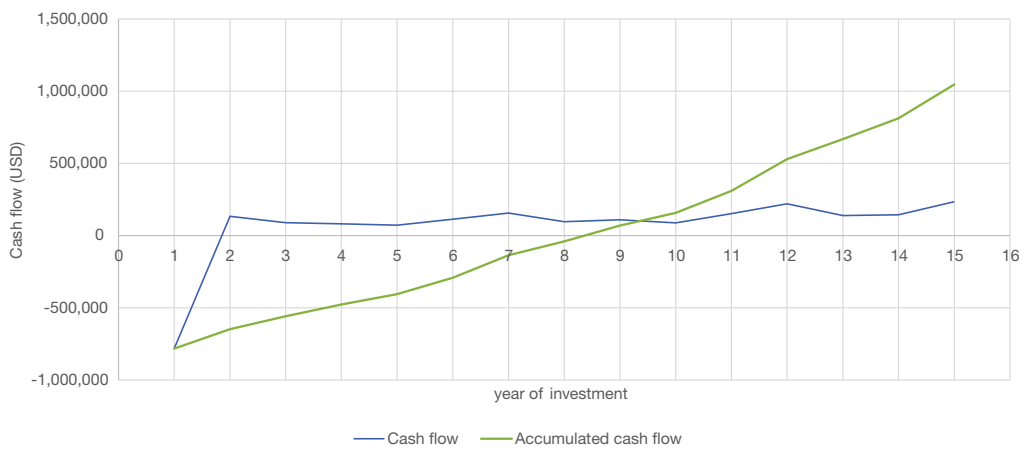
The FCCF pioneers a business model for timber production of secondary and degraded forests primarily for local markets. The model is based on existing market demands, leveraging local and regional value chains.

Business models are not focused on optimizing productivity per hectare but on minimizing investments in manpower, road-network and other resources to produce commercial timber and rely on natural productivity.

The viability of local business cases is determined by potential income from the main competing activity: in many cases extensive cattle farming. In many cases SDFs show to be economically attractive, with higher return than alternative land use. An investment in an existing SDF aged at least 15-20 years is expected to have an attractive cash-flow and generate income within a few years.

At the core of the business model lie sustainable forestry practices and its bottom-up approach. Cooperative models and profit sharing schemes ensure that the economic benefits are shared equitably amongst actors. Local actors largely retain control over the projects and land. To further ensure the sustainability of the project, land

GRAPH 1
EXAMPLE OF A PROJECT LEVEL CASH-FLOW PROFILE GENERATING POSITIVE INCOME FROM YEAR 2 ONWARDS



Source: UNIQUE analysis of FCCF pipeline

acquisition by the FCCF is avoided. With this, the FCCF differs from many conventional forestry approaches and timberland funds.

Sustainable management of SDF is innovative and differs from both plantation forestry on the one hand and natural primary tropical forest management on the other. Most forestry projects today either consist of the protection, conservation and management of primary forests or of conventional even-aged forest management. To reconcile ecological and economic objectives, the approach should be based on a set of alternative principles including the avoidance of clearcutting, emphasis on structural diversity, small scale variability, the deployment of mixed local species with natural regeneration and the avoidance of intensive site preparation.

These principles ensure the balance between ecological concerns and importance of local biodiversity, economic interest to optimize monetary value-creation and long-term social interest to have functioning forest eco-systems.

Sustainable forestry practices for SDF

	Conventional	Approach for SDF
Economic	• Profit maximization • Focus on productivity • Focus international markets • Focus on intensive exploitation of limited number of valuable species	• Multiple success factors, people, profit, planet • Focus on rationalizing interventions, lower costs • Focus on local & regional markets • High value speciality timber, diversity
Social	• Competing land use model • Buying land, foreign ownership • Hiring labour especially on temporary basis	• Integration in existing land use practices • Cooperation models, local ownership • Land lease • Benefit sharing
Ecological	• Monocultures (even aged) • Focus on few foreign species • Genetically improved species • Extensive use of pesticides • Use of fertilizers • Small conservation areas	• Biological diversity (uneven aged) • Harvesting adapted to types of tree species • Marketable and non-marketable native species and non-timber forest products • Locally occurring genetics • No pesticides, fertilizers • Overlay of conservation and production
Technical	• Management top-down • Managing nature as a risk • Mechanisation • Low complexity	• Management of bottom-up approaches • Managing nature as a resource • Biological rationalization, natural regeneration • Higher complexity

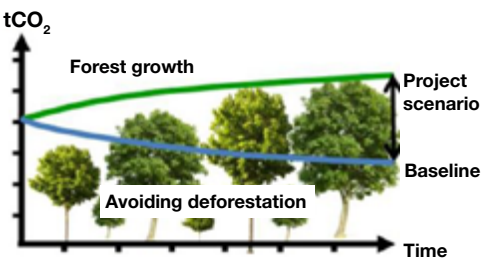
Environmental Impact

Mesoamerican forests are one of the largest biodiversity hotspots on earth. These areas with significant numbers of endemic species are currently under threat. Many species are in dramatic decline mainly due to habitat loss. The FCCF offers a model by which the forests hosting such biodiversity are enabled to recover. The actions of the Fund should contribute to the preservation of soil and water.

Beyond their importance for the local environment, these forests contribute to climate change mitigation in important ways. Forests present a low-cost, nature-based solution for carbon sequestration. The FCCF protects the SDF from deforestation for alternative land use, facilitates the absorption and long-term storage of carbon to unfold. This potential can be enhanced by adequate management. Further controlled regrowth of secondary forests represents an excellent opportunity to absorb CO2 and mitigate climate change.
Secondary and degraded forests grow rapidly and sequester larger amounts of carbon in their biomass, but they tend to be ignored, as most of the debate on the carbon balance tends to revolve around deforestation risks of old-growth forests and afforestation projects on degraded lands.

Well managed secondary forests are important contributors to carbon sequestration and thus to REDD+.

GRAPH 2: CARBON STOCK ENHANCEMENT THROUGH IMPROVED FOREST MANAGMENT (IFM)



Source: Carbon Accounting in Secondary Forest - UNIQUE

The estimate of carbon sequestered by the FCCF was developed by UNIQUE following Intergovernmental Panel on Climate Change (IPCC) methodologies as well as project specific recommendations and methodologies from the Verified Carbon Standard (VCS).

Carbon sequestration achieved by the FCCF is done so through three main sources:

1. Avoiding **deforestation** when the project protects the secondary forest from land use changes;

2. **Balance** between carbon stock enhancement in the forest through improved forest management and preservation considering the extraction rate;

3. **Substitution** effect of harvested wood products from extracted wood. This substitution effect comes about as wood-based products are (1) a physical pool of carbon, (2) a substitute for more energy-intensive materials and (3) raw material to generate energy (IPCC,2001).

Social Impact

FCCF aims to generate sustainable income streams for those living around the forests and secure a flow of ecosystem services. They provide a safety net from rural communities when crop fails and act as a buffer for impacts of climate change and natural hazards. Through these channels, SDF can reduce social vulnerabilities.

The FCCF follows a bottom-up approach with a strong community focus. In the target countries, significant areas of SDF are owned by smallholders and local communities. The Fund focuses on building financing and technical solutions addressing the needs of smallholders and communities. A key condition for such solutions is the efficient aggregation of smallholders through agricultural cooperatives or other structures. It is important to note that FCCF will normally avoid acquiring land.

Ownership and use of SDF are closely linked to local communities. These communities tend to be poorer and less developed compared to urban and peri-urban communities. Poverty rates are twice as high and access to basic services including education, health care and social protection is scarce. This is especially true for smallholders and indigenous populations.

Hence the development of forestry management practices for SDF needs go hand in hand with social development opportunities for the local communities. Forests need to provide concrete benefits to local communities to ensure their long-term development. Regular and reliable income, either through paid work for forestry intervention in SDF, land lease payments, profit sharing schemes or secure employment, are key to ensuring that benefits materialize for the community.

FIGURE 2:
TYPES OF PARTNERSHIPS PURSUED BY FCCF

Smallholders

likely to hold < 100 ha

Community forestry

control over large forest areas > 1.000 ha

Larger private landowners

ownership of > 1.000 ha, strategic interest in SDF timber production

Combining technical assistance and investments efficiently

Climate finance often emphasizes the challenge to mobilize the substantial financial resources needed to transform the global economy and land use practices to a low-carbon environment. The mobilization of investments also depends on the availability of attractive investment propositions.

In many areas these opportunities are still scarce and business models insufficiently developed.

Therefore the Fund is complemented by a Technical Assistance Programme which has worked to generate the pipeline, knowledge and certainty required to enable the Fund to invest.

Secondary and degraded forest landscapes in Nicaragua

Community managed forestry in the RAAN, Nicaragua // CATIE

Important Information

This material comprises information relating to the Forestry and Climate Change Fund (FCCF), a Sub-Fund of the Investing for Development SICAV investing in tropical forestry projects with high environmental, economic and developmental impact.

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