

Recommendations for policy makers

to promote Impact Investments in forest and biodiversity conservation

Impact Investments in forest and biodiversity conservation are currently still a niche market. In comparison to conventional investment products, they present an opportunity to combine a financial return with a positive ecological and social impact. The small but growing market can enable biodiversity conservation and adaptive measures to climate change to be financed through private capital. However, the high risk and the difficulties involved in calculating rates of return pose

challenges for the providers of such investment products. These recommendations for action proposed by the OroVerde Tropical Forest Foundation and the Global Nature Fund illustrate how policy makers can address the challenges faced by Impact Investments in forest and biodiversity conservation. In our view, the three major issues in the successful design of Impact Investments are: handling the investment risk, generating returns, and achieving an ecological and social impact.

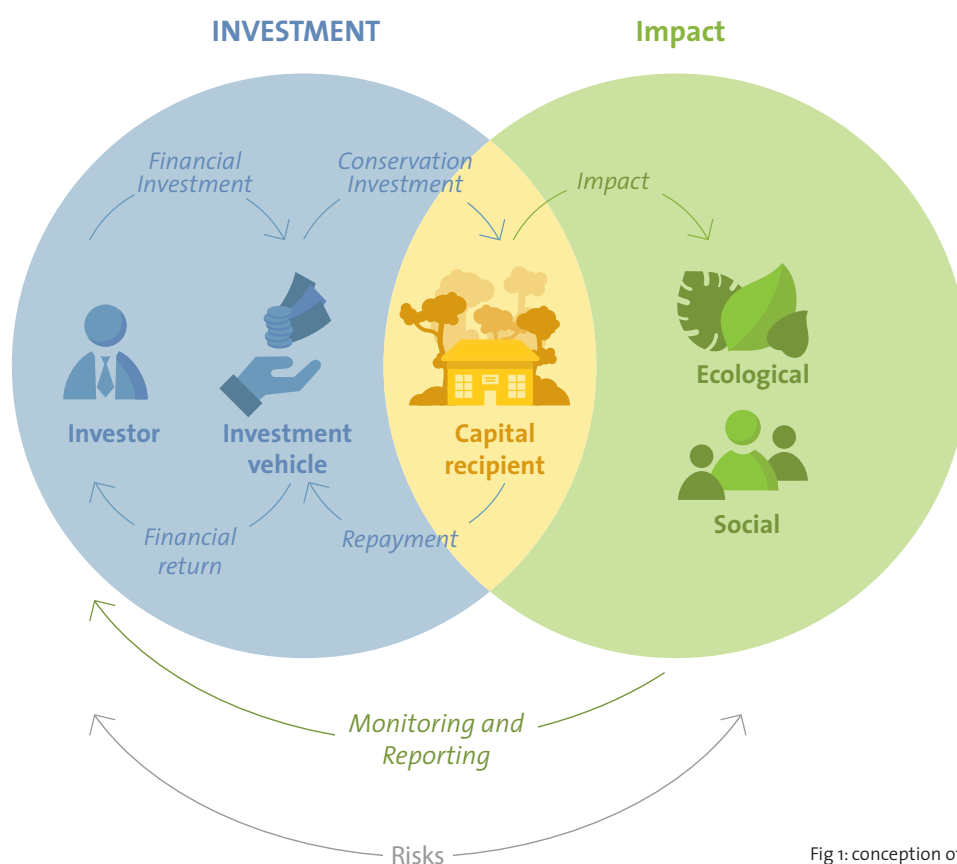


Fig 1: conception of Impact Investments

The recommendations are based on the results of five case studies and interviews conducted with experts as part of the “New innovative financing mechanisms for forest and biodiversity conservation” project by OroVerde and Global Nature Fund. The project was funded by the German Federal Agency for Nature Conservation with funding from the Federal Ministry for Environment, Nature Conservation, Building

and Nuclear Safety. The document reflects the views and opinions of the beneficiaries and does not necessarily coincide with the views of the funding agencies. A detailed description of the results can be found in the research study “Private capital for nature conservation – Could Impact Investments be a solution?”



RISK REDUCTION AND RETURN

Minimising the risk of Impact Investments in forest and biodiversity conservation

Currently, government funding is used in many investments as a risk buffer, supported by the argument of its leverage effect in making the investment more attractive to private investors. However, government funding often plays a subordinated priority. The consequence is that any losses from the investment are mainly borne by the tax payer. At the same time, there is no clear evidence that government funding has a leverage effect, nor is it clear to what extent and for how long government funding needs to be used to successfully mobilise private capital.

In order to keep the risk from the Impact Investment for the investor low, investments are primarily made in existing projects/companies, instead of developing new capacity. At present, there still tends to be a lack of projects that meet the requirements of Impact Investments, particularly in economic terms.

Investments in nature conservation can reduce ecological and thus also economic risks in the project area. For example, investments in various agroforestry systems increase the resilience of ecosystems to extreme weather events, including those related to climate change. Additionally, ecosystem services of a forest area, such as water storage, erosion protection, etc., are supported and made available to the community. To date, not enough attention has been paid to these positive ecological effects on the investment risk and they have, therefore, also not been taken into account, either in the conditions for the capital recipient or in calculating the rates of return.

Returns of Impact Investments in forest and biodiversity conservation

The capital recipient generates income from the sale of products (timber, coffee, cocoa, etc.), services (ecotourism), or partly also from the sale of CO₂ certificates. The financial return promised to the investor varies considerably between individual investments and ranges from an annual dividend of 2 per cent through to a return of 11 per cent. Achieving a positive ecological and social impact is not compatible with expectations of investors who wish to obtain a normal market return in the short-term. Other sources of income must therefore be developed.

Although sometimes government funds flow into Impact Investments, there is a lack of transparency in calculating the rates of return. Similar to risks, predicting returns is difficult to calculate and there is currently a lack of experience with ecological and social impact investments over a longer period of time.

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Recommendations for policy makers

- ➔ Government funding should focus on developing new projects suitable for Impact Investments that aim to have a high ecological and social impact.
- ➔ Impact Investments that have already received state funding need to be examined to establish how successful they have actually been in generating private capital. This will enable a better assessment of the appropriate duration and extent of state involvement in future.
- ➔ Research should be promoted into determining the ecological and social impact of Impact Investments on risk minimisation so this can be taken into account in risk assessment in future.

Recommendations for policy makers

- ➔ Demand more transparency in the calculation of the rates of return, particularly where there is state participation in Impact Investments.
- ➔ Promote payment programmes to ecosystem services (such as REDD+, Payments for Ecosystem Services), which could generate additional income for the capital recipient in the short-term.

ECOLOGICAL AND SOCIAL IMPACTS



According to a study by the Global Impact Investing Network (GIIN)², only half of the existing Impact Investments have a social impact focus. Only 5 percentage of investors were motivated solely by ecological reasons, mostly renewable energy sources. Forest and biodiversity conservation currently play a minor role. Reasons for this include a lack of information and interest to include the ecological benefits of investments. The higher risk and the lower rates of return associated with Impact Investments also play a role.

Positive ecological and social impacts are currently not, or only insufficiently, recorded and communicated. There is a lack of local monitoring that indicates both the baseline and any changes that have resulted from the investment.

In addition, a uniform definition or a framework outlining the requirements for Impact Investments, or for investments in forest and biodiversity conservation in particular, have generally not been available up to now.

The term “Impact Investment” has to date not furnished any insight into the nature and extent of the desired impact. Furthermore, measures such as the protection of natural forest areas or inclusion of the local population tend to have been taken on the initiative, or in the interest of, the capital recipient, and have not necessarily been established or encouraged by any influence on the part of the investment providers.

The costs involved in capacity building for capital recipients or in measuring the impacts are not included in the investments since these additional costs reduce the rates of return. Instead such activities have mostly been funded by donations or additional government funding.



Forest and biodiversity conservation currently play only a minor role in impact investments.

“The positive ecological and social impacts are currently not, or only insufficiently, recorded and communicated.”



Impact investments provide the means of obtaining a loan for capital recipients who otherwise would have no access to financial support.

² GIIN 2016: Annual Impact Investor Survey

ECOLOGICAL AND SOCIAL IMPACTS



Recommendations for policy makers

➔ Define the minimum ecological and social requirements for Impact Investments and in particular for governmental involvement in forest and biodiversity conservation, for example:

- Conservation of existing natural forest areas.
- The currency risk should not be transferred to the capital recipient, but should be covered by other mechanisms (e.g. insurance).
- Conditions for a loan should take ecological and social impacts into consideration, thereby increasing the incentive for sustainable development by the capital recipient.
- To ensure increased project sustainability, a minimum duration for the investments should be determined. This would also enhance the (planning) security for capital recipients and improve prospects for development.

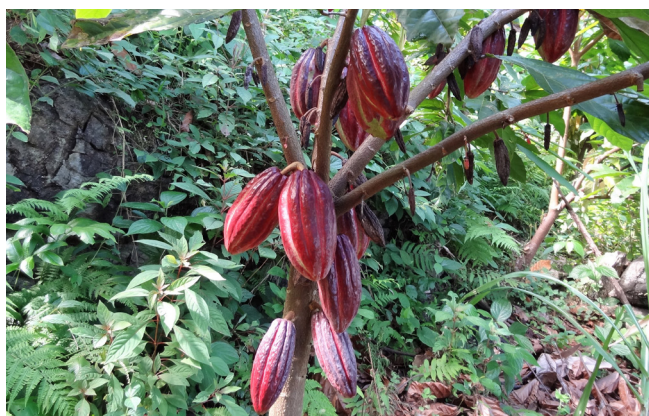
➔ Develop ecological and social indicators for measuring the effects of Impact Investments. Rather than having to develop new standards, these indicators could supplement current standards and therefore facilitate comparison and validation of the investments.

➔ Promote pilot projects for evaluating these standard indicators. Additionally, certifications (Fairtrade, FSC, Demeter, etc.) could provide a first basis for measuring impacts.

➔ Government funding should be made available for local capacity building and development of suitable projects for investment, as well as monitoring by local organizations.

➔ Make proposals on sustainability issues in investment decisions in the public discourse and raise awareness in the financial sector for responsible investment decisions.

➔ Strengthen the exchange of information and the creation of synergies, for example, in assessing projects and the impact of measures between the financial and the nature conservation sector, e.g. via a common platform.



Defining minimum ecological and social requirements can enhance the effects of Impact Investments.

Impressum

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