

Forest Investment Program

Program Approval Request

1. Country/Region:	Lao People's Democratic Republic	2. CIF Project ID#:	(Trustee will assign ID)
3. Source of Funding:	<input checked="" type="checkbox"/> FIP	<input type="checkbox"/> PPCR	<input type="checkbox"/> SREP
4. Project/Program Title:	Smallholder Forestry Program		
5. Type of CIF Investment:	<input type="checkbox"/> Public	<input checked="" type="checkbox"/> Private	<input type="checkbox"/> Mixed
6. Funding Request in million USD equivalent:	Grant: US\$ 3 million (advisory services only)	Non-Grant: n/a	
7. Implementing MDB(s):	IFC		
8. National Implementing Agency:	Private Sector		
9. MDB Focal Point and Project/Program Task Team Leader (TTL):	<i>Headquarters- Focal Point:</i> <i>FIP Focal Point:</i> <i>Joyita Mukherjee</i> <i>(jmukherjee1@ifc.org)</i>	<i>TTL:</i> <i>Aimilios Chatzinikolaou</i> <i>(AChatzinikolaou@ifc.org)</i> <i>Michael Brady</i> <i>(mbrady1@ifc.org)</i>	
10. Program Description (including objectives and expected outcomes):			

Program Description:

The FIP Lao Investment Plan was endorsed in November 2011. The Plan includes four thematic programs designed to put all forest land and resources under participatory and sustained protection, development, and management, in a serious although ambitious attempt at leaving no gaps for the various drivers of deforestation and forest degradation to operate.

One of the themes, Smallholder Forestry, includes investments in development and direct management by farmers and the private sector forestry companies of forests outside state forest areas. This includes industrial tree plantations and smallholder woodlots following a systematic program of allocating such areas to appropriate local forest management entities. The underlying idea is that grassroots forest managers will be vigilant in protecting forests in their areas from the various

agents of deforestation and degradation, and will rehabilitate degraded forests and grasslands (hereinafter referred to as degraded lands¹) using land management systems that will provide them with benefits while enhancing carbon stocks.

This proposal conforms to the Smallholder Forestry Program in Lao PDR's FIP Investment Plan. The overall proposed program aims to develop successful Out Grower Schemes (OGS) that are commercially viable and environmentally sustainable in partnership with private sector forestry companies as a means to contribute to net reduction of GHG emissions and improve the livelihoods and incomes of the participating farmers.

Following the Investment Plan endorsement, IFC undertook a scoping study and carried out further identification missions and discussions with key market players, government, forestry experts, other development agencies, FIP partners and communities to develop the proposed program interventions. The concept of the program will be initially tested in partnership with a lead private sector forestry company that has the potential to scale up and to set standards across the forestry sector. As a minimum criteria all companies selected for partnership will adhere to IFC's social and environmental safeguards, and meet the IFC Internal Due Diligence requirements.

The testing phase will start at a modest scale to strengthen buy-in by all stakeholders, build up farmer confidence and experience with a range of different tree and crop combinations to demonstrate the viability of the proposed OGS model. An evaluation is scheduled for last quarter of the test period in order to create the foundation for decision making to scale up the program based on transparent and clear recommendations from the pilot lessons learned. Once the approach has been successfully piloted and the lessons learned are incorporated into the program design, it will be scaled up and replicated with other companies operating in the country that also adhere to IFC's social and environmental safeguards. The program has the potential of reaching 15,000 farmers engaged in the sustainable management of an estimated 15,000 ha of land.

The program is comprised of two complementary components as follows:

1. Farmer Engagement Plan (FEP)
 - a. Out Grower Scheme (OGS) Model
 - b. Land Security
2. Farmer Organization and Capacity Building
 - c. Farmer Groups
 - d. Farmer Technical Capacity Building

The program's intended business model aims to be both sustainable and profitable through the establishment of long-term forestation of degraded lands with tree crops to sequester carbon and reduction of GHG emissions, while contributing to adaptation to climate change and farmer's income through diversifying use of trees and annual crops, which will also promote the gradual improvement of impoverished soils. The combination of annual cash and subsistence crops and perennial tree

¹ The Forestry Law (December 24, 2007), defines degraded forest as "... the forest areas that have been heavily damaged such as land without forest or barren forestland, which are allocated for tree replanting, agriculture- trees products, permanent animal husbandry areas or using land for other purposes in accordance with the socio-economic development plan".

crops provides for shorter term revenue streams, while managing for longer term forestry expansion and profit through industrial timber or other commercial products. Where possible a mix of fast growing and local species will be used. The current practice in Lao PDR for establishing government licensed tree plantations is to locate concessions in areas of degraded land where merchantable timber has been previously harvested. Although designated as degraded, these areas typically contain residual biomass (mainly grasses and woody shrubs). Current practice is to windrow this material and often burn it, resulting in GHG emissions. The business model proposed in this program aims to utilize this biomass in a number of ways that help to generate additional income for the farmers and reduce emissions from the land to be used. The program will also contribute to the sustainable management and protection of remaining natural forest along riparian corridors and other areas of intact natural forest. Such areas can be managed by the farmer groups as community forest.

The context for the sector, the market barriers, and the proposed activities are described below.

Context:

Lao PDR is one of the least developed countries in Southeast Asia. Forests cover 40% of the country, the highest percentage in the region. Forestry and agriculture sectors represent 30% of GDP and contribute to 75% of employment. Around 80% of the population live in rural areas where poverty incidence is 32% compared to 17% in urban areas. Forestry resources including non-timber forest products contribute between 30-70% of rural income.

The country's forest cover declined from 70% in 1940 to 40% in 2010, due to a combination of over-logging, shifting cultivation, grazing, defoliation, bombing and repeated fires. In addition to what is classified as "forest", which means that the tree crowns cover more than 20% of the ground, there is a similar area of former forest that is now classed as "unstocked forest" that still has some vegetative cover. Much of this land is used for extensive cattle grazing, which provides important supplementary income to households. Some of this unstocked forest land has soils that are impoverished and a substantial proportion has soils that are either infertile or compacted and generally subject to seasonal flooding. Some of this degraded land could potentially be improved by better management and provides areas that could be utilized for development of industrial tree plantations (ITPs), expansion of agricultural production and improved livestock management, as rural communities continuously seek to improve livelihoods.

The Government of Lao PDR's (GoL) Forestry Strategy 2020 calls for increasing the forest cover to 16.576 million ha or 70% of the total land area by 2020. In order to reach this target, actions will have to be implemented in state forestry areas as well as in non-state forestry areas. Specifically, this requires that the national target for ITPs of 500,000 ha be met by 2020. Additionally, another 515,000 ha of tree plantations and naturally regenerated forests need to be established through reforestation efforts outside the state forestry areas by local community village forests including individual households in small landholdings. Furthermore, degraded lands (35% of the country's total land) could be used to achieve this latter target. Most recently, the GoL has stated that the success of industrial plantations will be defined partly on how well OGS are incorporated.

Market Barriers:

As stated above, degraded land accounts for approximately 35% of total land cover in Lao PDR. These areas could be utilized for expansion of agricultural production and development of industrial forest plantations which can create alternative livelihood for rural communities and help mitigate climate change by sequestering additional atmospheric carbon and reduce pressure on remaining natural forests. Moreover, the productive utilization of degraded land could represent an opportunity for farmers to benefit from the rapid economic growth in Lao PDR and neighboring countries in recent years, which has increased the demand for a wide range of commodities (e.g., wood, estate crops, cash crops, fodder, etc.). However, Lao farmers derive very little benefit from these opportunities because they are not organized to capture the benefits of scale to access markets efficiently, lack the technology to diversify their farming systems and the financial resources to invest in inputs required such as seed, fertilizer and fencing materials. There have also been major problems with access to land and security of land tenure for both farmers and private sector companies that have greatly restrained progress due to for example the lack of secured land as collateral needed to obtain financing from local banks.

The transformation of degraded land into productive use has proven to be a challenge for the GoL, as well as the private sector. The main market barriers that need to be addressed to promote Smallholder Forestry are as follows:

Limited success in company community partnerships in the forestry sector: Private enterprises managing concessions for tree plantations in Lao often have encountered limited success themselves in the past due to a failure to fully appreciate the importance of soil quality and the difficulties of securing sufficient land. A major contributory factor in the past to the lack of success with OGS has been the failure by the companies or the government to provide sufficiently intensive extension services. Companies have tended to provide seedlings and then leave the farmers to look after the plantations, but the farmers have not been adequately advised and supervised on maintenance, which is crucial for the survival and growth of the trees. Thus many of the smallholder plantations have failed or seriously underperformed.

Limited GoL capacity in land transfer to rural communities: There has been considerable development of the regulatory framework in the Lao forest sector since mid 1990s. However, the regulatory framework is hindered by capacity issues to implement and enforce laws. As a result, land security is a concern among farmers because land use plans are outdated or not conducted at all. In addition, there has been hardly any legal land ownership proof and existing contracts contained no clear stipulation of rights, benefits and obligations. Farmers' poor understanding of land ownership obligations and benefits including the absence of a proper farmer organization body exacerbates this issue.

Limited community organizational capacity, poor technical and business skills of farmers to produce agricultural and forestry commodities: Communities lack the organizational capacity and technical skills to produce agricultural and forestry commodities at a scale and in a cost effective and sustainable manner to capture local as well as international markets. As a consequence, these communities face substantial constraints to sustaining economic activities and consequently improving their livelihoods.

Summary of the Program:

Advisory Services (USD 3 million)

The program aims to assist private sector partners build successful OGS partnerships with communities. IFC has identified as an initial partner a lead forestry company that manages two plantation concessions in Lao PDR, which has had experience in developing OGS schemes in Lao and other tropical countries. The company is fully integrated with upstream forestry operations as well as downstream processing and product manufacturing. This integration experience provides important expertise to the OGS program in both plantation operations, as well as wood product marketing and value added.

The program will start with a pilot phase with this company to create a test and demonstration. This will help in promoting appropriate technology to farmers based on combinations of tree and annual crops and encourage the formation of farmer groups. In the expectation that farmers respond positively and that land security issues can be addressed efficiently, work will then start to scale up the program to reach as many as 10,000 farmers with the first partner company. These farmers will be supported to sustainably manage an estimated 10,000 ha of land in areas within an economically viable radius from the first company partner concessions. The scale of operations in each province will be geared to a combination of the scale of operations required to meet market requirements and the likely available human resources. An evaluation is scheduled for last quarter of the test period in order to create the foundation for decision making to scale up the program based on transparent and clear recommendations from the pilot lessons learned. Once the approach has been successfully piloted and the lessons learned are incorporated into the program design, it will be scaled up and replicated with other companies operating in the country that also adhere to IFC's social and environmental safeguards. Replication of the program with a second company partner has the potential of engaging additional 5,000 farmers in 5,000 ha.

The program will be based on the two following components:

1) Farmer Engagement Plan (FEP)

a) Out Grower Scheme Model: The program will facilitate private enterprises in developing commercially viable and environmentally sustainable OGS in Lao PDR. The program will work with the identified private partner to develop OGS that are aligned to the current company strategy of diversification of wood products and agro commodities. On a cost sharing basis, IFC will assist the partner develop the business case of the model, its structure and will commence the development of the FEP. IFC and the partner will communicate the model concept in the participating areas, engaging communities and all other relevant stakeholders. The program will ensure the development of detailed and informative contractual arrangements with interested farmers and raise farmer awareness in this area while promoting fair representation of all stakeholders, including women and vulnerable groups.

b) Land Security: In order to enhance the success of the proposed scheme and a long term partnership between the company and communities, IFC will work towards establishing land security for the participating farmers. IFC will seek the services of a qualified organization that will

work with Ministry of Natural Resources and Environment (MoNRE), its local agencies and a relevant organization to support the implementation of the Government's Participatory Land Use Planning Process (PLUP) and subsequent land registration and titling in the pilot area. Support in this area will provide land survey and registration technology, data recording and dissemination, capacity building to relevant GoL agencies, land rights awareness and development of grievance mechanisms. GIZ is leading the implementation of the Government's Participatory Land Use Planning process and titling policy in rural areas and is a potential partner in this program component.

2) Farmer organization and capacity building

a) Farmer Groups: IFC will partner with a NGO/partner to identify best practices and how to organize community participation into Producer Organizations (POs) including defining how Community Resource Persons (CRPs) will be developed. A PO governance and operational system will be developed and relevant training will be provided. Furthermore, IFC and the NGO/partner will develop business plans to help the POs become financially sustainable in the medium term. The Deutscher Genossenschafts- und Raiffeisenverband e. V. (DGRV – German Cooperative and Raiffeisen Confederation) has significant experience on group/cooperative establishment, both globally and in Lao PDR, and has expressed written interest in program collaboration.

b) Farmer Technical Capacity Building: IFC specialists will work with the company partner to convert their technical plantation package of the multi-commodities, including site preparation, planting, titling, fertilization and intercropping into easy to use media tools, customized to the participating farmers. IFC specialists will train a number of the partner's extension teams on the effective use of these tools in order to on-train farmers and build farmer technical capacity.

The expected outcomes of the program are: emission reductions, enhancement of carbon sinks, and improvement of rural community livelihoods. At completion, the program will result in:

- Reduction of approximately 755,400 tCO₂ of GHG emissions relative to reference levels (initially using IPCC default values for the region).
- 15,000 farmers trained in farming and business practices.
- 15,000 hectares of sustainably managed land (as per 7 criteria of SFM defined by the United Nations Forum on Forests).

11. Consistency with Investment Criteria:

The program description above has outlined the overall consistency of the program with the FIP investment criteria. Additionally, there are specifically consistency issues that need to be addressed:

a) Climate change mitigation potential.

Net 755,400 tCO₂ reduction in emissions from reforestation activities over the five years of the program and 548,400 tCO₂ per year in the final year and thereafter through the continued growth of the tree plantations². This represents a minimum estimates and does not include emission from avoided deforestation and forest degradation from natural forest adjacent to areas adjacent to targeted plantations.³

b) Demonstration potential at scale.

The Government of Lao PDR has set the target of 500,000 ha of industrial plantations to be established by 2020 in state forest, and an additional 515,000 ha of tree plantations and naturally regenerated forests need to be established through reforestation efforts outside the state forestry areas by local communities. Additionally, the Government has set the target to issue 1 million land titles by 2015. Moreover, the Government has stated that the success of industrial plantations the will be defined partly on how well OGSs are incorporated. The proposed program aims to demonstrate a successful profitable and sustainable OGS model that could be scaled up with in the country.

c) Cost-effectiveness.

Based on the GHG reductions calculations and the program of US\$3 million, the implied direct GHG reductions per FIP financing will be up to 0.25 tCO₂/\$.

d) Implementation potential.

Program activities will be implemented by IFC. The development of the program interventions will build on the initial work where IFC undertook a scoping study and carried out further identification missions and discussions with key market players, government, forestry experts, other development agencies, FIP partners and communities. IFC will continue to work closely with key partners and relevant departments within government ministries, such as the Ministry of Agriculture and Forest. IFC will also work closely with private sector partners, local government agencies and community organizations to implement the program. At this point, IFC has identified a potential partner forestry company and other national and international partners (NGOs, community organizations, and other private sector entities) that have expressed the interest in the implementation of this program according to their specific expertise and the program needs. Bilateral and non-government organizations that are leading relevant work on this sector (such as GIZ on land security) have expressed support and interest to collaborate in the program.

² Program related GHG emissions are estimated using the Carbon Assessment Tool – Afforestation/Reforestation (CAT-AR), a tool endorsed for use by the World Bank Group. Input data used to track emissions in CAT-AR will be obtained by the Program partners and include, among others, area of land planted and sustainably managed, and proxies (height and diameter) for biomass increment of areas planted.

³ There are potentially further GHG emissions reductions associated with the program. These include avoided deforestation and forest degradation in natural forest areas adjacent to targeted plantations. Assessment of these emissions will require baseline and ongoing forest analysis separate from the main plantation activities. The feasibility of such analysis will be assessed in the first year of the program.

e) Integrating sustainable development (co-benefits).

The overall goal of the program is to demonstrate a sustainable and profitable agro-forestry business model through community based reforestation of degraded and underutilized land that will contribute significantly to reduction of GHG emissions as well as to improve the livelihoods for participating communities that are among the poorest in the country. Improvement in smallholder forestry OGS offer significant development potential especially in remote post-conflict areas of Lao PDR. Therefore, improvement of rural livelihood is one expected outcome of the program.

Moreover, the program will contribute to conservation of biodiversity and sustaining ecosystem services. This includes any intact natural forest within the plantations managed by companies and OGS managed by farmers. Biodiversity management will conform to SFM criteria and company efforts to achieve international SFM certification. IFC will not support OGS activity in areas of intact forests.

It is anticipated that the OGS program will have an indirect effect on reducing the degradation of nearby intact forests that would otherwise be used for wood supply and eventually cleared for agriculture. The feasibility of measuring, monitoring and reporting of the REDD related activities in nearby forests will be evaluated in the first year of the program.

f) Safeguards.

The program will be implemented on lands that have already been deforested and settled, and are unlikely to be reforested by natural means. Additionally, the program aims to prevent further conversion of forests to agriculture. IFC's policies on social and environmental sustainability will be applied. Furthermore, IFC will not work with any company involved in conversion of natural habitat, including forest. IFC guidelines also restrict engagement in forestry operations to companies that are implementing sustainable management practices to one or more globally, regionally or nationally recognized standards as demonstrated by independent verification or certification.

Moreover, all participating clients will need to go through IFC due diligence process and are subject to IFC Performance Standards. Besides financial, legal and credit due diligence, integrity due diligence is an essential component of IFC's overall due diligence efforts for any engagement with outside parties. The Integrity Due Diligence (IDD) Procedure is a framework for identifying and documenting the potential risks associated with unethical and illegal activities which include environmental, social, governance and financial crime issues such as child labor, corruption, fraud, and money laundering. The Performance Standards, which have recently been updated, include: Assessment and Management of Social and Environmental Risks and Impacts; Labor and Working Conditions; Resource Efficiency and Pollution Prevention; Community Health, Safety and Security; Land Acquisition and Involuntary Resettlement; Biodiversity Conservation and Sustainable Management of Living Natural Resources; Indigenous Peoples; and Cultural Heritage. For information on IFC Performance Standards see: www.ifc.org/sustainabilityframework

12. Stakeholder engagement:

This program builds on the stakeholder engagement process that was conducted during the development of the FIP Investment Plan for Lao PDR. In addition, during the pre-design phase of the program, IFC has carried out identification missions and discussions with key market players, government, forestry experts, other development agencies, FIP partners and communities to develop the program interventions. IFC has also engaged with several farmers and prospective partners companies in areas of possible intervention in order to assess needs, interests, farmers' socio-economic benefits and concerns over program implementation and participation.

IFC Performance Standards will be applied and therefore stakeholder engagement will continue as the basis for building strong, constructive, and responsive relationships that are essential for the successful management of the program. For information on IFC's Performance Standards see: www.ifc.org/sustainabilityframework.

Initial surveys in the program location in Southern Lao show that there are no recognized indigenous communities in the OGS. This finding will be confirmed at the start of the program and if needed the IFC Performance Standard 7 on Indigenous Peoples will guide actions.

13. Gender considerations⁴:

Role of Women:

IFC Performance Standards will be applied and therefore a greater assessment of the women's role in agro-forestry sector will be carried out in the geographical area covered by the program. The approach towards women's participation will be tailored according to the culture of the ethnic group mix participating in the program. The program anticipates engaging with women in two major ways:

- a) Consultation workshop/dialogue spaces which will ensure that women are included in the discussions and are part of the process of awareness raising and engagement in the out grower schemes, and
- b) Through development of specific trainings on rights and obligations linked to their participation in OGS in order to ensure that benefit sharing is not gender biased.

14. Indicators and Targets (consistent with results framework):

Core Indicator	Target
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⁴ Ibid.

a) CO2 sequestered through afforestation and reforestation activities.	- Net 755,400 tCO ₂ reduction in emissions from reforestation activities over the five years of the program and 548,400 tCO ₂ per year in the final year and thereafter through the continued growth of the tree plantations (see note 20 below) ^{5,6}
b) Sustainable management of forests and forest landscapes to address drivers of deforestation and forest degradation	- 15,000 Ha of sustainably managed land (as per 7 criteria of SFM defined by the United Nations Forum on Forests), consisting of plantations and agricultural crops.
c) Increased direct management of forest resources by local communities	- 15,000 people trained in sustainable forest and agriculture business practices and participatory community engagement

15. Co-Financing:

	<i>Amount (in USD million):</i>	<i>Type of contribution:</i>
• IFC	245,542	In-kind & Parallel Contributions
• Private Sector	3,400,000	In-kind & Parallel Contributions
• Other development Organizations	650,000	In-kind & Parallel Contributions
Co-Financing Total:	4,295,542	

16. Expected Board/MDB Management⁷ approval date:

- Expected MDB Management approval date: First semester of 2013
- Expected Mid-Term review date: At the end of the demonstration pilot phase (year 2)
- Expected Project/Program closure⁸ date: December 31, 2018

⁵ Program related GHG emissions are estimated using the Carbon Assessment Tool – Afforestation/Reforestation (CAT-AR), a tool endorsed for use by the World Bank Group. Input data used to track emissions in CAT-AR will be obtained by the Program partners and include, among others, area of land planted and sustainably managed, and proxies (height and diameter) for biomass increment of areas planted.

⁶ There are potentially further GHG emissions reductions associated with the program. These include avoided deforestation and forest degradation in natural forest areas adjacent to targeted plantations. Assessment of these emissions will require baseline and ongoing forest analysis separate from the main plantation activities. The feasibility of such analysis will be assessed in the first year of the program.

⁷ In some cases activities will not require MDB Board approval.

⁸ Financial closure date

17. Other

I. Role of other Partners involved in project/program⁹:

The Forest Investment Program in Lao is implemented through a partnership of the government of Lao PDR with IFC, World Bank (WB), and Asian Development Bank (ADB). IFC's Smallholder Forest Program complements the efforts of the WB and ADB FIP Programs in forest production and conservation by scaling up participatory sustainable forest management and forest protection for ecosystem services, respectively.

In addition, IFC will seek to involve other national and international partners (NGOs, community organizations, and other private sector entities) in the implementation of this Program according to their specific expertise and the Program needs. Some key partners in this field in Lao, such as German Agency for International Cooperation (GIZ) and the German Cooperative Association (DGRV) have expressed interest in collaborating with IFC.

II. Implementation Arrangements (incl. procurement of goods and services):

Program activities will be implemented by IFC. IFC will work closely with relevant departments within government ministries, such as the Ministry of Agriculture and Forests. IFC will also work closely with private sector partners, local government agencies and community organizations to implement the program. FIP resources will be used to facilitate and enhance the partnership between private sector forestry companies and farmers in order to demonstrate a successful commercially viable and environmentally sustainable OGS model. Resources will be used to contract consultants and staff to build capacity and awareness of farmers and will also benefit the Government on its capacity to provide land titling services to the communities. As per IFC procedures, partnership arrangements will be based on cost sharing with companies making cash contributions for program costs. IFC does not provide grants to private sector companies. In some cases purchases may be made on behalf of the company when it is necessary to facilitate demonstration results faster and demonstrate good faith.

In terms of procurement of goods and services, World Bank Group procurement guidelines will be followed. For more information, please see:

http://siteresources.worldbank.org/INTPROCUREMENT/Resources/278019-1308067833011/Procurement_GLs_English_Final_Jan2011.pdf

18. Trustee's confirmation of cash availability for this program

⁹ Other local, national and international partners to be involved in implementation of the project/program.