The Forests Dialogue

Dialogue on Investing in Locally Controlled Forestry
24–25 May, 2010 | London, United Kingdom
Co-Chairs’ Summary Report

by James Mayers, Christopher Knight, Ruth Martínez and Gary Dunning

The Forests Dialogue (TFD) held a two-day multi-stakeholder dialogue on Investing in Locally Controlled Forestry (ILCF) in London on 24–25 May, 2010. This dialogue was the fifth in this Initiative, which began with a scoping dialogue in Brussels in 2009, followed by field dialogues in Panama, Nepal, and Macedonia, each of which explored the opportunities and challenges facing both local forestry users and enterprises and those interested in investing in them.

This dialogue represented an important chance for the ‘value propositions’ of locally controlled forestry to be explored by investors. It brought together forty stakeholders from key parts of the forest sector internationally, including family forest owners, representatives of Indigenous Peoples and community forestry groups, forestry investors and consultants, forestry companies, development assistance agencies and international non-governmental organizations (see participants list). The aim of the dialogue was to bridge some gaps of understanding—between forest rights holders on the one hand and those who might wish to invest in their locally controlled forestry enterprises on the other—and to identify some clear next steps for stakeholders at local, national and international levels.

The dialogue was facilitated by Markku Simula, fuelled by a background paper by Dominic Elson, and hosted by the London office of PricewaterhouseCoopers, with support from Growing Forest Partnerships (a collaboration of the International Union for Conservation of Nature (IUCN), the Food and Agriculture Organization of the United Nations (FAO), the International Institute for Environment and Development (IIED) and the World Bank).

BACKGROUND ON THE ILCF INITIATIVE

The ILCF dialogue initiative run by TFD emerged from a collaboration with the Growing Forest Partnerships initiative which is exploring the importance of locally controlled forestry (LCF) to both forest rights holders and the global economy. Rights holder groups have estimated that around one billion people around the world depend on goods and services from LCF for a significant portion of their livelihoods, with some $75–$100 billion worth of goods and services and a range of wider environmental, social, cultural, and spiritual values provided by forests under local con-
The premise of this dialogue initiative is that these benefits could be increased with more investment in the sector. Diverse actors from pension funds to investment pundits have observed that returns on forestry investments, while typically not stunning, in the long-run often outperform other investments, as returns from forestry depend mostly on the relatively stable factors of biological growth and climate and as such are less tightly correlated with conditions in the rest of the economy than other investments.

Several themes have emerged from previous dialogues on ILCF and from separate meetings of three ‘rights holder groups,’ the International Family Forestry Alliance, the Global Alliance of Community Forestry, and the International Alliance for Indigenous and Tribal Peoples of the Tropical Forests. These alliances own or have traditional use rights over a forest resource and as they face some common challenges, they have begun to find collective voice. In a joint statement in March 2010 the ‘G3,’ as they have begun to call themselves, put forward their emerging shared mission: (i) Promote the G3 and participation in policy making processes; (ii) Recognize and respect the forest and land rights of indigenous, tribal peoples, communities and family forest owners; (iii) Support organising and organisations of rights holders; (iv) Share knowledge and best practices; (v) Pursue access to markets and the right to economic utilisation of the forest resources; (vi) Promote sustainable forest management and locally controlled forestry and; (vii) Foster world-wide solidarity between indigenous, tribal peoples, communities and forest owner families.

For more information on previous dialogues, background papers, presentations, including the meaning and use of terms such as ‘investment’ and ‘locally controlled forestry’ for the purposes of this initiative, and the collective position statements from the G3 please visit TFD’s ILCF London Dialogue webpage.

**EXAMPLES OF INVESTMENTS—SOURCES OF INSPIRATION**

Dialogue participants noted that there is plenty of commercial LCF to be found in many countries—particularly independent growers and small-medium forestry enterprises—that have not been the focus of external investment of any sort. There are also many examples—in natural forest, planted forest and dealing with ecosystem services—that already have a relationship with external ‘value investors.’ Many others show promise. The examples discussed during the dialogue—cases of LCF as well as other types of illustrative cases—were as follows:

**Lake Taupo Forest Trust, Turangi, New Zealand:** This case involves an indigenous-owned and -operated forestry enterprise. In this enterprise, individual landholdings have been aggregated into a large estate with integrated management overall. The business is run as a leasehold partnership with the state for a defined period of time. The state invested in the enterprise to start with (from 1969) but its stake is gradually being eliminated, such that at the end of 2021 the land own-
Forest owners’ cooperatives, Nordic countries: Forest owners’ cooperatives, common in the Nordic countries, have a history of over one hundred years. In this system, landowners sell their raw material to the cooperative, which processes it into high-value products. Many cooperatives nowadays provides the owners with a full range of forest management services, including planting, cleaning, harvesting, and planning, as well as an internal system of finance to support landowners’ investment needs. In this model, initial investments in the cooperatives have often been private but with government guarantees of the loans (this varies between countries and is not used in all Nordic countries). In more recent history, the cooperatives themselves have invested in secondary forestry businesses such as pulp mills, with dividends from these investments paid back to the members of the cooperative. As in the New Zealand model, the products are aggregated to achieve economies of scale, but in contrast to that model here the land itself remains under individual family ownership. For more information visit the Nordic Forest Owners’ webpage, or for two examples: Swedish Södra or Finnish Metsäliitto.

The Cochabamba Project Ltdt, Bolivia: This is an LCF enterprise which functions as a provident society—a structure used often in the United Kingdom, e.g., for community-owned wind-farm companies. Members of the society, mostly residents of the UK, have equal voice in its management, owning shares which cannot be traded. In this model, the beneficiary community is separate from the investor community: profits from the enterprise are used for the benefit of the community, while investors may or may not receive a financial return. For more information visit Ethical Investments’ webpage.

GreenWood/Madera Verde, Honduras/United States: This enterprise was created jointly by a Honduran NGO, a U.S.-based NGO, and several communities in Honduras. In this model, the Honduras-based Madera Verde supports community-run businesses by building capacity in business management, forest management, and woodworking skills. Meanwhile, U.S.-based Greenwood serves as a broker for the wood products produced by community artisans, linking the enterprise to markets in Honduras and abroad. This model avoids the problem of unwanted inventory by financing production through orders for specific products. Profits from the enterprise are used by the community for various social and productive functions, including investment in new equipment. For more information visit GreenWood’s webpage.

Green Resources, East Africa: Plantation and reforestation initiatives in Tanzania, Uganda, Southern Sudan and Northern Mozambique totaling to 15,000 ha planted since 1995, some involving small growers, some FSC certified and all of them organized as carbon offset projects. Costs so far (about US$80 million) have been considerable for the size of the project. Green Resources’ experience has been that it is very challenging to find investment for locally controlled forests and recommends that the management goal of LCF should be growing biomass. East Africa has worked well for them because of good rainfall and large land mass in relation to population density. For more information visit Green Resources’ webpage.
**ForestFinance, Central America:** The German ForestFinance group has been reforesting former pasture land in Central America with native precious woods back to tropical mixed forests for more than fifteen years. Over 5,000 private and business customers have long-term investments in forests with ForestFinance and benefit from the sale of timber, high quality seeds and carbon credits. In addition, the company develops agro-forestry products, such as investments in both timber and cacao forests, which are characterized by faster cash flow due to the sale of agricultural products. ForestFinance has also started carbon sink forests and agro-forestry projects in Vietnam. For more information visit ForestFinance’s webpage (see also www.co2ol.de).

Additional instructive examples of locally controlled enterprises and appropriate support for them included:

- A shareholder model from Germany in which private landowners own stakes in a wood processing facility.
- The Satoyama initiative in Japan, in which an initial government subsidy supported forest ecosystem services enterprises, with commercial banks now joining in lending.
- Community concessions in Guatemala producing timber for the domestic market and for export.
- The Sawlog Production Grant Scheme in Uganda—a partnership between the Government of Uganda, the European Union and the Government of Norway has, since 2004, supported the initiation of over 13,000 ha of small areas of timber plantations run by commercial and community growers.
- The work of the organization Root Capital, which has provided small-scale agricultural finance using teams of local or low-cost field agents.

### Challenges and Opportunities for Investing in Locally Controlled Forestry

**Different investors, different aims**

A starting theme of this dialogue was the recognition that there are different types of investors interested in LCF. Participants broadly accepted the lines drawn in the Background Paper between ‘soft investors’ and ‘hard investors’ and among the various classes of ‘hard investors’ identified by the paper. Participants also accepted that while improving governance, social equity, and environmental quality (soft investment) are all important—indeed often representing vital ‘legitimate subsidy’ to pave the way for possible hard investment—it was appropriate for the focus of this dialogue to be mainly on improving flows of cash towards enterprises producing financial returns.
(hard investment). It was noted that future dialogue work focused on the synergy between soft and hard investments may be useful.

**Same words, different meanings**

Cultural and professional differences in language arose both as possible obstacles in LCF initiatives and as difficulties during the dialogue itself. Different meanings held by rights holder groups and investors of common words and unfamiliarity with the professional or cultural language of the ‘other side’ hinders understanding at times and challenges joint progress. For example, rights holders often perceive their autonomy as immutable and their rights as inalienable yet the partial ‘relinquishment’ of both is perceived as critical to investors if contract-based investments are to take place.

**Communities as investors**

While the focus of this dialogue was on investment from outside the community, it was recognized that forest rights holders are often investors in the forest resource as well. Communities invest resources in, for example, forest management, fire protection, and in defending their property rights against encroachment by others. In the context of investing in enterprises operating in the marketplace, it was recognized that community members in the past have acquired shares in forest-related businesses by contributing their labor where outside investors contribute financial capital.

**Opportunities for major progress on ILCF**

A strong sense pervaded the dialogue that the value proposition of LCF (the right combination of perceived, real and potential opportunity) can and should be improved. In particular, there was much discussion about whether and how local rights can be both secure and ‘legible’ as a basis for investment. Synergies between soft and hard investment were also a recurring theme—soft investment in the systems, frameworks, and community capacity that ensure meaningful local control and that achieve critical mass for hard investment, which in turn helps further improve systems and frameworks. More can be done to develop business support services and capacity building into the business plan of investors, and to invest in the collective strength of LCF, through partnerships, alliances, aggregation and portfolio approaches. REDD+ presents major new potential for holistic approaches, and it is possible that global financial crisis stimulates stronger focus on more reliable long-term assets like forests, and forest-based enterprises that focus on local markets for basic needs.

**Barriers and pitfalls for ILCF**

Significant obstacles typically face the start up of ILCF efforts. Among these are:

1. **Misperceptions amongst both investors and communities of the prospects for LCF;**
2. **Limited capacity amongst communities for running businesses and amongst investors for engaging with communities and assessing the risks associated with community enterprises;**
3. **Insecure land tenure providing a disincentive to both rights holders and investors for enterprise development;**
High transaction costs, particularly the cost to investors of performing due diligence on relatively small projects in places with uncertain legal regimes and political instability;

Long time scales of forestry investments, with risks compounding over time.

Furthermore, once an ILCF process is underway, various potential pitfalls also typically present themselves:

- Inadequate value proposition in the business plan;
- Inappropriate representation, insufficient consultation and unclear communication plans;
- Mismatches in expectations and practices between investors and rights holders;
- Inadequately assessed market and political risk;
- Difficulty in extracting profit once the investment is generating returns;
- Unpredictable shocks and extreme events;
- Unplanned opportunities that divert effort and increase opportunity costs.

A partnership approach—with defined roles for hard investors and rights holders

If the above barriers are to be overcome and the pitfalls avoided, the key theme of partnership—which has been emphasized through all of the dialogues—must be made real. Many relationships between investor and community in the past have been paternalistic and exploitative. Partnership in this context means clear and agreed sharing of risk, cost and benefit according to the terms of a business relationship established between partners in an enterprise. A true partnership would entail each ‘side’ aiming to ensure that the other gains what it seeks: Rights holders might ask investors (and themselves), ‘How can we ensure you earn a return on your investment?’ Investors might ask rights holders (and themselves), ‘How can we help you secure and maintain your property rights and ensure that the proposed development supports the community’s vision for its future?’ Each side has roles to play, and participants identified the following:

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**Investors can provide:**

- Capital, including for capacity building/training, as in many other businesses;
- Management expertise;
- Market access/information;
- Political strength;
- Willingness to take on some risk, for example through pilot projects.

**Rights holders can provide:**

- Legitimacy among the people, building the social license of the enterprise and the investors behind it;
Critical roles for soft investment

Participants observed that governments and a host of other actors have often addressed the issue of insufficient investment in forestry by financing the planting of trees without addressing other aspects of rights, capacity, governance and market development. Such efforts often founder as a result. It was proposed that the better approach is for ‘soft investors’ and governments to work on more systemic challenges and thus help in part to develop the conditions under which private capital can flow to forestry investments. Participants emphasized the importance of investment in research and development and in the policy and institutional capability to quash the illegal logging that often undermines local benefit from forestry, depresses the price of timber and thus creates the disincentive to invest in the first place. The importance of soft investment in areas that would improve information flows was also emphasized. Examples of useful soft investment approaches discussed range from Forest Connect, an international network steered by IIED and FAO of small forest enterprise-supporting organizations and online information exchange, to the Fondo Ganadero in Paraguay, an initiative that has facilitated contact between the forest and finance sectors and has resulted in mutual learning and partnership building there.

Good, solid data—a critical need

It was frequently recognized that given the crucial importance of accurate and specific figures in attracting investment, there is a pressing need for developing, better using and generating fundamental data on locally controlled forestry, including figures on such basic information as the land area in question, its geographical distribution and the number of people involved. Additional information is needed on the types, scale, and return profiles of potential ILCF projects. It would also be helpful for various agencies to understand the financing facilities ILCF might typically require, e.g. equity investments (and scale), debt, trade finance and working capital, and to develop tools to assist investors in assessing the particular risks associated with ILCF.

DEVELOPING GUIDANCE FOR INVESTING IN LOCALLY CONTROLLED FORESTRY

Typology of investment models

Participants recognized that a system for characterizing various models of ILCF would be useful. This would help focus attention of both investors and rights holders on some ‘standard’ workable types of investment, and would also encourage thinking about the range of possible options in a particular situation. A preliminary matrix was proposed in which the forest type (natural forest, planted forest, etc.) formed the main dividing line, with further characterization according to the type of asset in question (e.g., wood, non-timber forest products, ecosystem services, intellectual property, capital), the local rights platform (security of tenure, sub-national variations in legal regime, etc.), the invest-
Elements for such a matrix describing the range of different LCF investments were identified as a first step to be further developed later on.

**Principles or guidelines for ILCF**

There was broad agreement that while a strict set of rules governing ILCF would be excessively rigid and also unenforceable, a set of principles or guidelines for ILCF projects would be useful to both investors and rights holders. Such a set of guidelines, perhaps eventually developed as a code of conduct, would have two principle functions:

- Provide an operational basis for ILCF projects that would aid both investors and landowners in defending their rights throughout the process;
- Enable project developers to gain the support of investors and local leaders and their communities by allowing both to present to their constituencies the set of principles/guidelines to which the other side has agreed.

Participants recognized that an ILCF set of guidelines might draw from others already developed for various related purposes. These include those developed in the mining and water sectors, the Sustainable Forest Finance Toolkit developed by PricewaterhouseCoopers and the World Business Council for Sustainable Development, principles developed by the OECD, the FAO-CIFOR-IIED company-community forestry partnership guidelines, forest certification standards, and the Equator Principles. Another set of guidelines considered important were those arising out of current discussions on Free, Prior, and Informed Consent (FPIC).

As a starting point, key elements for inclusion in such a set of principles/guidelines were identified:

1. An agreed long-term ‘end game’ (common vision of the investment);
2. Identification of an organizational entity with whom a deal can be made based on appropriate local representation;
3. Clear property and tenure rights, with the central or local government having a key role in defining and conferring rights;
4. Definition of the roles of other development actors, e.g., ‘soft investors’;
5. Requirements for governance and transparency;
6. Investment in capacity building (including organization of rights holders, business planning, and management skills);
7. Identification of entry and exit strategies;
8. Appropriate and agreed arbitration and conflict resolution mechanisms;
9. Commercialization of the resource respecting multiple benefits and cultural aspects;
10. Benefit sharing;
11. Effective safeguards;
Investment process model—steps in developing a good deal

Participants identified as important that all parties to an ILCF project understand how the others prepare and execute a potential forestry project. To this end, participants developed a skeletal model of the steps in the development and execution of a business deal, noting who might be responsible for each step:

### Steps in Exploring a Deal

<table>
<thead>
<tr>
<th>Step</th>
<th>Whose role? (investors, community, others)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Idea origination/concept/ often from strategic needs assessment</td>
<td>Either; both, government</td>
</tr>
<tr>
<td>Pre-feasibility study</td>
<td>Either; both; broker/project developer</td>
</tr>
<tr>
<td>Community preparedness</td>
<td>Soft investors; other strategic partners</td>
</tr>
<tr>
<td>Deal development: exchange of information, development of business plan/case</td>
<td>Either; both</td>
</tr>
<tr>
<td>Letter of intent: arranging terms, i.e., who will get what, arranging who will do what, arranging timeline, lay out due diligence; binding</td>
<td>Perhaps investors on large project, community on small projects; both</td>
</tr>
<tr>
<td>Approval</td>
<td>Both</td>
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</tbody>
</table>

### Steps in Implementing a Deal

<table>
<thead>
<tr>
<th>Step</th>
<th>Whose role?</th>
</tr>
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<tbody>
<tr>
<td>Community management capacity building</td>
<td>Soft investors; other strategic partners</td>
</tr>
<tr>
<td>Establishment phase—project activities developed and further finance released on preconditions being met</td>
<td>Both</td>
</tr>
<tr>
<td>Sharing of revenues through project activities</td>
<td>Both</td>
</tr>
<tr>
<td>Monitoring and evaluation</td>
<td>Both</td>
</tr>
<tr>
<td>Exit, when applicable: dilute outside investors' holdings; determine when enterprise shuts down</td>
<td>Both</td>
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Innovative mechanisms for increasing and securing investment

Participants noted some existing and proposed innovative mechanisms in getting investment to LCF enterprises. These included:

- Supporting the creation of risk-reducing measures such as escrow accounts, access by small-holders and communities to insurance against disasters, political risk insurance, and procedures of dispute resolution;

- Creating financing mechanisms like that of Root Capital by which investors aim to work at the community scale rather than communities aiming to increase project size to the scale of typical investors—and connecting potential ILCF project developers with the Finance Alliance for Sustainable Trade (FAST) and similar initiatives;

- Making use of systems like those developed to direct the rounding differences on credit card and currency transactions towards social or environmental causes;
Making use of new legal and financial mechanisms such as Real Estate Investment Trusts and leasing;

Aggregation of small-scale producers and constructing portfolios through various approaches to achieve appropriate scale for investment;

Working with networks like the Model Forests network to exchange experience on well-managed ILCF projects and share information with potential project developers.

NEXT STEPS

Dialogue participants identified the following next steps:

Further develop the guidance tools. There is much to do to convert the initial frameworks described above into useful tools:

- Typology of investment models;
- ILCF principles or guidelines;
- Investment process model;
- Innovative mechanisms.

It was suggested that a working group steering and fed by some contracted work by key individuals would be a suitable approach to develop these tools.

Generate, and make better use of existing, effective data. Several actions were identified in developing and using information:

- Support and link up existing information and networking initiatives on ILCF, notably Forest Connect and Rights and Resources Initiative, to help develop the repository and use of ILCF experience (recognizing that interesting material in some investment agreements will be locked up in confidentiality agreements);
- Commission independent researchers to gather and analyze quantitative aspects of ILCF—the types, scale, and return profiles of current and potential ILCF projects—and on the financing facilities ILCF might typically require;
- Facilitate a group of forest community enterprise leaders to do an independent assessment of ILCF projects considered successful. Their analysis would provide a healthy complement to analyses made by research organizations and others;
- Explore whether a study like the World Bank’s annual Doing Business study could be conducted specifically for ILCF. Such a study could draw attention to actual investment opportunities and serve as a valuable source for other ILCF information;
Further develop initial analysis by GFP of specific international funds for supporting ILCF and consider modalities for mainstreaming ILCF in existing funds, better linking existing funds and/or setting up one or more specific ILCF funds.

Help stimulate pilot projects. It was suggested that REDD+, if developed in a phased approach with interim finance, may provide one strong basis and opportunity to develop and evaluate new pilot projects in ILCF. Opportunities in other processes should be identified.

Continue the dialogue initiative. It was agreed that more dialogues will be useful, perhaps with a thematic or location-specific focus, or both such that at the end of the process they produce both solid guidance and preparedness to take ILCF forward. Suggestions for dialogue focus included: role of government and soft investors in improving ILCF; testing and validating guidance materials; and bringing investors ‘down to earth’ to engage with specific LCF initiatives in particular contexts.

Growing Forest Partnerships continues to support the ILCF initiative and will work with TFD to convene a working group to develop firm plans to take the above steps and take forward the wider agenda of fostering more and better ILCF. TFD will focus on the dialogues that develop guidance and preparedness for ILCF. It is hoped that real progress can be made on the above agenda through 2010 and 2011.

ACKNOWLEDGEMENTS

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FOR FURTHER INFORMATION AND CONTACTS

Please respond to this dialogue summary or get in touch on related issues by contacting TFD staff at tfd@yale.edu, or TFD’s Program Manager directly, Teresa Sarroca, at teresa.sarroca@yale.edu. Also, follow us on Twitter—@forestsdialogue—so you can stay up-to-date on TFD’s next steps.

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