



Financing Responsible Forest Management & Trade (RFMT) in Natural Tropical Forests

Working Examples from Latin America



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WWF Goal



Create market conditions that improve management in 200 million ha. of the world's production forests by providing economic and social benefits to the businesses and people that depend on them



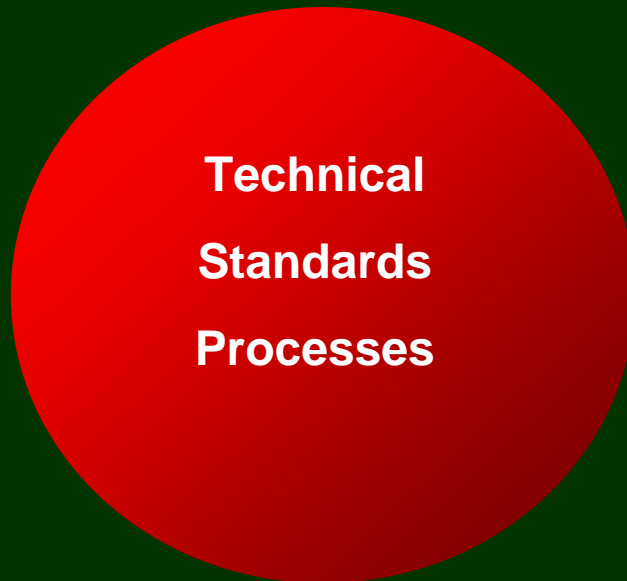


GFTN Approach:

Make responsible forestry a profitable business strategy

SUPPLY

DEMAND



LINKAGES



PRODUCTION

**Reduced Costs / Increased Efficiency + Increased Demand +
Quality Products +Linkages =
Sales...and Conservation**



Global Status of GFTN:

Growing with the wood products sector

- 263 Trade Members trading over \$146 million m3 in wood products
- 53 companies producing 19 million m3 round wood from 15 million has.
- 89 applicants producing 5.5 million m3 with another 2.6 million has.



Shanghai Anxin Flooring Co., Ltd

Growth in Tropical Wood Trade: *Would seem to be a good investment, no?*

Global

- LAC export growth increasing
24% annually to 16% of global
- \$ 6.6 Billion annual turnover in
tropical wood products
- 10% annual growth

GFTN

- 241 enquiries > \$200 million
- 93 market linkages = \$62
million
- 28 completely new and due to
action plans





**“Painted with the same brush”:
*Clients cannot get financing that recognizes
lower risk***

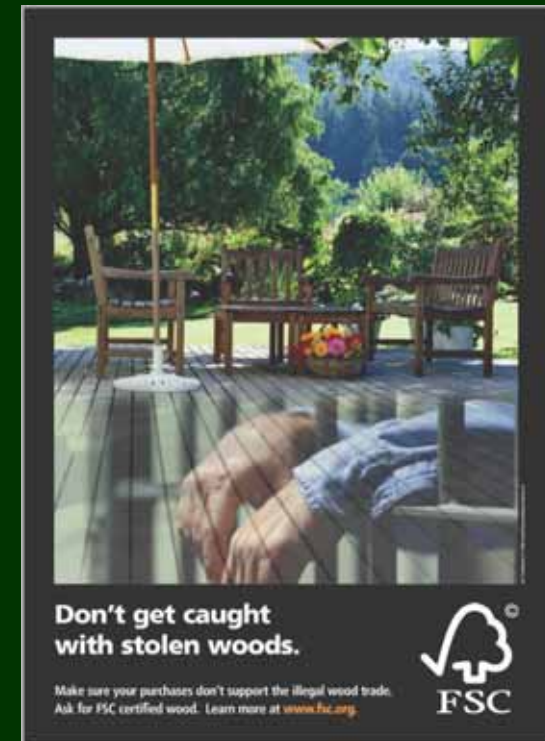
- **Traditional banks reluctant to lend due to:**
 - Risk to reputation
 - Unstable supplies of raw materials
 - Lack of collateral
 - Informality
 - Illegality





Role of GFTN in Finance: *Reduce Risk / Cost & Increase Returns*

- Ensure environmental & social integrity (credibility)
- Develop working solutions for financial institutions and GFTN members
- Develop investment portfolio of appropriate GFTN members (“deal flow”)
- Provide technical assistance



GFTN Financial Mechanisms: *Tailored approaches through a complex setting*

- Debt Model (Loans) for smaller companies and new, higher risk situations
 - Peru
 - 1-2 years
 - Donor funds
 - Nicaragua
 - 5 years
 - Donor / Private funds
 - Guatemala
 - 10 years
 - Private funds
- Equity Model for bigger companies and lower risk environments (Tropical TIMO)





Debt Model: *Peru (CEDEFOR Trust Fund)*



Objective

**Modernize forest sector and consolidate Year 2000
Peruvian Forestry Law by providing capital to
industrial concessionaires**





Debt Model: *CEDEFOR Trust Fund Structure (Peru)*

- USAID (Donor)**
- WWF**
 - Receive donation and pass funds to CEDISA**
 - Select participants**
 - Provide technical assistance
(credit/forestry/business)**
- CEDISA**
 - Receive contract and channel funds**
- Caja Rural San Martín (CRSM)**
 - Fiduciary responsibility for fund**
 - Issue loans & monitor program**
 - Return funds at end of trust fund life**

Debt Model: *Guatemala (Bancafe Private Loans)*

Bancafe

- 180 banks in Guatemala
- Fastest growing bank since 1978
- (US\$ 1.3 million in 8 communities in 2003)



Objectives

- Contribute to community development & improve quality of life for 1200 rural families
- Facilitate direct negotiation between bank and forest landowner to improve rates by eliminating intermediary



Debt Model: *Bancafe Approach (Guatemala)*

- Bank staff actively supervises portfolio
- Peer pressure from association of community concessionaires
- Maximum limit but flexibility for uses
- Forest as collateral
- 1 year period (usually) with market rates mainly for logging (post Annual Operating Plan)
- Next steps:
 - Other forest resources (Ecotourism)
 - Industrialization of processing in communities



Debt Model: *Nicaragua (FONFOR Trust Fund)*

Objective

- **Provide incentive to responsible forest managers and manufacturers in Nicaragua's Northern Atlantic Autonomous Region (RAAN)**
- **40% of Nicaragua's Forest**
- **Majority indigenous**
- **75% unemployment rate**



Debt Model: Nicaragua (FONFOR Trust Fund)

Potential in RAAN

- 350,000 ha (from 1,000,000)
- 28 million bf annually
- US\$ 21,000,000 (gross)
- Only for primary processing (not including employment in forest or mills, secondary processing or tax generation)



14,000 ha annual (25 year cc)
 140,000 m3 annual (10 m3/ha)
 (200 bf lumber / 1 m3 round wood)
 US\$ 0.75 / pt (low price)
 US\$ 4,200,000 (net) for producers (20% profit)

Debt Model: *FONFOR (Nicaragua)*

- Nicaraguan bank puts its own “hard” money on the table coupled with “softer” money from IDB and IFC
- WWF supervises technical performance on-the-ground
- Supervisory committee comprised of interested parties (Bank, IFC, WWF)
- Small program to start carefully (< \$300,000)





Debt Model: *FONFOR Trust Fund (Nicaragua)*

Category	Activity	Source of \$	Loan Term	Unique Requirements
<u>Execution</u>	<i>Harvest (working capital & roads)</i>	<i>50% hard (private) and 50% soft (donor)</i>	<i>12 months (\$10-100k)</i>	<i>Contract with buyer</i>
	<i>Processing (working capital and capital investment)</i>	<i>50% hard and 50% soft</i>	<i>3-5 years (\$35-100k)</i>	<i>Joint venture between community and processor</i>
<u>Technical Assistance</u>	<i>Planning</i>	<i>Soft</i>	<i>1-3 years (\$5-25k)</i>	<i>Legal right to access</i>
	<i>Training</i>	<i>Soft</i>	<i>1 year (\$1-10k)</i>	<i>NGO or private consultant</i>



Debt Models: *Lessons Learned*

- Share risk of failure and success
- Select participants impartially
- Establish clear, agreed upon procedures
- Obtain permits and contracts prior to granting loan
- Provide qualified technical assistance to loan recipients
- Design program to meet variable cash flow needs of sector
- Charge interest only on what is used (i.e. line of credit)
- Consider timber as collateral (particularly on non-private)
- Offer various periods depending on activity

Offer market rates (cheaper than "interest" rates)



Equity Model:

Tropical Investment Management Organizations (TIMO)

- **Trends in U.S. Timberland Investing**
 - Forest companies selling to investors (9% of total)
 - High Net Worth Individuals
 - Pension Funds
 - TIMOs provide direct management services
 - High prices in U.S. > Increase look at emerging markets
 - Trend toward large deals and larger accounts
 - Frequent combination of real estate and timber values



Equity Model:

TIMO model for the Tropics?

- **Why look at TIMOs for tropical hardwood forests?**
 - Traditional financial institutions reluctant
 - Leverage alternative sources (HNWI, Institutional investors, Donor organizations)
 - Feasible way for investors to enter unique asset class
 - Reasonable return expectations (i.e. IP sale @ 9-10%)
 - Provides portfolio diversification
 - Geographic
 - Sector
 - Product (Hardwood, NTFP, Recreation)
 - “Win – Win” with NGO involvement reduces social / environmental risk & costs



Equity Model:

Comparing Investment Opportunities in Natural Forest Management

- **North**
 - Low Risk
 - Moderate Returns
 - Sector diversification (within U.S.)
 - Commodity oriented
 - Growth of asset
 - Artificial price increase
 - Major real estate increase
 - Inflation Hedge
- **South**
 - High Risk
 - Mod-High immediate returns
 - Geographic diversification (outside of U.S.)
 - Specialty product oriented
 - Faster growth of biological asset
 - “Real” price increase
 - NTFP / Recreational potential

Take Home Message: *Let's not lose our heads over the issue*

- Despite some negative “macro” trends, companies and financial institutions and NGOs are developing working solutions that are providing real \$\$\$ to responsible forest managers and manufacturers

