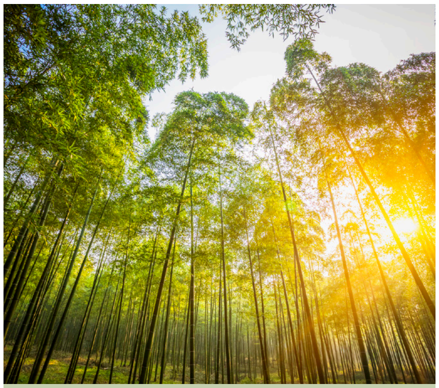
Evaluation and Learning

Towards Large-Scale Commercial Investment in African Forestry



QUICK FACTS

RELEVANT CIF PROGRAM:
FOREST INVESTMENT PROGRAM

EVALUATION FIRM:
ACACIA SUSTAINABLE BUSINESS ADVISORS

COUNTRIES COVERED:
AFRICA REGION; CASES FROM GHANA, MOZAMBIQUE, AND UGANDA

METHODS USED:
CASE STUDY, DESK REVIEW, STAKEHOLDER CONSULTATIONS, MARKET ASSESSMENT, FEASIBILITY ANALYSIS

AFRICAN DEVELOPMENT BANK GROUP
GROUPE DE LA BANQUE AFRICAINE DE DÉVELOPPEMENT

OBJECTIVE

This study reviews the conditions that enabled the successful structuring of the few recent private sector investments in African forestry. It aims to assess the current market potential for commercial forestry in Africa, to analyze alternative investment models for its development, and to advise on the feasibility of a dedicated fund promoting new and additional investments in the sector.

CONTEXT

Targeted investments in sustainable commercial forestry have the potential to catalyze economic, social, and climate-smart transformation across the African continent, contributing to broad areas, such as: (i) afforestation and reforestation of degraded lands; (ii) profit generation for private sector shareholders; (iii) natural resource value chain development; (iv) carbon sequestration and climate change mitigation; (v) job creation and improved livelihoods; (vi) and a range of other local and national development co-benefits.

Yet, there is a substantial gap between the available land and market potential for such investments, and the track record of successful investments. Financial barriers, such as historically low returns and high establishment costs, as well as persistent structural and technical barriers, continue to dissuade possible investors from entering the market and sustainably developing Africa's forests to their full potential. Since 2000, the commercial private sector has only established approximately 125,000 ha of new plantations, whereas smallholders have planted around 250,000 ha. In the meantime, government-owned forests have shrunk by approximately 100,000 ha over the same period.

AFRICAN FORESTRY INVESTMENTS: CASE STUDIES

Despite challenging market conditions, three recent blended finance investments demonstrate the viability of certain financial models in forestry development.

FIP GHANA CASE • The African Development Bank (AfDB) succeeded in structuring a *Public-Private Partnership for the Afforestation of Degraded Forest Reserves* project in Ghana. A blended loan (USD 10 million FIP; USD 14 million AfDB) for a sustainable commercial teak plantation provided a concessional debt package at sub-market terms and aligned incentives through a tripartite benefit-sharing agreement between the Government of Ghana, the project owner, and local communities. This pilot project is a good example of how a blended finance transaction deploying patient capital can play a catalytic role in unlocking investments in forestry assets. This approach can mitigate equity risk in a class of assets requiring time to mature and hence create value.

FIP MOZAMBIQUE CASE • In the International Finance Corporation's (IFC) *Emissions Reductions in the Forest Sector through Planted Forests with the Private Sector* project, a USD 1.85 million grant from FIP will support a plantation company to address local stakeholder engagement, community land delimitation, and farmer training, and to develop their concessions using a mosaic approach. This grant—and similar instruments—can play a crucial role at early stages in the project development cycle to help unlock long-term investments.

UGANDA SMALLHOLDER PRODUCTION GRANT SCHEME CASE • This program provided performance-based cash grants to pre-selected developers for sustainable plantations, and has facilitated extensive technical support, training programs, and seed supply, becoming one of the most successful smallholder forestry programs in Africa. Most of the 40,000 ha of forest established is believed to have been replanted after first harvest.

MARKET OVERVIEW

In Africa, new planting from private companies has ground to a halt in recent years, with few notable exceptions. This has occurred despite many companies' high-quality infrastructure and sustained access to additional land areas for afforestation. The current investment potential for planting on land already held/managed/leased by commercial-scale forestry stakeholders would be at least USD 1 billion and is concentrated in 12 African countries.

The most appealing market opportunity is in expansion (i.e. brownfield) afforestation projects that would benefit from lessons learned, silvicultural developments, existing seedling nurseries, physical infrastructure, and human resources. New investors would be able to capitalize on these lessons to establish new, better quality forest plantations at around half the cost of ten years ago. In addition, growing local demand for wood products indicates that these investors would have a high potential to sell much of the wood produced into local markets.

PROPOSED STRATEGY FOR A DEDICATED FUND

OVERVIEW OF PROPOSED STRATEGY

The strengths and weaknesses of ten potential investment vehicles were evaluated in this study as part of the strategy to formulate a platform for future investments in sustainable forestry in Africa. Among these, an equity fund, a holding company, and a blending framework emerged as the top three choices for the proposed fund, with the equity fund prioritized above others. The proposed fund would pursue a blended finance approach, engaging junior tranche concessional investors as a means to catalyze new investments from private investors into African forestry. Risk offsets provided by the junior tranche would drastically increase the appeal of the fund for investors that have otherwise made limited or no investments due to real and perceived risks and market barriers.

POTENTIAL SCALE AND IMPACT

The study identified approximately 500,000 ha of viable plantation land on close to 1 million ha of land in ten countries. The fund would target approximately 100,000 ha of new forestry plantation, which, once mature, would yield around 2 million tons CO_2-eq sequestration per year. This impact would occur alongside the direct and indirect jobs created for women, men, and youth; improved access to new infrastructure; possible adaptation benefits; as well as other livelihood co-benefits.

NEXT STEPS

The final strategy design has been validated by the African Development Bank and vetted by external stakeholders in the sector. Operationalization of the suggested fund will depend upon partner engagement and fundraising activities, the selection of an appropriate fund manager, and deal sourcing.