Forest Carbon Partnership Facility

Options for Addressing Financing Gap of ER Programs

Guarantee

Thirteenth Meeting of the Carbon Fund (CF13)
Brussels, Belgium
October 13-16, 2015
Outline of Presentation

• The Financing Gap in REDD+ Programs
  – Investment phase

• Options for addressing financing gap of REDD+ Programs (presented at CF12)
  – Advance payment
  – Loan/credit/grant

  — Guarantee (elaborated at this CF13 meeting)
    – Bond (elaborated at this CF13 meeting)
    – Bilateral funding
    – REDD Country’s own resources
    – Other
Financing Gap in ER Programs

- Results-based finance is available downstream and is only accessible for verified emission reductions during later part of an ER program.

- Lack of finance for investments ("missing middle") to achieve ER Program targets is a major risk to achieving the results of ER programs and consequently the objectives of the Carbon Fund.

- Available public finance (e.g., Forest Investment Program (FIP)) only meets partial investment needs of ER programs.

- Preliminary assessment of ER-PINs indicates that the majority of ER programs do not have adequate finance for implementation.

- Need to consider multiple options to address financing gap of ER Programs.

- At CF12 Participants Committee meeting, the FMT presented an overview of selected financing options for addressing the financing gap of ER Programs.

- Some options are elaborated at this CF13 meeting to share progress on the work program and to seek feedback to advance work on the identified options.
Guarantee
Options for Addressing Financing Gap: Guarantee

• In countries implementing ER Programs, public/private investors may be reluctant to invest in ER Programs and those that intend to do so may require risk mitigation measures to help share or manage risk.
• Guarantees can leverage additional finance by mitigating risks of public/private financiers thereby improve conditions for investment in ER programs.
• Different types of guarantees can help to mobilize finance by mitigating or sharing risks and leveraging additional public/private investment for ER programs.
• Guarantees can address barriers to investment, improve market access, provide certainty to off-taker agreements or performance contracts for sustainable production activities in ER programs.
• World Bank’s Operational Policy (OP) 10 (Investment Project Financing) provides a framework for design and implementation of the Guarantees for ER programs included in the FCPF Carbon Fund portfolio.
Overview of World Bank Guarantees

- **50 guarantee operations** approved for cumulative amount of $5.9 billion in 41 countries.
- $31.2 billion has been mobilized with $4 billion in guarantees - an industry leading **leverage of 7.8 times**.
- Guarantees contribute to design of innovative financing structures to leverage private capital.
- Most guarantees have been provided by IBRD/IDA and supported investment projects in **energy and infrastructure** sectors.
- Use of **trust fund guarantees** to address the financing needs of ER programs is an extension of World Bank guarantees to support the priorities of REDD+.

*All guarantee operations, 1990-2014*
Categories of World Bank Guarantees

Guarantees

Project-Based Guarantees

Loan Guarantees
Guarantees on loan related obligations for program/project investments

Payment Guarantees
Guarantees on non-loan related obligations for program/project investments

Policy-Based Guarantees
(Less relevant to financing of ER programs and therefore not considered as financing instrument for ER programs)

Guarantees support for implementation of policies
Carbon Fund Guarantee

Features of FCPF Carbon Fund Guarantee (CFG):

• Proposed on the concept of **project-based guarantee.**

• A **trust fund guarantee** that meets the requirements of World Bank’s Operational Policy (OP) 10 (Investment Project Financing).

• Enables raising **additional finance** from public/private sources for meeting investment needs of ER programs and promotes public-private partnerships in implementing ER programs.

• Provides **credit enhancement** to potential financiers thereby facilitating mobilization of additional finance from public/private sources.

• Promotes **risk sharing arrangements** in implementing ER programs
Types of Carbon Fund Guarantee

Carbon Fund Guarantee (CFG) proposed for ER programs can be of two types:

- **Loan Guarantee** covers debt service risk for public/private loans extended to entities implementing ER programs.

- **Contingent Finance Guarantee** is a payment guarantee that covers specific risks (e.g., technologies, practices) that are outside the control of implementing entities and potentially impact the costs of implementing ER programs.
# Features of Carbon Fund Guarantee

<table>
<thead>
<tr>
<th>Item</th>
<th>Loan Guarantee</th>
<th>Contingent Finance Guarantee</th>
</tr>
</thead>
<tbody>
<tr>
<td>Guarantor</td>
<td>FCPF Carbon Fund administered through the IBRD</td>
<td>FCPF Carbon Fund administered through the IBRD</td>
</tr>
<tr>
<td>Implementing agency</td>
<td>IBRD using its Guarantee processing guidelines</td>
<td>IBRD using its Guarantee processing guidelines</td>
</tr>
<tr>
<td>Guarantee beneficiary</td>
<td>Financial institution, e.g. commercial bank or investor fund or another entity extending finance to ER program with arrangements on recourse to guarantee funds from the Carbon Fund.</td>
<td>An entity with contractual obligations with ER Program and arrangements with Carbon Fund on recourse to guarantee funds from the Carbon Fund.</td>
</tr>
<tr>
<td>Maximum Carbon Fund Guarantee</td>
<td>As per the decision of CF Participants - ER program receives up to xx % (e.g., 10 %) of the Carbon Fund resources committed to an ER program</td>
<td>As per the decision of CF Participants - ER program receives up to xx % (e.g., 10 %) of the Carbon Fund resources committed to an ER program</td>
</tr>
<tr>
<td>Guarantee Period</td>
<td>ERPA period</td>
<td>ERPA period</td>
</tr>
<tr>
<td>Events triggering Guarantee</td>
<td>Specific events to be defined</td>
<td>Specific events to be defined</td>
</tr>
<tr>
<td>IBRD Fee for administering guarantee</td>
<td>As per the decision of CF Participants - 0.xx% fee on guaranteed amount or one time $xxxxx amount to cover administration costs of guarantee</td>
<td>As per the decision of CF Participants - One time charge of $xxxxx to cover administration costs of guarantee</td>
</tr>
<tr>
<td>Guarantee charge accruable to Carbon Fund</td>
<td>As per the decision of CF Participants - 0.xx% per annum of the committed and undisbursed balance of CFG Commitment from guarantee effectiveness date</td>
<td>As per the decision of CF Participants - 0.xx% per annum of the committed and undisbursed balance of CFG Commitment from guarantee effectiveness date</td>
</tr>
<tr>
<td>Counter-Guarantee</td>
<td>No requirement for sovereign government indemnity</td>
<td>No requirement for sovereign government indemnity</td>
</tr>
</tbody>
</table>
Loan Guarantee

- To cover public/private financiers against specific risks of debt service default (interest and principal) up to guarantee amount available to an ER program.

- To ensure an ER program is bankable for public/private financial institutions as loan guarantee can give financiers comfort that loan repayment risk is mitigated and thus help to mobilize additional funds for implementing an ER program.

- Provisions on the obligations of Carbon Fund and ER program in relation to guarantee to be clarified in ERPA.
Contingent Finance Guarantee

- To provide certainty to implementing ER program activities with additional finance backstop to address specific contingencies.
- To address risks associated with performance or barriers to implementing sustainable management activities of the ER program.
- To address barriers or perceived risks of investors in institutionalizing sustainable production and value chain interventions that sustain or enhance the results of ER programs.
- Provisions on the obligations of Carbon Fund and ER program in relation to guarantee to be clarified in the ERPA.
Carbon Fund Guarantee Framework

Carbon Fund Guarantee Facility – structure for risk sharing

• Enables mobilization of additional resources to meet guarantee requirements.
• To be created with contributions from Carbon Fund, grants, and funding from other participating public and private sector institutions.
• Criteria for participation in the Guarantee Facility to be established.
• Guarantee Facility to have two windows:
  • **Multi-country** – for public/private investors participating in ER programs of multiple countries
  • **Single country** – for public/private investors participating in ER program of a specific country
• ER Programs have option to receive guarantees from Guarantee Facility as part of the ERPA.
• Institutions participating in Guarantee Facility have option to negotiate contracts with ER programs for the ERs generated in excess of Carbon Fund ERPA.
• Provisions to be adopted on the use of funds from the Guarantee Facility in case no guarantees are triggered during the Carbon Fund period.
• Guarantee Facility is to be managed as part of the Carbon Fund Guarantee.

Guarantee provisions

• **First Loss** – Arrangements for sharing first loss to be defined
• **Second loss** – Arrangements for sharing second loss to be defined
**Example of Carbon Fund Guarantee: Loan Guarantee**

- **Carbon Fund**
  - Contributes $xx million to Guarantee Facility

- **Guarantee/Risk Sharing Facility**
  - (extends guarantee with funds from Carbon Fund and possibly other public/private sources)
  - Guarantee option linked to ERPA
  - E.g., up to $5m in loan guarantee (10% of ERPA value) to cover debt service risk of ER program under specified circumstances

- **Participating Public/Private Financial Institutions**
  - Repays loan per the agreed terms
  - Extends loans to eligible ER program activities

- **ER Program in Country A**

- **ER Program Activities**

- **Entity Implementing ER Program**

- **ER Program Area**

- **Monitoring, Verification and Reporting of ER Program**

---

**ERPA of $50 million for 10 million ERs**
Example of Carbon Fund Guarantee: Contingent Finance Guarantee

Carbon Fund

- Contributes $ xx million to Guarantee Facility

Guarantee/Risk Sharing Facility (extends guarantee with funds from Carbon Fund and possibly other public/private sources)

- Guarantee option linked to ERPA
- e.g. up to $5m in guarantee for EACH institution to cover specific non-loan related risks/contingencies
- ERPA of $50mm for 10mm ERs

Participating Public/Private Financial Institutions

- Extends funds to eligible ER programs activities

ER Program in Country A

- Monitoring, Verification and Reporting of ER Program

ER Program Activities

Entity Implementing ER Program

ER Program Area

Two Options for Contingent Finance Guarantee

- e.g. up to 5 m in guarantee (10% ERPA value) in direct guarantee to ER program to cover specific non-loan related risks/contingencies
Use of Carbon Fund Guarantee

- **Start Date**: 2017
- **ERPA Signature**: 2017
- **Interim Progress Report (IPR)**: 2018
- **ER Monitoring Report & Verification Report**: 2019
- **Possible event triggering CF Guarantee**: 2020
- **Payment for ERs Verified**: 2021
- **No event**: 2022
- **If event triggered, ER Payment Adjusted for CF Guarantee**: 2022

**Guarantee**

**ER Program Implementation**
Question

• Should the FMT prepare a proposal on the Carbon Fund Guarantee for consideration at CF14/CF15?

Next Steps

• In case of CFP consent for the proposal on Carbon Fund Guarantee, FMT will initiate following steps.
  • Preparation of concept note on the guarantee instrument, peer review and consultations with relevant World Bank units
  • Consultations with ER program countries and private sector investors on the potential use of guarantee instrument
  • Design of guarantee taking into account the CF charter and WB operational policies
  • Presentation of the proposal on CF guarantee at the CF14/CF15
THANK YOU!

www.forestcarbonpartnership.org