



# Global Environment Facility

## Summary of Document GEF/C.28/14 GEF Strategy to Enhance Engagement with the Private Sector

### Recommended Council Decision

The Council, having reviewed document GEF/C.28/14, *GEF Strategy to Enhance Engagement with the Private Sector*, welcomes the strategy and notes that it has been prepared in response to the policy recommendation of the third replenishment of the GEF Trust Fund calling for the GEF Secretariat, in collaboration with the Implementing and Executing Agencies, to develop a new strategy to better engage the private sector, taking into account previous practices and policies. The policy recommendation also calls for the GEF, in preparing the strategy, to consult with private sector actors to identify perceived constraints to working with the GEF. It also recommends that clear operational guidelines should be elaborated in order to define the scope of GEF collaboration with private sector activities.

The Council expresses its appreciation for the consultative process that has been followed in preparing the strategy, including consultations with the private sector, and notes that the strategy incorporates the comments that had been made by Council Members at their last meeting.

The Council endorses the operational guidelines that have been proposed to enhance private sector participation in GEF activities, and it invites the Implementing and Executing Agencies to follow the guidelines when developing GEF project proposals with a view to promoting beneficial partnerships between public and private entities that promise the greatest global environmental benefit for the lowest expenditure of multilateral resources and the least amount of risk.

The Council supports the three instruments proposed to enhance private sector engagement, and in this regard, the Council requests:

- (a) the IFC, in collaboration with the GEF Secretariat and the Implementing and Executing Agencies, to develop a project proposal for the establishment of a public/private sector partnership fund for Council consideration at the Council meeting in December 2006;
- (b) the Trustee and the Secretariat, in collaboration with the Implementing and Executing Agencies, to develop operational policies for the use of non-grant instruments, building upon an assessment of the GEF experience in the use of non-grant instruments; and
- (c) the Secretariat to explore tools and opportunities for strengthening knowledge sharing and information dissemination aimed at promoting engagement with the private sector within the broad GEF knowledge management activities.

## EXECUTIVE SUMMARY

1. The Council has requested that the Secretariat, working in collaboration with the Implementing Agencies, update the strategic work<sup>1</sup> to enhance engagement with the private sector.<sup>2</sup> On the basis of this request, the draft Strategy to Enhance Engagement with the Private Sector was presented to the Council for comments in November 2005. Council's comments on the draft November 2005 version have been incorporated in this June 2006 version. The accompanying Cover Note in Annex 1 should be read prior to the strategy document, as it clearly delineates the substantive revisions and specifies their location within the report. 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.

2. The overarching goal of the strategy is to generate global environmental benefits in a sustainable and cost-effective manner through enhanced engagement with the private sector. A means toward achieving this goal is by creating the enabling conditions for private sector investment to engage in commercial activities that deliver global environmental benefits. A clear, transparent and predictable investment climate is a crucial incentive. The role of the GEF is clearly additional to what the private sector is carrying out on its own. Partnership with the private sector will allow the GEF to achieve results on a larger scale than might otherwise be possible. The various ways that engaging the private sector can contribute to the goals of the GEF are outlined, including assistance in opening markets and promoting technologies that would not attract investment in the absence of GEF resources.

3. The GEF plays an important role in creating an enabling environment for private sector investment. Influencing the investment climate pertinent to the global environment in recipient countries can increase the willingness of the private sector to venture into risky markets for environmentally beneficial products and services. By strategically removing market barriers and creating sustainable market conditions, the GEF also paves the way for entrepreneurs to scale up and transform existing markets. Generating global environmental benefits through private sector engagement in the six focal areas serves as the foundation of this strategy. Building on the principle of incrementality, a matrix of recommended instruments then provides a framework to enhance and support this foundation. Section 1 of the document explores the rationale for private sector involvement. The goal and objectives of the strategy and the role of the GEF in promoting the enabling environment for the private sector are outlined in Section 2. Section 3 presents operational guidelines for the participation of private sector as a recipient. Section 4 reviews the experience to date with the private sector, in all the focal areas, as a recipient of GEF funded projects, and as a co-financier;<sup>3</sup> with a focus on three types of engagement: creating an

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<sup>1</sup> This update is based on previous work carried out, including: GEF Strategy for Engaging the Private Sector (1996); Engaging the Private Sector in GEF Activities (1999); Enhancing GEF's Engagement with the Private Sector (2003); Principles for Engaging the Private Sector (2004), all which are summarized in Chapter 1 of the Information Document GEF/C.28/Inf.4. This strategy is also 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 partnership as well as private sector leaders.

<sup>2</sup> The strategy is an iterative process, and will be updated when warranted by changes in the internal/external environment.

<sup>3</sup> The strategy does not cover procurement, authority for which strictly falls under the responsibility of IA/EAs.

enabling environment; demonstration/pilot projects; and strategic/policy dialogue. Section 5 proposes initiatives to facilitate private sector engagement, including a pilot GEF public/private sector partnership fund, non-grant/risk mitigation instruments, and knowledge management tools. Section 6 outlines proposed next steps for moving forward with the strategy. A companion information document, GEF/C.28/Inf.4 *Additional Information to Support the GEF Strategy to Enhance Engagement with the Private Sector*, is provided to substantiate the strategy.

## **Operational Guidelines for Enhanced Private Sector Engagement**

4. The strategy supports 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.<sup>4</sup> Under this strategy, GEF further qualifies the participation of private sector entities based on adherence to: general GEF operational guidelines; guidelines specific to the private sector; and relevant focal area guidelines. Some of the priority guidelines include:

### *General GEF Operational Guidelines*

- (a) GEF strictly finances projects that provide incrementality in terms of providing global environment benefits or advancing the prospects of reducing risk to the global environment;
- (b) compliance with national environmental and social impact assessments and regulations as well as agencies environmental and social safeguard policies; and
- (c) considering the implications for private sector participation and market development as part of an analysis of the existing market and investment climate in all projects.

### *Private Sector Specific Guidelines*

- (a) the GEF's role is clearly additional to what the private sector is carrying out on its own;
- (b) GEF will not subsidize the costs of enterprises in doing regular business consistent with the incremental cost principle;
- (c) ensuring Equity and Transparency through an open, transparent and internationally competitive selection process; and
- (d) substantial co-financing from the private sector.

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<sup>4</sup> See Chapter 8, The Scope of GEF Engagement with the Private Sector, in the Information Document for more information on the potential types of partnerships and categories of private sector institutions.

### *Focal Area Specific Guidelines*

- (a) projects must be consistent with at least one of the focal area operational programs or strategic priorities; and
- (b) activities to reduce negative impacts from industry on biodiversity, climate change, international waters and land degradation need particularly strong incremental costs arguments so that financing of standard mitigation activities are avoided.

### **Private Sector Engagement for each Focal Area**

5. The sustaining core of the proposed strategy and of GEF operations is project activities conducted within the focal areas. This report draws on private sector engagement in all six of the focal areas. In each focal area, private sector involvement has evolved over time based on the focal area specific experiences and lessons learned through three types of engagement: (a) Enabling Environment; (b) Demonstration/Pilot Projects; and (c) Strategic/Policy Dialogue. The biodiversity, climate change and international waters focal areas are already actively engaged with the private sector due to the maturity and size of their portfolios. The land degradation and persistent organic pollutants (POPs) focal areas are initiating, and planning further support to create the enabling conditions for private sector investments.

### *Biodiversity*

7. Under GEF-3, it was fully realized that the objectives of the Convention on Biological Diversity (CBD) can only be achieved if biodiversity is maintained both within and outside protected areas. The necessity for the private sector to play a more central role in GEF projects, and actively participate in sustaining biodiversity within their land use activities, became apparent. In recognition of this fundamental fact and in response to CBD recommendation, the GEF Biodiversity Strategy included a new strategic priority (#2): *Mainstreaming Biodiversity in Production Landscapes and Sectors*. In order to generate higher impacts outside protected areas, the GEF has engaged the private sector in financing conservation in landscapes outside protected area as well as in protected areas. So far, projects involving the private sector have been largely concentrated in *creating the enabling environment* through capacity building and technical assistance in eco-tourism, agro-forestry, silvo-pastoral production activities (certification of commodities, payments for environmental services), and conservation of medicinal and herbal plants – both in landscapes outside protected areas and in protected areas at the SME level.

8. Under GEF-4, the majority of projects involving the private sector will fall under Strategic Priority Two. The objective of *Mainstreaming Biodiversity in Production Landscapes and Sectors* is to internalize the goals of biodiversity conservation and its sustainable use into production systems, supply chains, markets, sectors, development models, policies and programs. The expected result is the overcoming of barriers to changes in production landscapes/seascapes that benefit biodiversity. Target sectors are determined by the Millennium Ecosystem Assessment as having high impacts on habitat change, climate change, invasive species, over-exploitation, and pollution. Hence, areas of concentration include: agriculture,

banking and insurance, fisheries, forestry, infrastructure, mining and gas, oil, tourism, and transport. The private sector can be involved in four types of *mainstreaming projects*, both inside and outside protected areas: spatial, sectoral, market, and institutional mainstreaming.

9. The GEF has a role to play in facilitating *Strategic and Policy Dialogue* on biodiversity related issues affecting the private sector. This includes: influencing relevant fora; promoting programs that target business best practices and accountability; promoting activities that increase consumer awareness and the general public of the biodiversity impacts of companies; and encouraging relationships between GEF's IA/EAs and individual business entities and business associations that focus on maximizing biodiversity conservation.

### *Climate Change*

10. *Barrier Removal to Replicate Demonstration* was the initial focus of the climate change area as at the outset of GEF-1. It was soon realized that demonstration investments were insufficient to ensure the long-term viability of these efforts. Alternatively, barrier removal activities to replicate demonstrations were considered more cost-effective as GEF resources were used to lay the foundation for further private-sector investment into the technologies and interventions that are part of the long-term solution to climate change. Activities focused on creating enabling conditions for private sector investment, including: access to financing, conducive policy environments, appropriate business models and management skills, sufficient information and awareness, and technological factors. An over-arching objective now focuses on *Transforming Markets for Efficient and Renewable Energy Technologies* to ones in which more efficient or renewable technology becomes the norm. This has been best demonstrated with the appliance standards and labels activities. In GEF-4, *Strategic Policy Dialogue* at the global level will focus on efforts to ensure that globalized markets for technology in both developed and developing countries are moving to adopt similar, more efficient and/or more renewable technologies and practices.

### *International Waters*

11. Initial support to countries has been through *Enabling Activities* to engage the private sector as part of initial regional projects. *Demonstration Projects*, mainly in the public sector, ranged from agriculture, industry, and municipal pollution reduction to water use efficiency and science-based management in the fishing and maritime transport industries. *Priorities under GEF-4* are now on-the-ground implementation within sectors creating stress on transboundary water basins. The aim is to catalyze widespread replication and scaling up of successful public sector demonstration projects within the private sector, while continuing to test new technology and innovative approaches to finance. *Policy Dialogue* under the IW focal area has been carried out under the IW:Learn and policy events like the World Water Forum between countries, both at a regional/basin and global level. Reducing discharges and risky substances is envisaged through working with industry associations and industrial groups.

### *Persistent Organic Pollutants*

12. In POPs, possible forms of engagement with the private sector under the Stockholm Convention are being explored, taking into consideration the broad range of stakeholders that POPs affects, such as producers and end-users of POPs pesticides, and operators of hazardous waste disposal facilities. Examples of potential forms of engagement include awareness raising and training, providing incentives to phase out the use of a particular compound and disposing of wastes, and facilitating the adoption of Best Available Technique/Best Environmental Practices (BAT/BEP) through barrier removal-type activities and access to financing.

### *Ozone Depletion Substances*

13. In ODS, supporting technology transfer programs have prompted the private sector to improve the design and quality of their products while remaining competitive in international markets. The GEF experience shows the importance of combining investments that bring about direct ODS reduction with capacity building and institutional strengthening.

### *Land Degradation*

14. Priority support will be given to projects that shape the enabling environment for sustainable forest management. Examples of potential forms of engagement with the private sector include awareness raising and training of private sector entities on sustainable land management (SLM); providing incentives to shift from an unsustainable to a more sustainable land management technique or land use; and facilitating the adoption of available and cost-effective techniques through barrier removal-type activities and access to financing. Capacity development for the private sector will also be provided through sector-wide approaches in projects and programs.

## **Instruments to Facilitate Private Sector Engagement in the Focal Areas**

15. Building on the principle of incrementality, and the foundation of GEF focal area experience, this strategy identifies three cross-cutting instruments that could enable the GEF partnership to enhance its private sector collaboration: a public/private sector partnership fund, leveraging of GEF funding with a more directed approach with non-grant instruments and a private sector-focused knowledge management system are proposed to enhance private sector engagement within the strategic priorities of the focal areas. These three instruments are proposed because: (a) they offer the greatest potential to overcome general and focal area specific barriers (e.g., the risk averse nature and the lengthy processing time of the GEF and its IA/EAs); and/or (b) they reflect established track records in projects, and have a significant potential within particular focal areas to leverage private sector participation if further promoted. These instruments are not a radical departure from past practice. Rather, working as before to support private sector investment enabling 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. Rationales for each instrument are presented in the report, followed by a delineation of each instrument.

## *GEF Public/Private Sector Partnership Fund*

16. A public/private sector partnership fund, with administration more consistent with public-private sector realities, will offer the opportunity for the GEF to mainstream engagement of the private sector in operations through timely reaction to the creative solutions that such a public-private sector partnership could propose.<sup>5</sup> Adopting the efficient administrative structure of IFC's Environmental Opportunities Facility (EOF) will enable GEF funding to be effectively leveraged for some pilot projects.

17. The main principles for the use of the GEF contribution to the proposed fund are outlined, including application of the incremental cost principle and all GEF eligibility criteria, as well as substantial co-funding from the private sector. Additional specifics of the fund, including implications of the Resource Allocation Framework (RAF) are also discussed.

## *Strategic Use of Non-grant/Risk Mitigation Instruments*

18. The use of GEF resources—in the form of non-grant instruments—has helped the private sector address the incremental risks frequently associated with environment related businesses, particularly in the absence of financing on reasonable terms for SMEs. A trend toward increasing the inclusion of loans, guarantees, and other non-grant instruments has been witnessed in recent work programs, particularly in the climate change focal area to leverage GEF grants.

19. Non-grant instruments have an important place in efforts to engage the private sector, but must be applied carefully and selectively by multilateral and regional development banks using the appropriate tools at their command.<sup>6</sup> New and innovative non-grant instruments are constantly being devised in response to changing investment climates and market conditions. They encompass products with differing characteristics that respond to diverse financial needs and circumstances. The various instruments—such as partial loan guarantees and concessional credit—are defined, and the conditions and context under which these instruments should be applied are illustrated.<sup>7</sup>

## *Knowledge Management Tools*

20. Specific management tools can facilitate the flow of information in developing public-private sector partnerships and projects with the GEF partnership, and can measure progress of such projects. As part of a GEF knowledge management system, a component will be established to address priorities and opportunities for forging mutually beneficial public-private partnerships. The specific features of the private sector component are described, including an information database.

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<sup>5</sup> Recent consultations in Brazil and India revealed top interest for the fund accompanied by a RAF allocation. They viewed the proposed pilot fund as a sine qua non instrument without which the benefits would not outweigh the costs to engage with the GEF.

<sup>6</sup> The World Bank Group and regional banks have developed substantial expertise and experience in the design, implementation, and dissemination of knowledge related to financial instruments.

<sup>7</sup> See Chapter 13 in the Information Document.

## Next Steps—Going Forward

### *Focal Areas*

21. The GEF will continue to carry out the work outlined in the focal area sections—making use of the proposed operational guidelines to strengthen its work with the private sector. Ensuring an enabling environment for private sector investment; transforming markets for environmentally friendly products and services; and increasing efforts to engage the private sector at the global level, will continue to be major objectives in the focal areas having significant experience with and relevance to the private sector.

### *GEF Public/Private Partnership Fund*

22. Based on the Council's approval and the outcome of the GEF-4 Replenishment, operational aspects of the pilot public/private partnership fund will be finalized and implementation launched. The fund will be reviewed two years following its launch to assess its effectiveness.

### *Non-grant/Risk Mitigation Instruments*

23. The GEF will encourage the use of non-grant instruments amongst the multilateral and regional development banks. The next steps include: (a) developing operational policies with the Trustee for increased use of instruments;<sup>8</sup> and (b) assessing the experience in the use of non-grant instruments with a cross-cutting evaluation to categorize, summarize, and evaluate the range of operational experience.

### *Knowledge Management Tools*

24. The GEF will continue to develop and implement a knowledge management system to enhance the work of the GEF partnership. The private sector component will be structured within the umbrella knowledge management system, and will be continually updated and expanded with new information from governments, the private sector, IA/EAs, donors, project reviews, private sector consultations, etc.

25. More expansive communication and outreach will continue to ensure broader awareness of the GEF partnership and its mission, and subsequently the effectiveness of any marketing tools developed. Options for encouraging private sector associations to provide input at GEF Council meetings will also be explored.

### *Engaging with the Private Sector*

26. Where and when opportunities arise, the GEF partners will continue to engage and seek enhanced input on the strategy from private sector entities operating in developing countries.

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<sup>8</sup> A number of protocols and implementation issues need to be clarified or revised, including control of financial proceeds.



The GEF partners will also actively seek out pilot project opportunities with individual companies and business associations.

27. 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 recommended Council decision and the section on Next Steps outlines the way forward for proceeding with focal area activities and the three supporting instruments.

28. GEF 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.