

INTER-AGENCY TASK FORCE
ON FINANCING FOR DEVELOPMENT

Issue Brief Series



Forest Finance

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SUSTAINABLE DEVELOPMENT GOALS
17 GOALS TO TRANSFORM OUR WORLD



FINANCING FOR DEVELOPMENT

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Forest Finance United Nations Forum on Forests

1. Introduction

Forest finance is understood to refer to all forms of financing for sustainable forest management (SFM). It is the primary focus of paragraph 63 of the Addis Ababa Action Agenda (“Encourages the mobilisation of financial resources from all sources to conserve and sustainably use biodiversity and ecosystems, including promoting sustainable forest management”) and of target 15.b of the Sustainable Development Goals (SDGs) (“Mobilize significant resources from all sources and at all levels to finance sustainable forest management and provide adequate incentives to developing countries to advance such management, including for conservation and reforestation”), while also being relevant for a number of other paragraphs of the Addis Ababa Action Agenda and of other SDGs. As an increasingly important component of forest finance, REDD+¹ is also discussed in this brief.

2. Stocktaking

2.a. Forest finance is characterised by blurred definitions, data gaps and fragmentation

The general classification of financing for sustainable development can easily be applied to forest finance which breaks down into the following categories:

- Public international financing, notably official development assistance (ODA);
- Private international financing, such as foreign direct investment;
- Public domestic financing, namely domestic resource mobilisation;
- Private domestic financing such as domestic investments; and
- Blended and innovative financing, including forest funds and REDD+.

However, this categorisation glosses over an important aspect of forest finance, namely its cross-sectoral nature. Sources of financing for SFM originate from the forest sector but also climate (such as REDD+), agriculture (through investments in mixed forest and agricultural systems known as agroforestry) and tourism (notably forest-based ecotourism), among other sectors and issues. In addition, financing SFM can be seen as distinct from financing unsustainable forms of forest management, notably management which degrades forests or even which prompts land conversion.

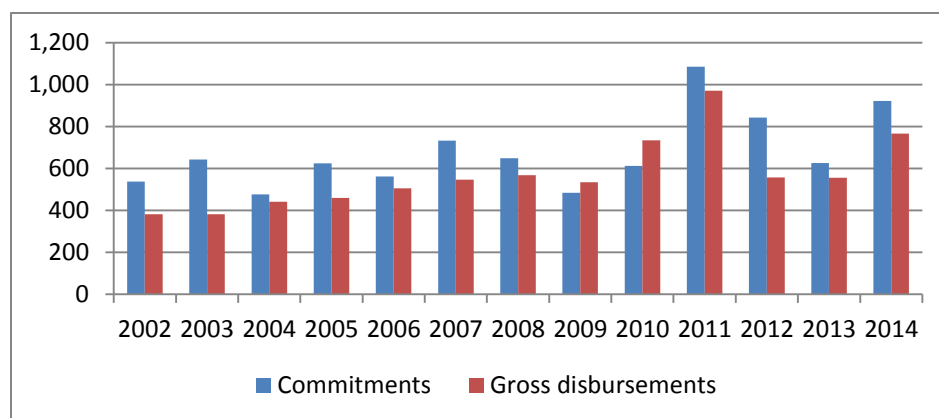
Forest finance is therefore composed of a wide array of different flows, public, private, domestic, international, from different stakeholders and sectors, and each with their own dynamics, distribution in time and space, and conditions for access. The highly fragmented nature of the resulting forest finance landscape, along with the blurry line between what is

¹ REDD+ stands for “Reducing emissions from deforestation and forest degradation, plus the role of conservation, sustainable management of forests, and the enhancement of forest carbon stocks”.

sustainable and what it not, partly explains the dearth of overall global figures for forest finance.² Instead, attempts have been made to quantify individual financial sources or categories such as the ones presented below.

The source of forest finance with most reliable data is forestry ODA, which has been systematically compiled by the Organization for Economic Cooperation and Development (OECD) since 2002 (see Figure 1). Figures show a gradual increase in gross disbursements from below US\$ 400 million in 2002 to almost US\$ 800 million in 2014. Since 2007, this increase has largely been due to the emergence of REDD+ financing, part of which (but not all) has been labelled as forestry ODA. Figure 1, however, smooths over the considerable disparities in forestry ODA distribution both geographically and over time which have raised issues about its reliability as a sustained source of forest finance.

Figure 1: Commitments and gross disbursements of forestry ODA 2002 to 2014 in US\$ millions³



Other sources of forest finance, however, suffer from major gaps in data with only a few sparse figures found in the literature. In 2008, private investment in the forest sector in developing countries and countries in transition was estimated by the World Bank at US\$ 15 billion,⁴ 24 times the value of forestry ODA for that year. Castrén *et al.* estimated annual total private forest plantation in developing countries alone at US\$ 1,763 billion, with 83% directed at Latin America and only 1% at Africa.⁵

² AGF (2012). *2012 Study on Forest Financing*. Unpublished report, 211 pp. Document available at http://www.un.org/esa/forests/pdf/AGF_Study_July_2012.pdf (retrieved 5 July 2016); and Singer, B (2016). Financing sustainable forest management in developing countries: the case for a holistic approach. *International Forestry Review* 18(1):96-109.

³ OECD Creditor Reporting System database (<http://stats.oecd.org/#>), retrieved 5 January 2016.

⁴ World Bank (2008). *Forest Source Book: Practical Guidance for Sustaining Forests in Development Cooperation*. Washington D.C.: World Bank, 402 pp.

⁵ Castrén, T., Katila, M., Lindroos, K. and Salmi, J. (2014). *Private Financing for Sustainable Forest Management and Forest Products in Developing Countries: Trends and drivers*. Washington, DC: Program on Forests (PROFOR), 127 pp.

According to FAO, private financing for SFM remains a fast-growing trend with a positive outlook⁶ and in recent years, institutional investors have grown to be the main market participants in developing countries with over 1,000 pension funds, endowments, foundations and others. From approximately US\$ 1 billion in 1983, investment in the “timberland” asset class had grown to US\$ billion in 2010, mostly in the United States. However, the focus on investments on developed countries appears to have since been inverted (Figure 2).

Even less is known about domestic forest finance, both public and private. No global data were located on either source of finance. If data on agriculture and forestry as a whole is anything to go by, however, it seems that domestic sources contribute the overwhelming majority of forest finance (see Figure 3).

Figure 2: Global inward FDI flows to wood and wood processing in 1990–1992 and 2008–2010 in millions of US\$⁷

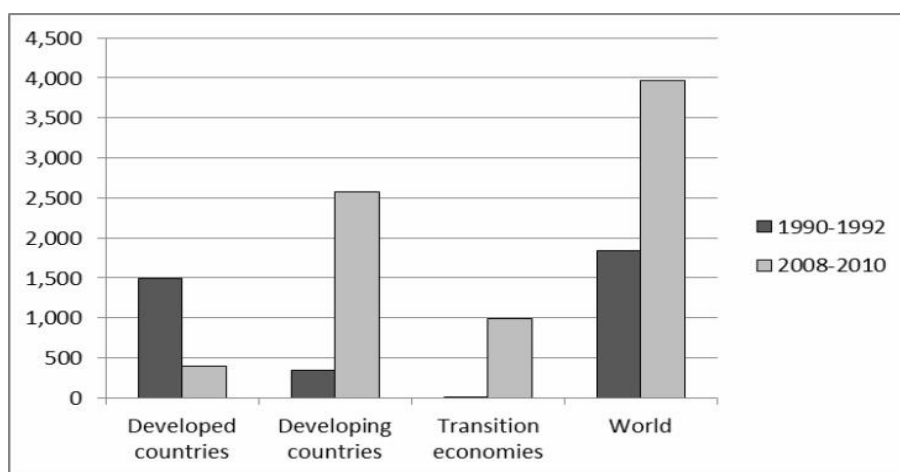
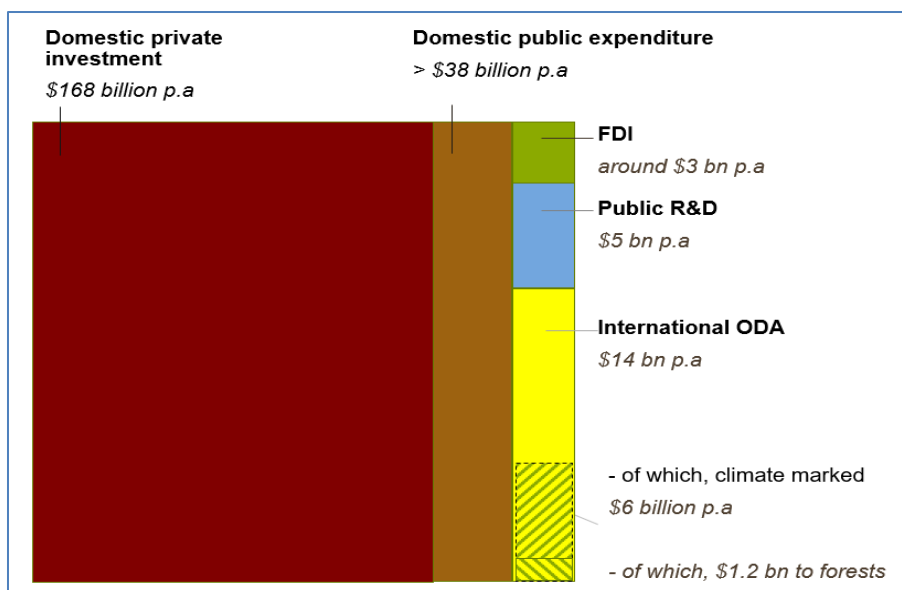


Figure 3: Sources of financing for agriculture and forestry combined at global level for 2012.⁸

⁶ FAO (2012). Timberland in institutional investment portfolios: can significant investment reach emerging markets? FAO Forestry Policy and Institutions Working Paper No. 31, 51 pp.

⁷ UNCTAD (2012). *World Investment Report 2012*. Geneva: UNCTAD, 239 pp.

⁸ Climate Policy Initiative (<http://www.slideshare.net/climatepolicyinitiative/sustainable-land-use-finance-opportunities-for-philanthropy>)



2.b. Forest finance is dwarfed by finance for unsustainable forms of forest management

While figures on financing sustainable forest management are hard to get by, research into levels of financing for unsustainable forest management is only just beginning. And yet the latter is a highly relevant topic in forest finance as it largely explains the economic rationale behind deforestation, particularly in developing countries. For instance, if a landowner is given the choice between maintaining natural forest and clearing it, and finds that converting to agriculture is much more lucrative, then deforestation is highly likely.

The last few years have given rise to a small number of studies related to this domain. Lawson⁹ calculated that 71% of all tropical deforestation between 2000 and 2012 was caused by commercial agriculture, with Brazil and Indonesia accounting for 75% of the global area of tropical forest converted illegally to commercial agriculture. McFarland *et al.*¹⁰ investigated subsidies to key commodities driving deforestation to find that Brazil provides over US\$ 10.5 billion and US\$ 14.3 billion annually in subsidies to beef and soy respectively, while Indonesia contributes US\$ 5.8 billion and US\$ 16.7 billion to timber and palm oil production respectively. All these figures make forestry ODA, which reached a “mere” US\$ 8 million for Brazil and US\$ 23 million for Indonesia in 2013, look like a drop in the ocean. Obviously, not all government subsidies in beef, soy, timber and palm oil are invested in unsustainable forms of forest management, but even a tiny percentage of these amounts still would still forestry ODA.

2.c. The growing “climatization” of forest finance

⁹ Lawson, S. (2014). Consumer goods and deforestation: an analysis of the extent and nature of illegality in forest conversion for agriculture and timber plantations. *Forest Trends*, 158 pp.

¹⁰ McFarland, W., Whitley, S. & Kissinger, G. (2015). Subsidies to key commodities driving forest loss: implications for private climate finance. ODI Working paper, 51 pp.

In the past decade, the most significant trend in forest finance – particularly in international public finance – has been the growing connection between forests and climate. At the heart of this nexus is REDD+, which first appeared under the acronym RED in 2005 and has since dominated discussions both in forest and climate finance. The principle whereby developing countries qualify to receive funding for reducing their deforestation rates is deceptively simple, to the extent that in the early 2010s it harnessed unprecedented levels of political attention and associated funding.

Since then, both attention and funding have waned somewhat,¹¹ but REDD+ has left several crucial legacies. First, while the world has witnessed a dip in international public finance for forests since 2012, REDD+ could be the mechanism whereby the trend is reverted in the upcoming years thanks to the role that the Green Climate Fund, with its current endowment in excess of US\$ 10 billion, may play in channelling REDD+ payments to developing countries.

Secondly, by constituting a results-based payment mechanism, REDD+ has the potential to go beyond the forest sector (unlike most traditional forestry ODA) to address the root causes of deforestation, including in the agricultural sector. Perhaps most importantly, REDD+ has cemented the link between forests and climate, ensuring that a growing proportion of climate finance is allocated to forests. The identification of forests and land use as one of the four main areas of intervention of the Green Climate Fund is witness to the prominent role that forests now play in both mitigating and adapting to climate change.

The sustained connection between forest and climate finance has not been entirely beneficial, some highlighting the risk that climate finance will focus on the carbon storage function of forests to the detriment of their multiple social, economic and environmental functions. Yet it has also presented forest stakeholders with an unprecedented opportunity to benefit from the limelight by emphasizing their crucial contribution to solving one of the most pressing challenges humanity faces today.

3. Policy options and recommendations for corrective action

3.a. Improving the distribution of forest finance

With financing needs to implement SFM worldwide estimated anywhere between US\$ 70 and US\$ 160 billion,¹² the forest finance gap is huge. Large amounts of financing, both public and private, are available, but some either go untapped (in the case of international public finance)¹³ or they are allocated to unsustainable forms of forest management (both public and

¹¹ Verchot, L. (2015). CIFOR's REDD+ research. Presentation at the Paris Global Landscapes Forum, 5-6 December, Paris, France. Slides available at <http://www.landscapes.org/cifors-redd-research/> (retrieved 6 July 2016). Data from the Voluntary REDD+ Database (<http://www.fao.org/forestry/vrd/data/>) also suggest that REDD+ financing peaked in 2011.

¹² AGF (2012) op.cit.

¹³ According to data retrieved from the Climate Funds Update (<http://www.climatefundupdate.org/data>), as of 8 July 2016, 27% of the amount managed climate funds had not been spent.

private sources). A growing number of successful initiatives are aimed at bridging sources of finance with areas most in need:

- In order to steer (some of) the large existing amounts of private finance towards more sustainable forms of forest management, international organisations such as the World Bank's Programme on Forests (PROFOR) and Forest Investment Programme, along with FAO and the Centre for International Forestry Research all have initiatives aimed at harnessing private finance for SFM. Different levers have been used, including (i) fomenting dialogue and sharing of information between forest stakeholders and institutional investors and (ii) reducing the risk of investing in forests, including by guaranteeing returns and improving enabling environments through policy reform. In so doing, actors are increasingly exploring the complementary roles of public and private finance, notably the public sector's leveraging role in mobilising private sources.
- In a similar way, donors have increasingly turned to support "zero-deforestation" initiatives that focus on modifying legal frameworks and incentive systems to reduce the main causes of deforestation, notably in the agricultural sector. The GEF thus recently set up a US\$ 45 million programme on "taking deforestation out of commodity supply chains" – the first of its kind at tackling the issue at such a scale.
- In terms of accessing international public finance, the Global Forest Financing Facilitation Network (GFFFN), established in 2015 under the auspices of the United Nations Forum on Forests (UNFF), builds capacities of forest-related agencies in mobilising funding from multilateral sources for SFM by supporting them in developing project proposals. Some donors, such as the Global Environment Facility (GEF), have similar built-in capacity development mechanisms.

3.b. Addressing fragmentation in forest finance

The overwhelming fragmentation of the forest finance landscape has been identified by stakeholders inside and outside of the forest sector, to the extent that the Standing Committee on Finance (SCF) of the UNFCCC highlighted "increasing coherence and coordination on forest finance" as the main topic of their Third Forum in 2015. Thanks in part to the increasingly important role climate-related organisations in forest finance, the initiative of the UNFCCC SCF made a significant contribution in promoting dialogue between relevant international organisations on forest finance. It has notably helped bridge, at least conceptually, two largely disconnected but parallel international processes on forest finance, namely REDD+ in the UNFCCC and forest finance in the UNFF.

At national level, one of the main priorities of the UNFF's GFFFN is to assist developing countries in developing national forest financing strategies. These strategies aim to (i) map relevant sources of financing and (ii) design policies to harness them in a synergistic and complementary fashion, so as to provide the means of implementing sustainable forest management comprehensively and nationwide. Such strategies, if sufficiently ambitious in nature, have the potential to mobilise an important trend in the donor community, notably the growing appetite in investing unprecedented amounts of funding into large-scale and long-term

ground-breaking initiatives, as illustrated by the interest of the Green Climate Fund in supporting “paradigm shifts”, including in SFM.

Coherence and coordination on one hand, and redistribution on the other hand, are actually two sides of the same coin. Both require a holistic approach¹⁴ which views the forest finance landscape as a whole, with interactions and synergies between sources and recipients and between flows. While still sorely lacking, such an approach is increasingly being recognised as a solution to at least partly closing the global forest finance gap worldwide.

¹⁴ Singer 2016, op.cit.