Global Environment Facility

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Agenda Item 13

GEF STRATEGY TO ENHANCE ENGAGEMENT WITH THE PRIVATE SECTOR

Recommended Council Decision

The Council, having reviewed document GEF/C.27/13, *GEF Strategy to Enhance Engagement with the Private Sector,* underscores the importance of strengthening the engagement of the private sector in the work of the GEF and approves the directions described in the strategy. The Council requests the Secretariat to bring back to the Council for decision at its meeting in June 2006 concrete proposals to implement the strategy.

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EXECUTIVE SUMMARY

1. The GEF has engaged in private sector partnerships in the past but largely on an *ad hoc* basis. GEF must be attentive to the greater opportunities for productive collaboration with the private sector to achieve greater environmental benefits in part by positively shaping private sector activities. The private sector has not always been an environmentally responsible citizen, though this is changing as the private sector increasingly identifies its interests as having a reputation for environmentally sound practices. This proposed strategy builds upon past experience and the changing dynamics of the private sector.

Learning from Experience

2. The sustaining core of the proposed strategy and of GEF operations is project activities conducted within the focal areas. This report draws on the experience with private sector partnerships in three focal areas, highlights barriers to implementation and indicates ways to overcome them. Some of these barriers and potential solutions are common across the focal areas, while others apply to a particular focal area. The three identified focal areas are the initial focus of this strategy due to the maturity, size and experience with the private sector in their portfolios. It is intended that future work will seek to extend this strategy, as appropriate, to the other focal areas (land degradation and persistent organic pollutants (POPs)). For example, the current priority in the POPs focal area is assisting countries with the development of National Implementation Plans (NIPs). Once completed, their implementation is expected to require greater engagement with the private sector.

3. Building on the foundation of GEF focal area experience, this strategy identifies three cross-cutting initiatives that could enable the GEF family to enhance its private sector collaboration – both in terms of quality and quantity. The three initiatives this framework presents are pilot partnership projects, a knowledge management system, and risk-mitigating financial instruments. This strategic framework is not a radical departure from past practice. Rather, working as before to fund activities through the focal areas, GEF proposes modest initiatives and achievable next steps to codify the principles and to standardize and facilitate the process of GEF engagement with the private sector.

4. Operational experts throughout the GEF family have contributed valuable ideas and effort to help identify the right priorities for action, operating principles, metrics of success and failure, and new initiatives that, taken together, will constitute a comprehensive strategic plan. The proposed strategy will guide GEF's engagement as an organization, giving immediate operational effect to reforms. Within each focal area, the GEF will shape initiatives to address country-specific conditions and priorities; facilitate dialogue with the private sector; target selected near-term opportunities to demonstrate early results; and tie together into an integrated program the specific elements across the spectrum of the GEF's work.

5. The timing is opportune for an energetic initiative to build new GEF-private sector partnerships, as evidenced by the increased global urgency in seeking new approaches to sustainable development. Even though the private sector must inevitably be regarded as a source

of both the problem and the solution, better alignment of public-private interests is both an important goal and a realistic prospect. Private enterprise is increasingly being seen as a key to sustainable economic development, and is contributing to leading watershed protection, carbon reduction programs, and biodiversity conservation. This is true for local entrepreneurs as well as multinationals operating in recipient countries of interest to the GEF. Large NGOs are now increasingly engaging in corporate partnerships, such as Starbucks and Conservation International (CI), WWF and the Coca-Cola Company, CEMEX and Profauna, Unidos para la Conservación, Agrupación Sierra Madre, as well as CI and IUCN, and the World Resources Institute Renewable Energy Partnerships. The GEF is well suited to foster such collaboration, particularly with private sector actors in developing countries.

Findings and Recommendations

6. This strategy is the result of an extensive review of Council deliberations, project experience, key management reports such as the third Overall Performance Study (OPS3), and conversations with experts in the GEF family of institutions as well as private sector leaders. This report's recommendations reflect particular consideration of the following points:

(a) The GEF and its family of countries and agencies play a critical role as a catalyst for projects enhancing local and global environmental benefits. Its resources are being spread over a growing list of geographic and focal areas;

(b) Priority goals in the major focal areas cannot be achieved without local capacity building and private sector investment. There is general endorsement of the value of private sector partnerships across a range of experts in the GEF family;

(c) The private sector is not a monolith, but a diverse set of entities, large and small, that can bring potential benefits ranging from capital, expertise, roots in local and international markets, and the ability to build capacity and sustained follow through;

(d) Contemplated private sector partnerships fall in three categories, all requiring attentive management:

  (i) Projects focused on barrier removal and capacity building (including financing);

  (ii) Public-private partnerships serving broad public objectives such as protecting watersheds – for example, sustainable agriculture in sensitive habitats; and

  (iii) Projects which deploy private sector technologies in support of GEF global goals.

(e) The absence of, or lack of ready access to, clear information about GEF processes and project experiences has led to misperceptions in both the public and private

sectors about the opportunities and risks which may flow from GEF-private sector collaboration.

7. GEF also recognizes that some of its most important environmental initiatives may take many years to bear fruit. By GEF's standards, as a steward of global environmental and developmental objectives, a longer time-frame is not inherently undesirable if the end results are substantial and significant. Yet, private companies are driven by metrics of success such as timeliness, quality and quantity of results. To make the GEF's program compatible with those of private sector partners, GEF will review ongoing project initiatives and identify opportunities to bring forward tangible, near-term results as a way of validating, for prospective private sector partners, their commitment to long-term collaboration with the GEF.

8. As a result of these and other findings set forth in the report and the related information document, it is the conclusion of this review that strategically designed and systematically managed private sector partnerships can produce enhanced global environmental benefits if pursued in accordance with a transparent, equitable and accountable process. The strategy reflects a more discerning analysis of the private sector aimed at bringing forward the appropriate private sector partners for each opportunity, country and focal area. In response to legitimate concerns about partnering with the private sector, this strategy proposes principles of engagement, and describes elements of a process (Section 2 and Chapters 10 in the information document). These will meet institutional needs of the GEF and the private sector alike to ensure transparency, equity and measurable net environmental gain; a predictable, efficient process; local capacity; protection of intellectual property; and availability of effective financial instruments. The strategy calls for developing a knowledge base to facilitate project selection and evaluation by better disseminating each focal area's priorities and project experiences (Section 4). This and other specific innovations in Section 4 form the basis for the path forward recommended in Section 5.

Initiatives to Support the Enhancement of Private Sector Engagement within Focal Areas

9. Recognizing that expanded private sector partnering can succeed only if it is viewed as legitimate and equitable, the proposed strategy will allow GEF to build on its private sector experience through development of strategic pilot projects within focal areas. It preserves flexibility as to the nature of engagement and type of private sector entity in different countries and GEF focal areas. It seeks to build a useful knowledge base without changing its basic approach to operations and funding priority projects. To move ahead with the strategy, this report proposes early commitment to pursue three specific initiatives:

(a) <u>Knowledge base</u>: Build on the focal areas' private sector experience to provide a shared understanding of opportunities, common standards of program execution, and a useful clearinghouse of information for the GEF family regarding needs and potential matches of GEF and the private sector or other institutional interests. This will enable a more systematic engagement of business and country stakeholders around appropriate communities of interest;

(b) Pilot fund: It is proposed that funding be dedicated to implement and evaluate a pilot vehicle for private sector engagement, building on the administrative structure of the Environmental Opportunities Facility (EOF)[1]. Success at the pilot phase should be reflected quickly in the design and implementation of larger projects, and the facility would be subject to effective monitoring and evaluation; and

(c) Strategic use of non-grant financial instruments: Through IFC and other entities, strategic application of financial tools such as loan guarantees, revolving funds, special debt instruments and investment funds can be made available to qualifying parties. The key here is a plan for systematically and transparently developing opportunities based upon a menu of already available instruments, ranging from guarantees to grants, with a preference for the least expensive in each case. These opportunities would then be translated rapidly into projects, evaluated, and used to inform future projects.

10. In summary, this strategy does not advocate radical change, but rather proposes to build a framework for private sector collaboration that draws on the lessons of GEF project experience. The framework envisions pilot projects to support innovative private sector initiatives, a knowledge management system, and risk-mitigating financial instruments to enhance private sector engagement within the focal areas. This should enhance the leveraging of GEF resources.

The GEF Secretariat together with the Implementing and Executing Agencies will pursue these three measures, and other tasks delineated in Section 5, and report back to the Council with more detailed proposals in June 2006. In moving forward, the proposed initiatives will take into account the Resource Allocation Framework (RAF) that was approved by Council in September 2005. In the ensuing process, priorities from the private sector perspective will be more systematically engaged in the GEF business planning process. To ensure that the path from concept to execution is as successful as possible, the Secretariat proposes as a first step to build the information base, reach out to other multilateral and private financial institutions, and define specific pilot project priorities.

[1] The EOF is a donor support facility of IFC's Environment and Social Development department, which provides catalytic funding for innovative projects that produce goods and services with environmental benefits. See Chapter 8 in GEF/C.27/Inf for more information on EOF.

FOREWORD

11. The Council has requested that the Secretariat, working in collaboration with the Implementing Agencies, articulate a strategy to enhance engagement with the private sector. On the basis of this request, the first phase of the Strategy to Enhance Engagement with the Private Sector has been prepared. The report describes a concept and provides operational guidance to generate global environmental benefits in a sustainable and cost-effective manner through enhanced engagement with the private sector.

12. Section 1 of the document explores the rationale for private sector involvement. The goals of the strategy and the principles of GEF engagement are outlined in Section 2. Section 3 highlights past and present engagement in three focal areas: biodiversity, climate change and international waters, providing first an overview of the general barriers shared by all focal areas and suggested actions to overcome them and, second, an analysis for each focal area of the status of GEF activities involving the private sector, limitations of the current portfolio, barriers to implementation, and what to do differently. Section 4 proposes initiatives to facilitate private sector engagement, including a pilot GEF public/private sector fund, non-grant/risk mitigation instruments, and knowledge management tools. Section 5 outlines proposed next steps for moving forward with the strategy. A companion information document, GEF/C.27/Inf.7 *Additional Information to Support the GEF Strategy to Enhance Engagement with the Private Sector*, is provided to substantiate the strategy.

13. The Council is invited to review and provide comment on the proposed strategy to advance its further development and implementation.

INTRODUCTION

14. As requested by the Council, the Secretariat and Implementing Agencies have developed for Council review and comment the first phase of a proposed Strategy to Enhance Engagement of the Private Sector[2]. The proposed strategy reflects the collaborative efforts of an Inter-Agency Working Group[3] and consultations with private sector stakeholders. Important insights from preparatory steps undertaken over the years, including policy documents, meetings, workshops and a monitoring and evaluation review (summarized in Chapter 1 in the information document) are captured in this initiative. The strategy, when implemented, will take into account the recent changes in the GEF, including the Resource Allocation Framework[4].

15. Generating global environmental benefits through private sector engagement in the three key focal areas of biodiversity, climate change and international waters serves as the foundation for the strategy. A matrix of recommended tools and activities then provides a framework to enhance and support this foundation. This matrix builds on the principle of incrementality,

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[2] The strategy is an iterative process, and will be updated following guidance from the Council, and when warranted by changes in the internal/external environment.

[3] The Inter-Agency Task Force is composed of GEFSEC,GEFME, STAP, UNDP, UNEP and World Bank/IFC.

[4] With special reference to the Resource Allocation Framework (RAF), endorsed at the extraordinary Council meeting on September 1st.

which underlies the GEF mission, to leverage investments in GEF's focal areas. GEF's review of past experience has yielded important lessons and suggests that having this well-conceived framework for engaging and leveraging the private sector will help the GEF family achieve positive impacts on a larger scale. Success with small-scale demonstration projects will influence local attitudes and, hopefully, inspire replication and better practices more widely.

16. At the November 2004 GEF Council meeting, attention centered on barriers to private sector engagement during the discussion of the *Management Response to the Review of GEF's Engagement with the Private Sector*[5]. Council cited the need to reduce bureaucracy and simplify private sector access to the GEF, and to examine "possible incentives to make collaboration with the GEF attractive for the private sector." Advice was also solicited from Council Members during the preparation of this strategy, revealing that many would like to see an actionable, and less theoretical, approach to private sector engagement. The third Overall Performance Study of the GEF (OPS3) similarly recommended that a private sector pilot program be funded as a special initiative, to test means and modalities of working more effectively with the private sector. These barriers and recommended instruments to overcome them are addressed in Sections 3.

17. OPS3 also suggested that the GEF Secretariat (GEFSEC) maintain a clearinghouse of information on donors and their associated interests as a tool in arranging project co-financing. A broader information management tool for the GEF family is being proposed to improve the quality of the engagement with all stakeholders, including the private sector, while maximizing the benefits contemplated in the area of co-finance.

18. Inputs were also sought from private sector representatives while preparing this strategy (see Chapter 2 in the information document). The following feedback was received:

(a) Leading corporations today <u>do</u> see the link between environmental investments in their communities and enhanced shareholder value;

(b) Most companies are unfamiliar with the GEF;

(c) Companies view environmental issues within economic or industrial sectors, and not according to GEF focal areas;

(d) GEF and the private sector use very different vocabularies, and the language common to the GEF family has no meaning or resonance with private companies;

(e) GEF procedures are cumbersome;

(f) GEF activities are perceived as taking too long to satisfy private sector timeframes;

[5] See Joint Summary, "Highlights of Council's Discussions".

(g) GEF projects must be relevant to business goals; a credible business case is needed for many companies to become involved in GEF projects;

(h) GEF's promotion of policies conducive to environmentally-friendly business activities can be valuable to many companies;

(i) Interested companies do not see the GEF purely as a channel for corporate charitable activities; in order for them to participate, other important entities must be involved;

(j) Multinationals operating in, or sourcing supplies from, developing countries are increasingly attuned to the environmental sustainability of their resource base as well as offsetting adverse environmental impacts;

(k) Companies are not staffed to prepare GEF projects, nor will they invest in personnel solely for this activity; participation must be made relatively straightforward;

(l) Multinationals leading in environmental stewardship have developed relationships and operations with major international and local environmental NGOs, among them: Conservation International (CI) with Shell and Wal-Mart; The Nature Conservancy (TNC) and World Conservation Union (IUCN) with Shell; World Wildlife Fund (WWF) with Coca-Cola, Shell and Unilever; CEMEX with Profauna, Unidos para la Conservación, Agrupación Sierra Madre, as well as CI and IUCN; TRAFFIC-Hong Kong with Cathay Pacific Airways Ltd; Friends of Nature-China with the Beijing Hotel Industry; and Botanical Society of South Africa with the Wine Industry; and

(m) There is increasing private sector interest in carbon finance initiatives, as well as linking biodiversity and climate change impacts.

SECTION I: RATIONALE FOR PRIVATE SECTOR INVOLVEMENT (See Chapter 9 in the information document)

Why the GEF Should Seek Private Sector Engagement

19. Structured correctly, partnership with the private sector will allow the GEF to achieve results on a larger scale than might otherwise be possible.

20. Engagement creates opportunities for the GEF to positively influence private sector practices while benefiting from private sector strengths that contribute to advancing GEF's mission.

(a) The private sector has a deep and pervasive influence – positive and at times negative – in the economies of various countries. At its best, it contributes significantly to:

(i) Replication;

(ii) Sustainability of global environmental benefits;

(iii) Leveraging (human, technological and financial) resources;

(iv) Influence on policy and regulations;

(v) Development and dissemination of technological solutions to environmental problems; and

(vi) Acceleration of research and development.

21. Only by engaging productively with the private sector is it possible to mitigate the potentially very harmful footprint of companies and individual private operators that impact the environment through:

(a) Sourcing raw materials for production and consumption;

(b) Managing landholdings;

(c) Producing waste, pollutants and emissions that might be released into the surrounding environment;

(d) Supporting supply chain partners (and their associated practices); and

(e) Influencing local social and economic development (e.g., migration of people as a result of commercial operations).

Incentives/Motivations for the Private Sector to Engage with the GEF[6]

22. The GEF can add value to the private sector in the following ways:

(a) Partnerships can provide opportunities to sell technology or services that would not attract investment absent of GEF resources (e.g., technology demonstration project);

(b) Partnerships with the GEF will not necessarily benefit the private sector through direct increases in profits, but through longer term benefits of environmental risk mitigation, improved business image/reputation, or access to GEF's global networks and experience;

[6] Incentives were identified through private sector consultations and relevant publications.

(c) A partnership with the GEF is integral to its long-term business development strategy. The partnership may help open markets over the long term, or help to protect current markets by foreseeing environmental risks that may ultimately threaten its business;

(d) Local businesses also have clear incentives to be involved in projects that increase demand and build local capacity to support their products and services and activities in a sustainable manner; and

(e) Among the large companies and multinationals most interested in participating in GEF activities are those that stand to lose the most from damage to corporate brand, image and reputation. Specific benefits include:

  (i) Protection of share value through mitigation of environmental and related business risks: access to capital, land, markets, reputation, security of supply, relations with regulators, liabilities, and insurance premiums;[7]

  (ii) GEF sharing risk with companies and providing financial support for demonstration projects;

  (iii) GEF facilitation of supportive policies and institutional environments conducive to private sector investment;

  (iv) Access to GEF worldwide experience and global information networks;

  (v) Assistance in identifying partnership opportunities;

  (vi) Compliance and moving beyond compliance with environmental regulations and reporting requirements[8]; and

  (vii) Improved local/official acceptance of companies as corporate citizens.

SECTION II: GOALS OF THE STRATEGY AND PRINCIPLES OF GEF ENGAGEMENT

Overarching Goal

23. To generate global environmental benefits in a sustainable and cost-effective manner through enhanced engagement with the private sector, and the alignment of public, NGO and commercial activities toward common goals.

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[7] F&C, Is Biodiversity a Material Risk for Companies, September 2004.

[8] Environmental regulations include EIAs, EU Habitat and Environmental Liabilities (Foreign Direct Liability) Directives and EU REACH Directive. Environmental Reporting include Global Reporting Initiative (GRI), Operating and Financial Reviews, ISO14001 and Equator Principles.

Priority Objectives of the Strategy

24. Strategic objectives include:

(a) Defining operating principles to guide the GEF's work with the private sector;

(b) Identifying initiatives and approaches at the GEF focal area-level that have a greater demonstration and replication potential; and

(c) Proposing instruments and initiatives to encourage and facilitate private sector engagement.

Definition of the Private Sector

25. The private sector is conceived as a basic organizing principle for economic activity in a market-based economy where: physical and financial capital is generally privately owned; markets, competition, and profit drive allocation and production; and decisions are made and risks are taken as a result of private initiative (CIDA, 2003).

26. A strategy to enhance engagement with the private sector must approach each business based on its individual characteristics and motivations. This strategy also recognizes that not all multinational or local companies will have characteristics compatible with GEF's goals, or be inclined to commit resources and pursue long-term efforts consistent with the GEF. The engagement effort will be informed by factors such as those presented in Section 1.

Principles of GEF Engagement with the Private Sector

27. The GEF is committed, as a general principle, to supporting beneficial partnerships between public and private entities that promise the *greatest global environmental benefit* for the lowest expenditure of scarce multilateral resources and the least amount of risk. Under this strategy, GEF will further qualify the participation of private sector entities on the basis of the following criteria:

(a) GEF eligibility criteria are complied with:

(i) Convention guidance;

(ii) Incremental costs;

(iii) Cost-effectiveness;

(iv) Transparency;

(v) Country drivenness;

(vi) Catalytic role and leveraging financial resources and/or appropriate technology;

(vii) Sustainability and replicability; and

(viii) Monitoring and evaluation of inputs and outcomes

(b) GEF will not subsidize the costs of an enterprise's regular business consistent with the incremental cost principle;

(c) Flexibility is exercised to accommodate appropriate types and levels of engagement;[9]

(d) Non-exclusivity is achieved through accessibility to all micro, small and medium enterprises (SMEs), large national corporations (LNCs) and multi-national corporations (MNCs) operating in an environmentally and socially progressive manner (e.g., promoting environmental stewardship, supporting a precautionary approach, and respecting local and international environmental, human rights and labour laws.)[10]; and

(e) Local private sector entities take steps to:

(i) Expand target country national competence and capacity in the areas relevant to GEF's mission; and

(ii) Diversify local private sector participation.

28. GEF is committed to transparency and impartiality in administering this initiative, which will be carried out by adherence to these principles:

(a) GEF IA/EAs will make a good-faith effort to invite the interest of a sufficient number of private sector entities for relevant project opportunities to ensure competitive selection;

(b) GEF will protect the intellectual property of partnering private sector participants that approach GEF with collaboration opportunities; and

(c) GEF IA/EAs will be attentive to target country official processes that could undermine confidence in the equity and transparency of the financial aspects of a project.

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[9] *"There is no single, reproducible process to achieve private sector development that can be applied in all cases, all regions, all countries, all industries or all firms. Each solution must be tailor-made to the institutions, actors and markets that define the initial conditions."* (IDB, 2004)
"Avoiding the 'one size fits all' approach. Partners active in a variety of geographic regions noted that careful business and governance analyses, and flexible design and delivery models, are necessary on a project-by-project basis to ensure effective and sustainable PSD initiatives." (CIDA, 2003)

[10] UN Global Compact Principles.

Process of Engagement

29. The process of selecting private sector partners for projects must not only be equitable and transparent, it must be demonstrably and consistently so in order for a project not to be plagued with challenges, grievances or complaints seeking to reverse selection decisions once made. As Chapter 10 in the information document elaborates, the strategy contemplates a process with several requirements for GEF project eligibility and mechanisms to facilitate the straightforward, competitive and efficient selection of partners, including:

(a) GEF eligibility criteria are satisfied;

(b) GEF financing is strictly for projects that provide incrementality in terms of improving the global environment or advancing the prospects of reducing environmental risk;

(c) A bidding process is designed to ensure[11]:

  (i) transparency;

  (ii) equal opportunity; and

  (iii) low frequency of grievance or challenge registered in response to GEFSEC and IA/EA decisions[12]

(d) An efficient way to post Requests for Proposals (RFPs), solicitations, award notices, etc., with time limits for proposal submissions is developed.

SECTION III: PRIVATE SECTOR ENGAGEMENT FOR EACH FOCAL AREA

30. The strategy targets the three focal areas of biodiversity, climate change and international waters. This section reviews the experience to date with the private sector in these three focal areas as a recipient of GEF funded projects, and as a co-financier.[13] The assessment here of methods, techniques, and/or processes that have worked, barriers that have been encountered, and types of remedies that would be necessary to overcome such barriers, sets the substantive basis for the modes and level of engagement recommended in Sections 4 of the strategy.

31. The strategy must be structured to address the distinctive needs and priorities of each focal area, though a number of barriers and notional solutions are common to all areas:

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[11] Concessionary instruments (see Section 4) will be available when enhanced global environmental benefits are generated through proponents with proprietary technology and/or preferential access.

[12] Depending on other factors including co-financing and local participation, the required competition may precede rather than follow GEF support. For example, a developing country might select a technology supplier through its own review of competing firms prior to approaching the GEF as its investment-backed selection may serve the purposes of competitive bidding more effectively than a procedure administered by an IA.

[13] The strategy does not cover procurement, authority for which strictly falls under the responsibility of IA/EAs.

(a) GEF and IA/EA rules and procedures can be overly time-consuming and cumbersome.[14] The complexity involved in designing and getting GEF projects approved is especially challenging for SMEs.[15] Disincentives particular to private sector participation can be overcome by:

(i) Encouraging a more business-like approach, and a more direct, flexible and responsive interaction between the GEF, IA/EAs and the private sector;[16]

(ii) Determining non-eligible projects rapidly (with a "quick no");[17]

(iii) Improving communication channels (including communication concerning project approval);[18]

(iv) Using straightforward language in lieu of internal jargon and acronyms;[19]

(v) Considering a "single entry point to GEF" for communication with private sector entities;[20]

(vi) Considering incentives such as a private sector pilot facility to enhance direct access to the GEF with reduced transaction costs to access GEF funds. A pilot facility could potentially cut the time and administrative efforts to access GEF funds while allowing for enhanced program flexibility with novel approaches;[21] and

(vii) Setting aside dedicated financing for engaging the private sector that could be competitively accessed.[22]

(b) Private sector actors view the environment as a single issue when planning their commercial activities, and may be put off by GEF's strict categorization into focal areas[23] (although this is less the case with larger corporations).

(i) Be conscious of rigid subdivision into specific sectors and focal areas when designing projects and programs; and

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[14] "Given the uncertainty, risk, and high opportunity cost inherent in GEF projects, private sector firms do not have sufficient incentive to wait up to two years for approval and endorsement" Joint Summary of the Chairs, October 19998 GEF Council meeting, par. 15.
[15] Swiss Agency for the Environment, Forests and Landscape (SAEFL) Workshop Report.
[16] Ibid.
[17] Ibid.
[18] Ibid.
[19] Water operator CEOs in Water Operators and World Bank Roundtable, November 2001 and WBCSD PPP workshop in June 2002.
[20] Swiss Agency for the Environment, Forests and Landscape (SAEFL) Workshop Report.
[21] Ibid.
[22] Engaging the Private Sector in GEF Activities (1999).
[23] Swiss Agency for the Environment, Forests and Landscape (SAEFL) Workshop Report.

(ii) Work with groups or associations of companies focused within specific industry sectors, as industry sectors generally have impacts on more than one GEF operational program area. Building broad-based partnerships and developing strategies with groups of companies within industry sectors can stimulate private sector investment and other actions to address negative environmental impacts, and can generate guidelines that support sustainable business development.

(c) GEF and IA/EAs are risk-averse.

(i) Failures associated with risk-taking should not call into question the validity of the strategy but be analyzed to create a learning experience;[24]

(ii) Formalize a greater commitment to experimentation, with increased flexibility regarding procedures, to enable the GEF to identify and exploit promising new possibilities; and

(iii) Work with a group of companies within a specific industry sector to reduce the risk of directing finance to projects supported by individual or a very small number of companies, thus giving them a commercial advantage.

(d) Private sector entities seeking to maintain commercial confidentiality may be inhibited by the transparency of GEF processes. The private sector is concerned about revealing intellectual property.

(i) While meeting GEF's and the IA/EAs' information disclosure requirements, establish protections assuring that proprietary data and confidential business information will not be compromised[25]; and

(ii) Define criteria, in conformance with the IA/EAs procurement rules and procedures, for GEF support of projects that could involve some element of sole source procurement when the activity is sufficiently innovative, e.g., the private party assumes a greater than usual share of the risk, co-financing is primarily non-grant, and/or the potential benefit is substantial and highly replicable.[26]

(e) GEF is not broadly known within the international private sector and thus lacks a "brand" image.[27]

(i) Pursue better "branding" for the organization in carrying out this strategy;

[24] Swiss Agency for the Environment, Forests and Landscape (SAEFL) Workshop Report.
[25] GEF Strategy for Engaging the Private Sector (1996).
[26] Draft IFC Perspectives and Proposals for a GEF Private Sector Strategy.
[27] Swiss Agency for the Environment, Forests and Landscape (SAEFL) Workshop Report.

(ii) Address “branding” in the GEF’s communications and outreach strategy; and

(iii) Promote a clearer understanding of the GEF’s role, mission, strategies and work methods by disseminating readily understandable information to the private sector.

(f) GEF funding is facing increasing demands.

(i) Provide dedicated finance for private sector activities (initially through a pilot program), taking into account the RAF.

(g) Governments, private sector, and other stakeholders may view themselves as competitors for GEF country allocations.

(i) Demonstrate how a better private sector environmental footprint yields larger overall national benefit despite adding the private sector as a new contributor to achieving the country’s global environmental objectives; and

(ii) Develop an outreach program to inform operational focal points about the strategy, and to provide for a constructive dialogue with respect to their concerns in supporting private sector projects.

(h) There is a lack of capacity, such as finance and business, within the GEF family to support private sector partnerships and to work entirely successfully with the private sector across the range of potential projects.

(i) Enhance the capacity of GEF staff and countries through well-developed procedures for private sector engagement, readily available outside expertise, and training or recruiting of in-house staff with specific private sector skills;

(ii) Dedicate staff to addressing private sector issues; and

(iii) Provide capacity-building assistance to country focal points to aid interaction with the local business community.

Biodiversity [28] (see Chapter 4 in the information document for details)

Status of GEF activities involving the private sector

32. The GEF is already actively conducting significant activities involving the private sector in the biodiversity area:

[28] This section is based on the work of the BD Task Force and the 2004 STAP workshop.

(a) Implementation of the Convention on Biological Diversity (CBD) guidance: “key actors and stakeholders, including the private sector, are engaged in partnership to implement the Convention and are integrating biodiversity concerns into their relevant sectoral and cross-sectoral plans, programmes, and policies”[29];

(b) To date, projects involving the private sector have been largely concentrated in eco-tourism, agro-forestry (coffee and cacao), and silvo-pastoral production activities (certification of commodities, payments for environmental services) both in landscapes outside protected areas and in protected areas at the SME level;

(c) The vast majority of protected area projects have components promoting sustainable and alternative livelihoods. Hence, the GEF has significant experience with strategies to support and influence households and micro-businesses; and

(d) The majority of projects involving the private sector fall under GEF activities to: mainstream biodiversity in production landscapes and sectors**.** Private sector opportunities are also sought to strengthen protected area networks (e.g., private sector concessions, private sector co-financing, private sector management).[30]

Limitations of the current portfolio

33. GEF biodiversity projects involving the private sector present the following weaknesses:

(a) Private sector engagement in the biodiversity portfolio is modest in scope and scale, and concentrated mostly at the farmer level. There is little SME involvement and an absence of participation by national companies, multi-national companies and umbrella trade associations;

(b) There are few projects with a focus on market transformation and public-private partnerships;

(c) The focus of large, integrated production landscape projects has been more on public sector activity and less on market-based interventions;

(d) Few economic and market assessments or effective delivery mechanisms supporting micro-business development and alternative livelihoods have been incorporated in project design;

(e) Systematic assessment of results and gathering of success stories has been inadequate;

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[29] Objective 4.4 of the Strategic Plan of the CBD.

[30] These activities fall under GEF Strategic Priority 2, Mainstreaming Biodiversity in Production Landscapes and Sectors, Strategic Priority 1, Catalyzing Sustainability of Protected Area Systems, and Strategic Priority 4, Generation and Dissemination of Good Practices.

(f) Thus far, the impact of GEF's engagement with the private sector on biodiversity projects is largely unknown;

(g) Little engagement of the private sector has occurred on the demand side.[31] There has not been a project focus on product demand, nor analysis of markets and economic opportunities to stimulate sustainable production of goods; and

(h) Experience to date has been marked by complexities in setting targets and measuring for market transformation within a project.

Barriers to implementation

34. There are constraints and barriers to private sector engagement in biodiversity projects at the market level:

(a) Taking biodiversity values into consideration has often been seen as an undue cost burden and can be perceived to put a business at a competitive disadvantage;

(b) There is a lack of consumer awareness and associated demand for biodiversity-friendly products and services;

(c) Incentives for private sector involvement are insufficient (supply and demand sides);

(d) Long term sustainability issues (particularly for payment for environmental services) are present;

(e) SMEs pressed to comply with requirements of national laws, which go beyond the environmental impact assessment requirements, are faced with private capital limitations;

(f) Governments and the private sector have not traditionally demonstrated an ability to work together to develop supportive policy frameworks, suggesting the need for facilitation assistance;

(g) Staff in the countries and the GEF lack sufficient skill sets required to champion opportunities, sponsor and implement biodiversity/ private sector operations;

(h) Biodiversity is often not perceived as a priority within the management of the IA/EAs and governments; hence biodiversity is seldom mainstreamed in infrastructure, agriculture, fisheries, tourism, and finance operations;

(i) A resulting lack of interest of, and incentives for, sectoral IA/EAs staff in biodiversity/ private sector operations/components exists; and

[31] Meaning buyers, including wholesale companies, retailers and consumers.

(j) Public sector culture and orientation amongst IA/EAs, governments and project design teams leads to under emphasis on the role of the market and market based approaches to biodiversity conservation.

The way forward

35. In light of these conditions drawn from recent experience, the following framework is suggested as a guide to engaging the private sector in the biodiversity area:

(Priority sectors are identified according to their degree of impact upon globally-important biomes[32])

Biome/Sector	***Agriculture***	***Forestry***	***Fisheries***	***Tourism***	***Infrastructure and Transport***	***Oil, Mining and Gas***	***Banking, Insurance***
Tropical Forests	X	X			X	X	X
Temperate Grasslands	X				X		X
Mediterranean	X						X
Tropical Grasslands and Savanna	X					X	X
Inland Water	X		X		X	X	X
Coastal	*X*[33]		X	X	X	X	X
Marine	*X*		X	X		X	X
Island	*X*			X	X		X

36. The private sector can be involved in four types of mainstreaming projects, both inside and outside protected areas: spatial, sectoral, institutional and market:[34]

(a) **Spatial** mainstreaming: ensuring that biodiversity considerations are effectively internalized into the planning and management processes of a particular spatial area;

(b) **Sectoral** mainstreaming: internalizing biodiversity into a particular sector;

(c) **Institutional** mainstreaming: internalizing biodiversity into a company and all its operations to reduce its ecological footprint and to foster innovative partnerships and approaches to conservation that can be adopted by other companies in similar fields; and

[32] Matrix of “Drivers of Change in Biodiversity and Ecosystems” (CWG, Millennium Ecosystem Assessment, Synthesis, Figure 13).
[33] Italic *X’s* were added by the Inter-Agency Working Group and are not part of the original MEA Figure 13.
[34] While distinct, these are not mutually exclusive.

(d) **Market** mainstreaming: balancing the approach of threat removal with the pursuit of opportunities to influence production sectors and systems in newly-created markets.

37. The level and nature of private sector involvement in a project will depend upon its influence on biodiversity and private sector interest in being part of the solution. Detailed assessments are necessary to identify the source of threats to biodiversity in a given landscape, link them to markets and private sector stakeholders, and select appropriate opportunities for collaboration through identification of joint goals.

38. These activities have been demonstrated through various GEF projects, including the following:

(a) *Central American Markets for Biodiversity (CAMBio):* Supporting SMEs in a broad range of economic sectors (agriculture, sustainable forestry, ecotourism, etc.) to develop biodiversity-friendly business ventures and access new markets for their products and services. The partner bank – CABEI – provides loans, financial instruments and technical and business management capacity building to entrepreneurs across Central America. The program is gaining popularity and validating the utility of working in a defined geographic area to bring together government and NGO players, all the while fitting into the existing financial sector through CABEI's developed network with 150 financial institutions;

(b) *Biodiversity and Agricultural Commodities Program (BACP):* Identifying a small number of priority commodities and working with key private companies and other stakeholders to implement and accelerate the adoption of better practices. The BACP commodity-wide initiatives, in combination with market forces, can then lead to replication of these new practices by other producers; and

(c) *Mainstreaming of Biodiversity Conservation into Coffee Production and Sales through Private Sector Sourcing Partnerships*: Working with coffee companies to transform the way that coffee is sourced. This program increases the supply of certified sustainable coffee; promotes sustainable production practices; improves the economic well-being of coffee farmers and workers; and establishes new environmentally and socially responsible ways of doing business.

Climate Change (see Chapter 5 in the information document for details)

39. The private sector constitutes a major source of global greenhouse gas (GHG) emissions, while at the same time it also controls most of the technologies and capital that hold potential solutions to the climate change problem.

40. Therefore, GEF engagement with the private sector should:

(a) Promote activities by the private sector to reduce GHG emissions;

(b) Support the private sector to develop and transfer climate-friendly technologies; and

(c) Help expand the markets and provide increased business opportunities for the private sector in replicating these practices.

Status of GEF activities involving the private sector

41. The modes of engagement in the private sector within the GEF climate change focal area have been three-fold. First, the private sector is engaged as a beneficiary of GEF-funded projects and activities in that GEF projects provide the policy environment for private sector investments. Some projects even deliver technical and financial assistance directly to the private sector. Second, the private sector is engaged as a co-financier of GEF projects mostly as an investor in, and owner/operator of, climate-friendly projects. Third, the private sector is engaged as a provider of technologies as well as goods and services tendered by the GEF projects. Almost all projects in the climate change focal area have some kind of private sector engagement in these forms.

42. Private sector-related GEF activities have been undertaken within all four operational programs of climate change:

(a) Removal of barriers to energy efficiency and energy conservation. [35]

(i) Market transformation programs involving both demand-pull and supply-push strategies, such as consumer awareness and quality assurance efforts;

(ii) Over 25 projects promoting energy service companies (ESCOs) and buying down associated market risks;

(iii) Facilitation of access to financing through local financial institutions (mainly to benefit SMEs without borrowing capacity); and

(iv) Technical assistance and capacity building.

(b) Promoting the adoption of renewable energy by removing barriers and reducing implementation costs. [36].

(i) On-grid market: Working with governments to provide attractive conditions for independent power producers (IPPs) investments;

[35] climate change operational program 5.
[36] climate change operational program 6.

(ii) Off-grid market: technical assistance and financial support for expanding the businesses of private entrepreneurs and dealers of distributed energy equipment; and

(iii) Support to equipment vendors and financial intermediaries to facilitate credit lines for the consumers of energy products.

(c) Reducing the long-term costs of low greenhouse gas-emitting energy technologies and sustainable transport.[37]

(i) Private sector is the main equipment supplier;

(ii) Limited private sector participation as owner/operator of the new technologies in some projects due to perceived high risks of investing in new technologies in unfamiliar countries;

(iii) Investments in concentrated solar power have been converted into public utility-style projects to make the risks more bearable for all participants; and

(iv) New types of technologies and applications relating to a specific development problem are being promoted to encourage innovation and greater private sector participation.

Barriers to implementation

43. There are no particular barriers to engaging the private sector that are unique to the GEF climate change focal area. The following barriers identified relate to the complementary use of the GEF and carbon finance resources:

(a) The different mandates of the two instruments serve distinct functions.; and

(b) Limited guidance from the UNFCCC or the GEF Council on the possible modalities of building synergies between the GEF and carbon finance.

The way forward

44. GEF engagement with the private sector in the climate change focal area will focus on technology transfer, improving capacities and strengthening enabling environments as well as providing incentives for investments into clean technologies.

45. The GEF will continue to facilitate the transfer of climate-friendly technologies between countries using the conceptual framework it has developed for technology transfer based upon

[37] climate change operational programs 7 and 11.

the removal of barriers to the uptake of the technology. Recent analysis – supported by the results of the Climate Change Program Study (CCPS2) and OPS3 – has highlighted the importance of barriers pertaining to the policy environment, technological knowledge and experience, information, financing, and business models and services, that prevent wider dissemination of these climate friendly technologies. The GEF will continue to serve as an honest broker – north-south, south-south, and public-private – to be able to achieve this mission.

46. To this end, the GEF will explore opportunities to build synergies and foster collaboration with other venues for supplying clean energy development such as carbon finance. Three models can be envisaged for GEF collaboration with carbon finance. These options can help harmonize the GEF top-down barrier removal and market transformation approach with the bottom-up, project-by-project approach of carbon finance. Moving forward on this front should strengthen GEF's engagement with the private sector in GEF climate change activities, since the private sector is often the developer, sponsor, and financier of carbon finance projects as well as the buyer of the carbon credits generated.

(a) Use GEF funds to remove barriers to investment in carbon finance and demonstrate the technical and financial feasibility of investment activities. Replication of these investments can then benefit from the additional revenues accruing through carbon finance. GEF funds would not be used to carry out specific activities required for certifying carbon finance activities such as establishing baselines or developing monitoring plans;

(b) Use GEF funds to remove specific financial barriers to investments (e.g., through a guarantee facility) for projects that may qualify for carbon finance support. The GEF project would not count the anticipated carbon credits, while for the carbon finance projects, the credits would not be registered if the guarantee is called; and

(c) Use GEF funds to support projects in other focal areas that can earn carbon credits. The GEF would finance the incremental costs of components of a project relevant to focal areas other than climate change, while the carbon finance component would derive credits for carbon reduction. GEF funds would not be used to pay for the transaction costs involved with the issuance of carbon credits, including methodological development, verification, and certification.

International Waters (see Chapter 6 in the information document for details)

Status of GEF Activities Involving the Private Sector

47. The international waters focal area includes a number of regional projects that have tested different ways of engaging the private sector and business community to help protect water resources. These activities include:

(a) Businesses and industries collaboratively reducing discharges into Batangas Bay, Philippines, and dialoguing with regulatory agencies on future pollution reduction (PR) requirements;

(b) 'TEST'[38] projects: Pilot audits and feasibility studies with individual industries in the Danube Basin to identify PR measures that pay for themselves in a short time period. Concepts are approved for replication in the Mediterranean and Dnipro basins;

(c) Six projects ongoing in Eastern Europe and Asia to provide cost-sharing incentives as well as technical assistance for farmers and the agribusiness community to leverage pollution-reduction investments (e.g., the East Asia project, which is expected to leverage $25 million from the agribusiness community);

(d) Lending by financial intermediaries to SMEs in Slovenia to install PR measures that reduce toxic substances polluting rivers;

(e) Investigation of public-private partnerships in East Asia through:

    (i) Advisory committees to the regional project; and

    (ii) Testing new satellite technology for preventing ship collisions and for avoiding contact with important ecological areas (with co-funding by Intertanko, a shipping industry association).

(f) Testing new, innovative means of financing to support public-private partnerships (such as revolving funds); and

(g) Oil/gas/mining industries providing co-financing in GEF projects (e.g., Benguela Current, Caspian Sea):

    (i) Mobilizing the participation of multinational companies in GEF regional international waters projects;

    (ii) A global dialogue on private sector and marine overfishing; and

    (iii) Use of ISO certification in East Asia coastal areas.

Limitations of the Current Portfolio and Barriers to Implementation

48. In the international waters area, as elsewhere, there are limiting factors:

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[38] Transfer of Environmentally Sound Technologies.

(a) The international waters portfolio is maturing to the point that in certain transboundary water basins, a transition is now needed from enabling activities in regional projects to on-the-ground implementation in sectors creating stress on the transboundary waters. Demonstration efforts have been successful in engaging the private sector, but have been limited in scope and scale as part of balancing requests from governments in the GEF projects. Projects facilitating large private sector investments have not been forthcoming;

(b) Additionally, barriers to more substantial engagement in mobilizing private sector finance for infrastructure in order to reduce pollution and increase water use efficiency, include:

    (i) A poor investment climate in water infrastructure, given the uncertainties surrounding the privatization of this infrastructure; and

    (ii) Insufficient engagement between GEF and infrastructure staff in the private sector arms of IA/EAs and target countries.

The way forward

49. Now that many joint action programs for implementation have been agreed, the potential of the private sector contributing to widespread impact needs to be harnessed by agencies. Implementation should focus on the following:

(a) Pollution reduction, particularly municipal sewage (the world's largest pollution source), industrial pollution and ship-related contaminants;

(b) Water use efficiency, in cases of excessive water diversions;

(c) Reduction of fishing efforts and use of proper gear; and

(d) Transboundary water resource management/cooperation.

50. Implementation should reflect a greater emphasis on, and more resources for, the following types of interventions:

(a) Developing specific water-related public-private partnerships at scales from local to global:

    (i) Corporate level GEF partnerships with trade associations and opinion-leader businesses in the water area; and

    (ii) Transboundary-level partnerships with countries, GEF agencies, and regional organizations.

(b) Seeking to replicate demonstration-scale interventions in the private sector for more widespread application. (Examples: low-cost constructed wetlands for pollution reduction, recycling and reuse strategies, use of modern technologies, reuse of sewage water in agriculture, and institutional reforms such as ISO14001 with associated spin-off effects);

(c) Piloting innovative finance (such as revolving funds) to catalyze private sector (and agriculture) investments in low-cost technologies needed to sustain transboundary waters;

(d) Offering risk-sharing guarantee products to large companies to foster sewage investments for transboundary systems;

(e) Engaging with the business community, trade associations and individual facilities in cleaner technology and water conservation measures. Multinational companies may be well positioned to pursue these opportunities in partnership with IA/EAs;

(f) Medium-sized projects should be used to test focused, geographically limited partnerships that could be scaled up if successful; and

(g) Enhance capacity by:
   (i) Establishing a private sector advisory committee for the GEF international waters task force to build its capacity to provide leadership within agencies and in country dialogues;

   (ii) Harnessing different units of the agencies or changing the skills mix so as to engage the private sector; and

   (iii) Incorporating a local capacity-building component in GEF projects dealing with municipal infrastructure.

51. These interventions would need to accompany traditional GEF regional projects that are aimed at policy reforms or could otherwise facilitate such investments.

52. Overall, the record of private sector engagement across the three aforementioned focal areas suggests the possibilities for larger-scale positive results, and illuminates important areas of focus in overcoming both general and specific barriers to implementation. These inform the sections that follow, where specific recommendations are advanced to carry forward the private sector strategy.

SECTION IV: INITIATIVES TO FACILITATE PRIVATE SECTOR ENGAGEMENT

53. Sections 4 builds on the discussion in Section 3 of barriers, and contains potential solutions in the form of three instruments – a fund for private sector pilot projects, provision of GEF financing using non-grant instruments and establishing a private sector-focused knowledge management system, to expand and enhance private sector engagement on a global, cross-cutting scale.

GEF Public/private Sector Partnership Fund

54. As reflected in recent discussions with Council Members and business groups, the projects and outreach strategies so far implemented by the Agencies have not fully responded to the need for more effective private sector engagement. There is a perception that a new "public/private sector fund" with administration more consistent with private sector needs may be timely and worthy of some commitment of GEF resources as a pilot program. Existing private sector programs such as Photovoltaic Market Transformation Initiative (PVMTI), Energy Business Finance Program (EBFP) and Renewable Energy and Energy Efficiency Fund (REEF) have narrowly focused on particular segments or technologies. What is needed is a pilot program with wider scope, one that can react in a timely manner to the creative solutions the private sector may propose, without being restricted to a narrow gamut of project configurations.

55. The Environmental Opportunities Facility (EOF), under the administration of IFC, provides a response to the need for more effective private sector engagement. The facility has the benefit of an established administrative structure, several years' experience, financial contributions from five European states to date (Austria, Denmark, Italy, The Netherlands and Norway) and co-financing from the IFC. EOF was established to support ventures with a strong potential to deliver environmental benefits but which face barriers to new markets, technologies and ways of doing business—characteristics also found in GEF operational programs. [39] Details concerning the EOF are provided in Chapter 8 of the information document.

56. If the EOF were to leverage GEF funding effectively, this would allow some pilot projects to proceed and allow testing the private sector response without the need for a new administrative structure. As the EOF project cycle is more rapid than that of the GEF, the EOF could provide initial support or demonstration for GEF projects or serve as a delivery mechanism for some targeted application of GEF resources. GEF resources could be placed in the EOF as an existing fund with many of the attributes sought for a dedicated private sector facility: a simple and rapid decision making structure, an established team of investment officers, and funding from the IFC as well as other donors. Some of its investments are already potentially GEF-eligible, such as those providing risk capital for innovative turbine manufacturers and suppliers of pollution control technologies.

[39] EOF's initial funding target was $25 million. It targets grants of about $120,000 and flexible investment funding averaging $600,000 per project.

57. The main principles for the use of the GEF contribution to the EOF include:

(a) Application of the Incremental Cost Principle. Funds will be used to cover costs associated with generating global environmental benefits beyond the costs to enterprises of doing regular business and meeting legal environmental requirements (i.e., projects should in general not be good candidates to proceed under other vehicles);

(b) Application of all GEF eligibility criteria (e.g. sustainability, replicability);

(c) Projects will be private sector or public/private partnership-driven and the private sector will provide substantial co-funding for each project;

(d) Strong preference will be given to projects which include developing country sponsors;

(e) Referral of projects from existing IA/EA's GEF programs will be welcome;

(f) EOF will deploy a range of instruments to support projects (e.g. grants, reimbursable grants, debt, equity and guarantees);

(g) Approval and processing procedures will be adapted from those currently used by EOF; and

(h) Four main types of projects will include:

(i) projects with financial intermediaries;
(ii) projects with large corporations;
(iii) projects with public-private partnerships; and
(iv) projects with small, highly innovative companies.

58. Pending feedback from Council, a more detailed proposal, which is compatible with the RAF structure, would be prepared and circulated for Council comment toward a submission of a pilot project for Council approval at its May 2006 meeting.

Non-grant/Risk Mitigation Instruments

59. The use of GEF resources to engage the private sector frequently takes the form of below-market interest rates and/or longer repayment terms, risk guarantees, and other non-grant instruments. These modalities address the incremental risks frequently associated with environment-related businesses, particularly the absence of financing on reasonable terms for SMEs and consumers. Appropriately designed and implemented, the use of these instruments in commercially-oriented projects has several potential benefits:

(a) GEF resources may have greater financial leverage insofar as loans are repaid and guarantees are not called. GEF may receive a return on its investment.[40] However, during project implementation, GEF accounting rules result in booking a guarantee at full potential value, and thus for this period may impose a larger cost than a grant;

(b) The introduction of sustainable financial products suited to the characteristics of global environmental enterprises may be a particularly effective means of promoting GEF objectives, as banks and other financial intermediaries are quick to replicate successful lending practices; and

(c) Investment projects are more likely to succeed to the extent participants are at financial risk. Grants may undermine the incentives for diligent management (this is also true of guarantees and other risk mitigation measures if poorly designed).

60. Recent work programs suggest a trend toward increasing the inclusion of loans, guarantees, and other non-grant instruments, particularly in the climate change focal area. Examples include energy efficiency projects approved for Russia, China, Poland, Croatia, and Tunisia, and a renewable energy project approved for the Caribbean. On the other hand, not all investment projects have been successful; several projects using GEF resources in a first-loss position to generate capital for equity funds were unsuccessful and had to be cancelled.[41] These failures highlight some of the risks and limitations associated with non-grant instruments:

(a) Following market trends, including the introduction of new financial products, is no guarantee of success. Many investors lost money in the 1990s due to excess optimism about prospects for emerging market funds;

(b) The design and execution of specialized financial products is a complicated business and requires knowledgeable staff and resources to implement effectively. Specialized financial and legal skills are needed. Local banks and institutions may need considerable training and supervision to internalize the combination of substantive knowledge (energy efficiency economics) and new financial products (partial risk guarantees);

(c) The cost and challenges of introducing and managing these instruments is such that a high volume of transactions and/or the minimum feasible transaction size may be relatively large ($20 million or more in the case of project finance). Local liquidity is effectively a prerequisite to the use of some products (guarantees); and

[40] In the past, GEF has not focused on the return of non-grant resources at project conclusion. Policies and practices related to the administration of these instruments are now being reviewed toward establishing consistent expectations and agency practice.

[41] Dedicated energy investment funds created in the Solar Development Capital (SDC) and Renewable Energy and Energy Efficiency Fund (REEF) were unable to meet rate of return expectations and had to be closed. Remaining SDC funds were returned to the GEF while REEF was restructured with the majority of funds reallocated for use as a source of low cost debt financing for small energy enterprises.

(d) Relatively smaller amounts of aid provided as grants may be quicker, more effective, and equally consistent with commercially-oriented projects (moral hazard concerns). The extra cost and time involved with the design and supervision of loans and guarantees may not be justified.

61. A strength of the family of GEF institutions is the wide range of financial products and services they offer. The World Bank Group, UNDP, and regional banks collectively have a significant role in facilitating financial flows to developing countries, and have accordingly developed substantial expertise and experience in the design, implementation, and dissemination of knowledge related to financial instruments. Even when private sources of capital are available, the presence of these institutions in development projects is often nevertheless essential to overcome perceived political, currency, technology, and other risks associated with investing in developing countries. [42] In summary, non-grant instruments have an important place in efforts to engage the private sector but must be applied carefully and selectively by agencies using the appropriate tools at their command.

The Range of Non-Grant Instruments

62. Non-grant instruments encompass a diverse array of products with differing characteristics that respond to diverse financial needs and circumstances. Examples of non-grant instruments include: [43]

(a) Partial loan guarantees;
(b) Insurance schemes;
(c) Contingent loans and concessional credit;
(d) Reserve funds;
(e) Equity investment funds; and
(f) Contingent grants.

63. These tools are broadly known and understood globally, but their application to particular problems and in specific locations requires careful design and execution. There is an implied hierarchy to non-grant financial instruments, ranging from the least to most expensive, in terms of impact per GEF dollar, e.g., a guarantee to a grant, respectively as presented above. By applying the least expensive tool to meet project needs, GEF and partner funds can be extended over more projects. A number of protocols and implementation issues need to be clarified or revised, including control of financial proceeds, but these instruments are promising components of a strategy going forward.

[42] For example, large energy and mining companies with large capital reserves continue to seek IFI participation in developing country investment projects as a means of mitigating country risks, relying on these agencies to reduce the likelihood of government intervention and corruption. The IFC has developed financial products to package private loans with IFC investments ("B" loans), effectively increasing the value of IFC participation and increasing the impact of IFC due diligence and safeguards policies.

[43] For an overview and description of these instrumentalities with project examples, see GEF/C.27/Inf…Chapter 7.

Choosing and Applying Non-grant Instruments

64. There is an opportunity to enhance private sector engagement through more systematic use of non-grant financial tools by the IA/EAs, including taking lessons from the GEF portfolio and considering the key features and risks associated with non-grant instruments (see below).

65. The choice of a non-grant instrument may depend upon several factors, and features that can make the non-grant instruments widely applicable to country settings and market segments should receive attention in the project design. Features to consider include:

(a) Instruments should be appropriate to the country, [44] market and project setting, and should focus on the critical barriers affecting the project or the market segment. Considering a portfolio of projects and financing instruments can allow a range of projects to be identified and developed in a given setting;

(b) Systemic issues in banking that affect the efficacy of the instruments should be identified and addressed;

(c) Early transactions involving the financing instruments allow IA/EAs with hands-on experience with the instruments to build successful case studies and credibility for the program involving the respective instruments; and

(d) Concurrent monitoring and evaluation of the market as well as the financing instruments can help to institutionalize the procedures. Efforts made to monitor and facilitate the initial transactions can help to adjust procedures to the market.

Risks associated with non-grant instruments

66. The performance of various financing arrangements has been mixed. The following risks have been identified with non-grant instruments implemented so far:

(a) A lack of commercial approach and inability of the project entities to identify financing instruments most suitable to the projects;

(b) Underestimating the technical assistance required to develop the bankable projects and supporting financial products;

(c) Rigid project criteria, high investment and transaction costs coupled with a lack of revenue stream over a long-term, limits follow on investments and provides few incentives for banks to promote the non-grant instruments and bear the associated credit risk;

[44] Many countries have a poorly developed banking sector, some lack liquidity necessary to develop new loan programs, and some simply lack experience dealing with global environment projects and require training and some initial risk mitigation before engaging in a new field.

(d) A grant can improve commercial feasibility through a smaller GEF commitment of resources than the corresponding non-grant instrument. However, the non-grant instrument may be more appropriate and effective and cost less to the GEF if the risk does not materialize;

(e) Non-grant instruments are typically more complex and costly to implement, and thus inappropriate for smaller projects and countries without established financial markets and lenders;

(f) Complexities are associated with introducing new instruments and new environmental markets simultaneously in countries where local banks lack experience with the requisite financial instruments; and

(g) Implementation of projects incorporating non-grant instruments requires specialized staff and experience.

Knowledge Management Tools

67. There is a need for management tools to facilitate the flow of information in developing private sector partnerships and projects with the GEF family, and to measure progress of such projects.

Knowledge Management

68. A centralized knowledge system would be established to address priorities and opportunities for forging mutually beneficial partnerships and to facilitate the creation of a greater number of more effective partnerships.

69. The proposed tools would include:

(a) An information database;
(b) A marketing tool; and
(c) A monitoring and evaluation tool.

70. All of these tools would help advance the following overall objectives:

(a) Providing the ability to analyze data, share information, and report and archive data;

(b) Addressing the needs of all stakeholders, including the Council, countries, private sector and NGOs;

(c) Providing the ability to interact with partner agencies (and their knowledge management systems), including the Trustee;

(d) Incorporating the needs of the GEF Office of Monitoring and Evaluation; and

(e) Providing real-time information for the GEF website.

Information Database

71. Within the GEF Knowledge Management (KM) system, a database will house strategically-collected information regarding partnerships with the private sector. The database will help identify opportunities for a given private sector partner to work with multiple IA/EAs, and thus leverage partnerships throughout the GEF family. This database tool will serve multiple functions, including to:

(a) Disclose identified private sector priorities and project interests in order to match them with GEF's IA/EAs country and focal area priorities;

(b) Flag potential barriers to project implementation throughout the IA/EA community;

(c) Centralize and share lessons learned from private sector partnerships across focal areas and IA/EAs;

(d) Supply project information in an effort to avoid replication of existing projects;

(e) Provide a centralized location for guidance documents, such as case studies; and

(f) Include a mechanism to protect business proprietary information.

72. The database could also provide links to knowledge services and networks of the IA/EAs (e.g., UNDP Knowledge Services, UNEP/GEF Sustainable Alternatives Network),[45] as well as links to Internet sites pertaining to focal areas (e.g., IW:LEARN; and BD-LEARN, which is being developed),[46] and existing public-private partnership sites that could provide useful models as knowledge management tools (e.g., U.S.- Climate Technology Cooperation (CTC) Gateway).[47]

73. The information database will be accessed through two portals: one for the public sector and one for the private sector. These portals will allow the GEF family and the private sector respectively to access the database and cross-reference priorities with those of potential partners, and obtain other information as detailed above. Similarly, the public sector portal will allow the GEF family to view the database of private sector priorities and other relevant information. Each portal will be designed to direct and facilitate straightforward navigation through the database to the information most relevant to the target sector's specific needs and interests. In other words, the portals provide a lens through which to view the information in the database.

[45] http://www.undp.org/knowledge/services.htm. , www.sustainablealternatives.net
[46] http://www.iwlearn.org.
[47] http://www.usctcgateway.net/.

74. To achieve an initial operational capability, the GEF could start right away with the following elements of a database:

(a) Foundation piece: database framework, key components;
(b) Contacts;
(c) Private sector priorities and potential projects; and
(d) Sectoral/focal area priorities.

75. Once the database is more fully developed, it will contain the following key components:

Components	***Description***
Barriers to Implementation	Barrier removal activities to foster an enabling environment for private sector engagement
Financial and Performance Data on GEF	Projects/dollars leveraged, projects/dollars generated, replication, environmental impacts/benefits etc.
Lessons Learned	Previous projects; methodology for determining future projects
Project Summary Information	Information to maximize replication while avoiding duplication of efforts
Private Sector Portal (open access)	Information relevant to private sector needs; place for the private sector to provide information of benefit to the GEF family
Monitoring and Evaluation	Baselines for performance indicators; measurements of project accomplishments

Marketing

76. A marketing tool could be developed that recognizes the private sector for certain environmental leadership achievements, as an incentive for large companies and multinational corporations to partner with the GEF. Such a tool would recognize that the private sector's involvement in a project is in accordance with, and/or exceeds, GEF standards and is aligned with major global environmental conventions. The tool could take the shape of an award, certification/label, endorsement, or other similar symbol of recognition. This tool could help magnify GEF's profile and credibility among private sector entities whose activities are affecting the global environment and potentially catalyze new partnerships to take form. An alternative approach would be for the GEF to help and/or promote other IA/EAs – or other entities[48] – in developing and/or standardizing marketing tools and symbols of recognition for environmental stewardship.

[48] e.g., the World Environment Center (WEC) Gold Metal for International Corporate Achievement and Sustainable Development wec.org

Monitoring & Evaluation

77. A monitoring and evaluation tool is recommended to determine the value-added of GEF funding for private sector activities. This tool would be developed in coordination with, and would be complementary to, the activities of the Office of Monitoring and Evaluation and the greater GEF knowledge management system.

Linkages to Communications & Outreach Strategy

78. The KM system will be linked to the broader, ongoing knowledge management and communications and outreach efforts of the GEFSEC and the IA/EAs, as well as to potential private sector and NGO forums. Communication and outreach will be particularly relevant to ensuring broader awareness of the GEF family and its mission, and subsequently the effectiveness of any marketing tools developed.

Staffing and Resource Requirements

79. Concerted work will be needed to establish a knowledge management system, including:

(a) Developing easy and straightforward procedures for gathering quality data and information, from IA/EAs and other partners;

(b) Establishing initial databases;

(c) Entering gathered data and information into the system; and

(d) Connecting the GEF family to these resources.

80. Additionally, ongoing, periodic updating and improvements will be required so that the set of tools remains useful to the GEF family and private sector practitioners. Corporate budgetary implications are associated with these activities, and additional resources and potentially staff will be required. Overseeing these tasks might best be done by outside experts with the requisite experience and resources. A budget proposal will be made in the context of the corporate/budget request in June 2006.

Key Sectors to Engage

81. In particular, this knowledge management system will focus on those sectors that have been identified as having the biggest environmental footprint[49]:

(a) Agriculture
(b) Energy[50]
(c) Finance[51]
(d) Forestry
(e) Industrial Manufacturing
(f) Mining
(g) Pharmaceutical
(h) Tourism
(i) Transport
(j) Water

Current Environment and Enabling Environment Needed

82. This knowledge management system will enable users to examine the current situation and identify the enabling environment necessary to develop strong private sector partnerships.

Current Context	Enabling Environment
Global environmental issues not at the forefront of government, private sector, and public concerns • Slow economic growth (except for emerging economies such as China) • High unemployment rates • Increasing population pressure • Health issues (HIV, malaria & water borne diseases) • War on terror While environment continues to degrade at an alarming rate (Millennium Ecosystem Assessment)	Enhanced role of the GEF to raise awareness on the economic costs of lack of attention to global issues and benefits of improved environmental performance • Millennium Ecosystem Assessment as a tool • Engage private sector as partner at the global level
GEF currently small player not widely known outside its current partners including the private sector and the public at large	Increase the corporate image of the GEF to gain recognition and credibility • GEF branding- sell our products and their impacts • Outreach – including media/TV campaign
IA/EAs currently ill-equipped to work with the	• Higher commitment and engagement from IA/EAs

[49] *"The Ecological Footprint is a measure of the 'load' imposed by a given [company] population on nature. It represents the land area necessary to sustain current levels of resource consumption and waste discharge by that [company] population." Friends of the Earth International (FOEI).*
"Our definition of environmental footprint is much broader than the traditional industrial measures of wastes and emissions. It includes injuries and illnesses to our employees and contractors; incidents like fires, explosions, accidental releases to the environment, and transportation incidents; global waste and emissions; and the use of depletable raw materials and energy." DuPont.
[50] Includes Oil & Gas, Electricity, Utilities.
[51] The sector's footprint is made indirectly through financing the other industries.

Current Context	Enabling Environment
private sector on a global scale and operate in a risk averse institutional culture	materialized by updated mechanisms • Envisage GEF involvement envisaged with the private sector through existing partnerships or entities within or outside the GEF family
Focal Points resistance to changes and pursuance of individual goals	Engage the Focal Points and Ministries of Finance and Planning
Private sector has different timeframe and thinking	Allowing for faster GEF response

SECTION V: NEXT STEPS – GOING FORWARD

83. Based on the Council's feedback regarding the three initiatives proposed in the strategy, the GEF Secretariat in collaboration with the IA/EAs, will further develop the strategy and report back to the Council in June 2006. The GEF will also embark on the following tasks in line with the comparative advantages of the IA/EAs, and will ensure that the process for engaging the private sector is equitable and transparent.

Focal Areas (Section 3):

(a) Use the presented guidelines to enhance and implement focal area activities with the private sector;

(b) Consider ways in which to overcome the barriers to private sector partnership common to and within each focal area, and to implement focal area-specific solutions that will enable more partnership opportunities with the private sector; and

(c) Partner with the private sector, when solicited, in the development of biodiversity strategies.

Instruments and Initiatives (Section 4):

(a) Develop the specifics of a pilot public/private partnership fund;

(b) Identify the type of appropriation of GEF resources to the fund, within the framework of the RAF,[52] and potential contributions from IFC;

(c) Develop specific operational policies that will allow for increasing the use of non-grant instruments to facilitate GEF-private sector partnerships and test pilot projects;

(d) Engage and seek enhanced input on the strategy from the private sector operating in developing countries and begin to develop pilot project opportunities;

[52] Potential options for sourcing funds have been proposed and will be explored in more detail.

(e) Develop the informational database as part of the larger KM system and tools to facilitate this strategy;

(f) Develop a marketing approach that recognizes private sector environmental excellence/engagement in GEF family projects; and

(g) Liaise with the GEF communication strategy/outreach/marketing activities to increase the GEF's corporate profile.