REDD+ Market : Sending Out an **SOS**

Near-term REDD Credit Supply / Demand Imbalances Threatens to Undermine the Future of Avoided Deforestation Projects

In Brief

The future of a mechanism for REDD+ is currently under threat. Early actions on REDD+ at the site level to reduce emissions from deforestation have not been met by similar progress at the international level in generating demand for forest carbon credits. The result is a near-term oversupply of verified emission reductions from REDD+ projects that has the potential to expand over the coming five years to over 20 times the current market demand. Such a market imbalance will depress prices for REDD+ credits, cutting off finance to projects that have not only succeeded in reducing deforestation but are also delivering multiple social and environmental benefits. A lack of finance to reward these successes would send a strong and worrying signal to all countries embarking on efforts to reduce deforestation and improve the provision of environmental services - their successes may not be greeted with further support but rather indifference and uncertainty. Such a signal would provide limited motivation to press ahead with the politically challenging, complex and long-term reforms needed for REDD+ to succeed.

A Call Answered

Calls for early action on REDD+ in 2007 and 2010 UNFCCC meetings led many countries, organisations and communities to embark on ambitious programmes to address deforestation and forest degradation through national programmes and site-based projects. These initiatives are now starting to deliver the results requested by the international community, both in terms of emissions reductions and multiple social and environmental benefits.

These successes are set to continue, with projects registered under just one of the voluntary carbon market certification schemes having the potential to supply nearly four times the total level of emission reductions issued to date. These successes on the ground are, however, not being met by commitments of further support from the international community. Instead, slow progress in international climate change negotiations and a fragmented donor and compliance

The Situation In Numbers

14 million
number of at risk hectares protected through REDD+ projects since 2012

73
number of projects validated under the CCB Standard as of May 2013

5
number of REDD+ programs likely to be supported by the FCPF Carbon Fund

22 million
potential annual REDD credits generated by existing VCS REDD projects

6.8 million
current voluntary market demand for REDD credits

$6-7 USD
average market price for REDD credits in the voluntary market in 2012 – down from $12 in 2011

landscape have left REDD+ projects battling for buyers within the relatively small voluntary carbon market.

Should the situation continue, there is a realistic possibility that many projects will be unable to find sufficient finance or demand to maintain their activities and start to fail even before an international agreement on REDD+ is reached. Such failures would not only result in a reversal of the successes achieved in conserving critical ecosystems and supporting poverty alleviation but would also destroy the hope that communities and national governments have placed in the international community to uphold their promises to deliver payments for performance to address climate change. Such a loss of trust would take a long time to repair -- time that neither the world's forests nor climate have available.

While the donor community has made some efforts to address this lack of payment for performance through mechanisms such as the World Bank Forest Carbon Partnership Facility's (FCPF) Carbon Fund, Germany's REDD+ Early Movers Fund, and the future Green Climate Fund, these schemes are limited in the level of available finance, geographical scope, and speed of implementation. Further action is therefore required to address the oversupply and to help catalyse the private finance necessary to absorb supply and drive further investment and commitments in REDD+. If this is not achieved not only will forests be unable to play an effective role in addressing climate change, but some of the world's most important ecosystems will be lost and with them the livelihoods of over 1billion people.

The current assessment has, through consultation with business leaders, development partners, governments, NGOs and project developers, identified two key tools that could be used to help provide a more stable environment for both investors and communities and address the potential levels of oversupply. These are:

Establishment of price support for REDD+ projects – a strong commitment to purchase credits of suitable standard, both from the public and private sector, would provide a clear indication to the market, country governments and communities that REDD+ is here for the long term. This could be established in a number of ways, including creating new dedicated REDD+ credit purchasing windows within existing climate funds, the expansion of current voluntary offsetting programs by companies, the creation of Advanced Market Commitments by REDD+ donor countries, and the expansion of existing risk guarantee products to cover market price risk. Such actions would help catalyse further investment as well as stabilise existing projects over the coming years, reducing the vulnerability of communities to decreasing market prices for REDD+ credits.

Recognition and support of the multiple benefits that REDD+ projects deliver – REDD+ projects have been successful in delivering a range of sustainable development and environmental outcomes, from improved health and livelihoods to the protection of critically endangered species. Existing and upcoming funds assigned to achieve similar outcomes need to look at REDD+ projects as a potential mechanism to deliver sustainable development results, thus moving away from "offsetting" and towards "paying for impact." In the case of REDD+ projects, this impact is quantified and independently verified through the use of standards, which should be attractive to a number of potential buyers while also removing emission reductions. Co-financing in this way would help stabilize projects, reduce oversupply, and help cement linkages between multiple benefits and emission reductions.

REDD+ Market Impact

Projects that seek to reduce or sequester carbon emissions from land use change, known collectively as "REDD+", focus on either avoiding deforestation, restoring habitat, or improving forest management practices. REDD+ projects typically sell carbon credits to finance their activities, which historically has mostly taken place in the voluntary market where individuals or companies are looking to voluntarily offset their emissions. This infographic is meant to relay the impact REDD+ projects have made to date.

Forest Impact

Hectares under increased protection due to REDD+ projects, an area larger than the size of England*

14 MILLION

Delivering Benefits

Just 3 REDD+ projects, Kasigau in Kenya, Alto Mayo in Peru and Oddar Meanchey in Cambodia have provided**

70,000
Local people directly benefiting from project activities

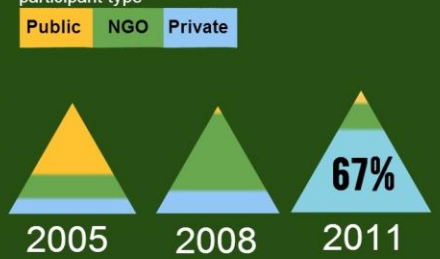
CO2 4Million
Tons of carbon emissions reduced since 2009 due to project activities

139
Red List species habitat protected by project areas

Private Sector

As the REDD+ market matured the risk burden shifted from the public sector to NGOs and eventually private actors who now dominate the space. Policymakers asking "where is the private sector in REDD+?" should take note.

Market share of credits supplied by participant type*



Countries with validated REDD+ projects. To date, a total of 73 projects in 24 countries have been validated to the Climate, Community and Biodiversity Standard (CCBS)**

What do they do?

REDD+ pilot projects are dealing with - and finding solutions to - some of the most important drivers of deforestation including smallholder agriculture and illegal activities. At right, a wordmap of the most repeated words related to drivers of deforestation taken from verified project documentation**

Finding Solutions

To reduce deforestion, projects support a variety of alternative livelihoods and community development projects, in addition to upgrading enforcement of protected areas. At right, a wordmap of the most repeated words related to project approaches to reducing deforestation taken from verified project documentation**

Learning Lessons

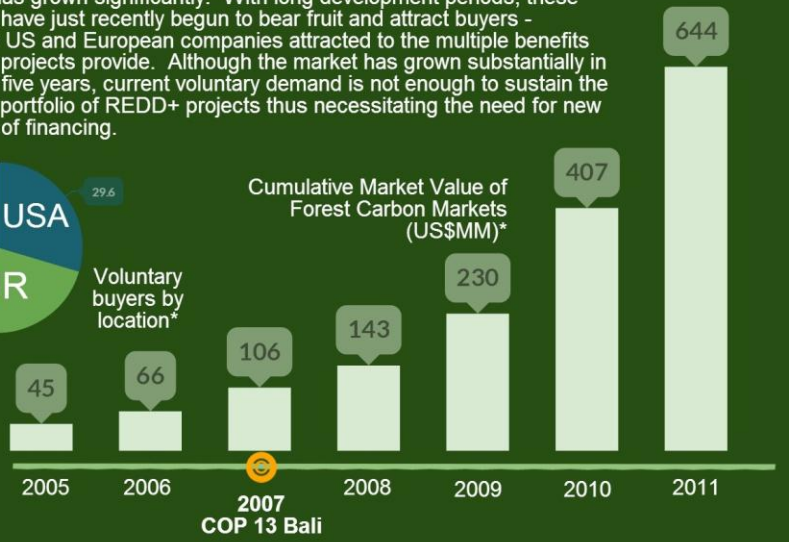
REDD+ projects are feeding directly into the development of national programs by developing and testing new ways to monitor forest health, structure legal arrangements and mechanisms needed to pay for performance, and procedures for ensuring the free, prior, and informed consent of impacted people

- Forest Monitoring
- Benefit Sharing
- Community Consultation

Paying for Performance

Since the 2007 Bali decision encouraging "early action", the REDD+ market has grown significantly. With long development periods, these projects have just recently begun to bear fruit and attract buyers - primarily US and European companies attracted to the multiple benefits REDD+ projects provide. Although the market has grown substantially in the past five years, current voluntary demand is not enough to sustain the growing portfolio of REDD+ projects thus necessitating the need for new sources of financing.

Voluntary buyers by location*



** Source: Ecosystem Marketplace Bloomberg New Energy Finance Peters-Stanley M, Hamilton K, and Yin D (2012) Leveraging the Landscape: State of the Forest Carbon Market. Available at http://www.forest-trends.org/publication_details.php?publicationID=3242*
***Source: Numbers taken from the projects' CCB and VCS documentation (PDDs, monitoring, and verification reports)*
Wordmaps created using Tagxedo

CONSERVATION INTERNATIONAL

Off to a Fast Start

Forests are important. They are central to the livelihoods of up to 1.6 billion people, are home to 80% of terrestrial biodiversity and provide a suite of environmental services that we are still only just beginning to understand[1]. They are, however, disappearing at an alarming rate with deforestation estimated at between 12-15million ha[2] per year.

REDD+ is recognized as a critical part of the fight against climate change. Analysis of the potential role of forests in addressing climate change identified the need to halve levels of deforestation by 2020 if forests were to play their part in preventing dangerous levels of global climate change[3]. To achieve this goal it was estimated that between $15 and $45 billion in financing per annum would be required[4].

> *'Continuation of current levels of deforestation will have serious implications for global security. In security we refer to security of food, water, energy, health and the livelihoods over a billion people'*
> ***Andrew Mitchell** – Executive Director, Global Canopy Programme*

The international community responded to these assessments by initiating efforts to develop a mechanism to provide positive incentives for reductions in emissions from deforestation and degradation (REDD+) within developing countries. Calls for 'early actions' [5] to prepare and demonstrate how this could be achieved resulted in international donors, development partners, foundations and NGOs committing an estimated $7.3 billion over five years from 2007 to help get ready for REDD+ and fast start any future mechanism[6].

Progress within the international negotiations and early financial commitments have led to the establishment of a range of national and site level REDD+ schemes globally. Development partners and national governments established national-level readiness initiatives in over 50 countries and donors have made over 250 agreements to support NGOs and communities working to test practical site level approaches to REDD+ in demonstration activities[7]. While national-level initiatives are working to support capacity building and the development of national strategies, site based activities have been more focused on piloting on-the-ground solutions to drivers of deforestation and the associated mechanisms needed to monitor impact and share benefits – thus very complementary to each other .

Delivering Impact

Early action on REDD+, driven by international donors and NGOs, has supported the improved management of over 14 million ha of forest through REDD+ projects[8]. These projects have delivered significant emission reductions with REDD projects registered under the Verified Carbon Standard (VCS) issuing over 5 $MtCO_2e$ of verified emission reductions (VERs) to June 2013[9] - the rough equivalent of taking all of Washington DC's cars off the road for four years.

[1] UNEP. Benefits of Forests, Forest Facts, Website of the UNEP, accessed November 20, 2012 at http://www.unep.org/wed/forestfacts/

[2] Estimates vary. The FAO estimates 13 million hectares a year are being lost.For details, see http://www.fao.org/forestry/fra/remotesensingsurvey/en/

[3] See Eliasch, J. 2008. Climate Change Financing Global Forests. The Eliasch Review. Office of Climate Change, London, UK. http://www.official-documents.gov.uk/document/other/9780108507632/9780108507632.pdf and Meridian Institute. 2008. Reducing Emissions from Deforestation and Forest Degradation: an Option Assessment Report. Prepared for the Government of Norway, by Angelsen, A., Brown, S., Loisel, C., Peskett, L., Streck, C. and Zarin, D.

[4] Ibid

[5] Bali Action Plan – available at http://unfccc.int/resource/docs/2007/cop13/eng/06a01.pdf

[6] Simula, M, (2010), *Analysis of REDD+ Financing Gaps and Overlaps,* REDD+ Partnership, Ardot, Helsinki, pp. 29 ff. Available at http://reddpluspartnership.org/25159-09eb378a8444ec149e8ab32e2f5671b11.pdf

[7] Number of national level initiatives identified with reference to UNREDD (www.unredd.org) and FCPF (www.forestcarbonpartnership.org) websites while number of project agreements taken from REDD+ Partnership REDD+ Financing website (http://www.reddplusdatabase.org)

[8] Peters-Stanley M, Hamilton K, and Yin D (2012) Leveraging the Landscape: State of the Forest Carbon Market. Available at http://www.forest-trends.org/publication_details.php?publicationID=3242

[9] Information based on VCS, VCU database of projects using REDD methodologies data downloaded 06/2013

These emission reductions, however, tell only a small part of the success of site-based activities. REDD+ projects have also made progress in delivering multiple social and environmental benefits through working closely with forest dependent and indigenous communities.

Environmental benefits from REDD+ projects stretch well beyond the emissions reductions they deliver. In supporting the improved management and protection of natural forests REDD+ projects are providing a vital window for conservation of some of the world's most vulnerable species as well as the ecosystems on which they rely.

Social benefits have been tailored to specific communities and have focused not only on addressing the drivers of deforestation but also addressing poverty and supporting sustainable development initiatives in pilot areas. Recent reviews of the impact of projects have noted their value in addressing poverty through empowering communities and providing them with enhanced livelihood opportunities and security in terms of land tenure and greater economic certainty.

> *'The REDD+ Project has really transformed the lives of the people. The community now owns the project through their own initiatives, they now grow seedlings and sell them back to Wildlife Works giving them more economic empowerment and turning them against tree cutting.'*
> ***Chief Pascal Kizaka** – Coast Province Kenya – Kasigau REDD+ Project*
> *(REDD Talks April 2013)*

Communities in many project areas have been empowered to develop and lead projects in partnership with external specialists. Safeguards such as requirements for Free Prior Informed Consent (FPIC) have helped structure these processes and ensured on-going engagement throughout a project's development and implementation phases. Some projects such as the Surui Indigenous Peoples' Project in Brazil have even been fully initiated and led by the Indigenous communities.

Economic and social benefits have come through the provision of both permanent and temporary employment to local communities as well as investments in education scholarships for communities and even building and funding local schools. A recent review of 41 projects identified them as having created over 1,500 jobs for local people as well as funding over 100 scholarships and the construction of multiple schools [10]. These approaches are normally agreed by community committees and will become more significant as projects move through their lifespan supporting further long-term livelihood improvements[11].

It is in terms of communities' land tenure security, however, that the most significant developments have been achieved. Requirements to provide clear land tenure for projects have resulted in significant investments in clarifying existing land tenure arrangements, in many cases supporting the claims of local communities to their forest areas. Cambodia's two most advanced pilot projects illustrate these developments, with the Oddar Meanchey Project supporting communities to gain management rights over their forest resources, and the Siema Project supporting indigenous communities to gain the first indigenous collective land title in the country.

Such achievements are also now closely measured, monitored and verified through the use of a range of certification standards. Two of the most prominent, the Verified Carbon Standard (VCS) and the Climate Community and Biodiversity (CCB) Standard account for a significant portion of the existing voluntary market with a demand for verification of both carbon, and social and environmental achievements becoming increasingly popular amongst both project developers and buyers within the market.

> *'Contrasting with fears that REDD+ will induce land grabs,…early REDD+ projects are instead doing more to enhance local populations' land claims. This is an important, transformational effect that projects can have—and likely more enduring than carbon payments.'*
> ***Katherine Lawlor** et al (2013) - Community Participation and Benefits in REDD+: A Review of Initial Outcomes and Lessons*

[10] Lawlor K, Madeira E, Blockhus J and Ganz D (2013) Community Participation and Benefits in REDD+: A Review of Initial Outcomes and Lessons. *Forests 4,* 296-318

[11] Current information on economic benefits from projects remains limited as only a few have yet sold credits and fully established their benefit sharing mechanisms.

These achievements have, however, required significant investments from both project proponents, be they NGOs or private sector developers, and the communities living in forest dependent areas. These groups have invested time, resources and their social capital in changing approaches to forest management at the grassroots level. Their investments have been based on the promise of future finance to help maintain project activities and to continue to support the transition from over-exploitation of forest resources to sustainable management of forests, combined with alternative livelihood approaches. A failure of this future support would result in a significant undermining of trust between these local communities, governments, and the international community.

'The model REDD+ project developed in the Alto Mayo Protected Forest can be considered a successful conservation initiative, generating the funding needed for its management and promoting sustainable development in the region– making it a valuable tool for avoiding large scale deforestation in the amazon rainforest with international support.' ***Pedro Gamboa****, Head, Peruvian National Protected Areas Service*

The Supply / Demand Imbalance

Project level activities for REDD+ have evolved rapidly over the past decade from a small number of pilots to a significant number of high quality and standardised activities delivering emission reductions and multiple environmental and social benefits. The speed of their success has, however, not been matched by the development of international and regional markets towards which they had aimed. As 2015 approaches, this mismatch has the potential to reach catastrophic proportions as REDD+ projects reaching verification flood a voluntary market, which is already struggling to maintain demand.

From verification of the first VCS REDD credits in late 2010, the supply of issued VCUs increased

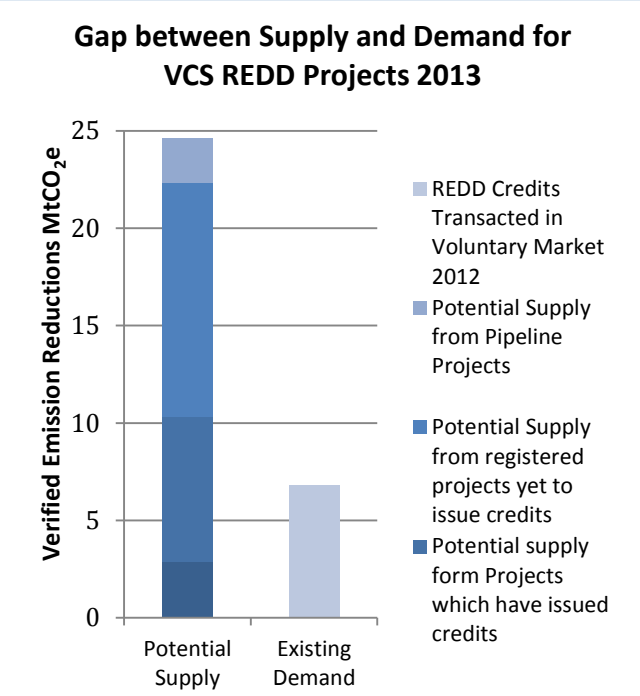


Figure 1 A large supply / demand imbalance is building in the market, with potential to drive REDD+ prices down.

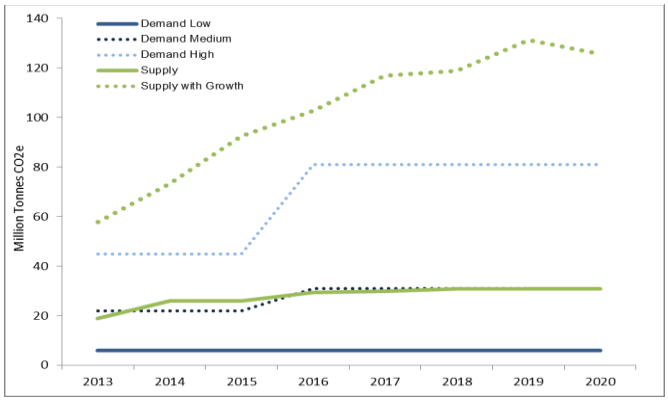
rapidly in 2011 to over 2.$MtCO_2e$ per annum, increasing further to close to 3 $MtCO_2e$ in 2012[12].

These levels, however, represent only the tip of the iceberg in terms of potential supply from registered REDD projects. REDD projects that have already issued credits have the potential to supply over 10 $MtCO_2e$ per annum while those that are yet to issue credits would increase the supply by a further 10 $MtCO_2e$ to over 20 $MtCO_2e$ per annum, over three times the current voluntary market size[13].

Current levels of annual demand within the voluntary market are well below these levels at just 6.8 $MtCO_2e$[14] presenting the risk of large-scale oversupply of credits into the voluntary markets from 2014 onwards. Such a level of oversupply would have a disastrous impact on the potential value of REDD+ credits, forcing prices down to unsustainable levels or preventing many projects from being able to sell at all.

[12] Values are for VCS registered projects only.
[13] Information from VCS Project Database. www.v-c-s.org
[14] Figures on demand taken from Peters-Stanley M and Yin D (2013) Maneuvering the Mosaic, State of the Voluntary Carbon Markets 2013. While these represent total transactions including secondary transactions, it has been viewed as an adequate representation of demand to account for undeclared transactions. Actual demand is less if forward transactions are not included.

Figure 2 Potential demand for REDD+ VERs versus supply to 2020. Current demand gap is likely to widen considerably unless new sources of demand are created. Source: FCMC, "Emerging Compliance Markers for REDD+: An Assessment of Supply and Demand"



Indeed, even within the current voluntary market, transactions of REDD credits have fallen repeatedly since 2010, decreasing by 65% to just 6.8MtC02e in 2012 [15]. This fall in demand has left project developers unable to sell the credits they intended with developers across the forest carbon market reporting in 2011 that they were unable to sell 32MtC02e – or 110% of the market value for that year[16].

A Market Lacking Exits?

Efforts are being made to increase demand through donor programmes and regional markets but these have been slow to establish, are focused primarily at regional or jurisdictional levels and in most cases are as yet unclear if REDD+ credits will be eligible. Even one of the most established mechanisms, the FCPF's Carbon Fund is unlikely to start purchasing credits until at least 2015 and only one currently registered VCS REDD project falls within one of the jurisdictions proposed to the FCPF as an investment- doing little to help the broader market. In addition to the geographical mismatch, although multilateral REDD+ funds such as the World Bank's FCPF Carbon Fund and Forest Investment Program have raised close to a billion dollars over the last five years, to date less than 1% of this has been disbursed due to institutional complexities and the newness of REDD+ investments[17].

Even when such mechanisms are included the potential market imbalances remain, as highlighted in a recent study of potential supply and demand until 2020[18]. This assessment included potential sources of demand but also looked more widely at REDD+ projects registered with other certification schemes, as well as those under development, and the potential for these projects to release backdated credits into the market. While identifying the potential for equilibrium between supply and demand in 2016, the figures also highlighted the potential for oversupply to reach levels of over 55MtCO2 per annum as early as 2013/14.

VCS REDD	FCPF CF
Belize	Chile
Brazil	Costa Rica
Cambodia	Ethiopia
Peru	Mexico
Kenya	Ghana
Zimbabwe	Rep of Congo
Indonesia	Nepal
DRC	Indonesia
	DRC

Figure 3. Not a perfect match: countries with most VCS REDD project supply vs potential FCPF Carbon Fund pilot investment countries.

> *'There is currently significant concern about oversupply in the market. Should project developers not be able to find buyers for their credits it would be a major body-blow to the market."*
> ***Chris Webb** - Assistant Director Sustainability and Climate Change, PWC*

Although jurisdictional approaches to REDD+ remain a key objective in the development of long-term strategies to address the drivers of deforestation, site-based projects are an important stepping stone to achieving this goal. Projects provide a tangible demonstration of the approaches and mechanisms that can be realistically adopted to effectively reduce deforestation on the ground, providing a platform for success that can be gradually scaled up to

[15] Levels of emission reductions transacted within the voluntary markets are in excess of current levels of emission reductions delivered. This is because transactions are made for credits that will be issued as part of long term financing. A small number of transactions are also secondary transactions.

[16] Peters-Stanley M, Hamilton K, and Yin D (2012) Leveraging the Landscape: State of the Forest Carbon Market. Available at http://www.forest-trends.org/publication_details.php?publicationID=3242

[17] Climate Investment Funds website. www.climateinvestmentfunds.org/cif/measuring-results

[18] FCMC "Emerging Compliance Markers for REDD+: An Assessment of Supply and Demand" March 2013. www.fcmcglobal.org/documents/Emerging_Compliance.pdf

encompass the adoption of strategies that operate at a broader socioeconomic and political level. Vital lessons can be learned from these initiatives and much progress can be made in pursuing the transition towards jurisdictional REDD+ frameworks by ensuring that project-level activities are able to thrive, thereby demonstrating their credibility as effective contributors in the safeguarding of a country's forests.

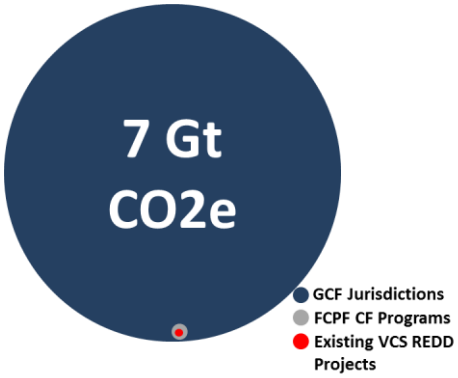


Figure 4 Comparison of potential REDD+ Jurisdictional supply to 2020, including Governors' Climate and Forests Taskforce jurisdictions, Early Idea Notes submitted by various countries to the FCPF Carbon Fund, and existing VCS REDD projects[19].

'It is a great mistake to assume deforestation is under control in the Brazilian Amazon. There was a strong perception that REDD+ would provide continued finance for forest conservation which supported action, and now that there is a real risk of no financing from REDD+ at the scale needed, deforestation is rising again."
***Mariano Cenamo** - Senior Researcher and Deputy Executive Secretary IDESAM - Institute for Conservation and Sustainable Development of Amazonas*

'The communities we work with are enthusiastic about REDD+ and the potential benefits but they are also cautious. They have seen many short-lived development projects come and go and think REDD+ will do the same. To make real changes they need to be confident on what the future will hold '
***Steve Ball** – Chief Technical Adviser*
Mpingo Conservation & Development Initiative

All the Wrong Signals

Taking early actions on REDD+ represented a significant commitment by tropical country governments and communities as well as the international NGOs and private sector groups that have supported them.

National governments have sought to address many of the most significant political and economic challenges facing forest protection while reorganising and refocusing ministries and agencies. The pilot projects they have worked with are most commonly seen as a way of testing the future of a REDD+ mechanism and a way in which forestry and environment related ministries can demonstrate the potential for financial return from REDD+.

At the site level communities have taken measures to change their livelihood practices and have invested their time and resources with the expectation that future revenues from the sale of carbon credits will help to maintain these changes and justify the sacrifices they have often made.

A lack of demand for these credits would leave key decision makers with little evidence base on which to sustain reforms, while project developers would no longer be able to support the multiple benefits REDD+ has the potential to deliver,[20] and leaving vulnerable communities with nothing to show for the time and resources invested in projects. Should projects start to fail at any significant scale it is

[19] The GCF is composed of representatives from 16 states and provinces of Brazil, Indonesia, Mexico, Nigeria, Peru, and the United States, including 14 states and provinces located in tropical forest nations that are developing jurisdiction-wide REDD+ programs capable of coming into alignment with California's new statewide GHG cap-and-trade program and other emerging market and nonmarket opportunities. GCF figures come from *Overview of Subnational Programs to Reduce Emissions from Deforestation and Forest Degradation (REDD) as Part of the Governors' Climate and Forests Task Force*. EPRI, 2012.
http://www.gcftaskforce.org/documents/EPRI.pdf

[20] Many offset projects developed with a view to sales within the carbon markets have a primary income that is not carbon related, such as sale of electricity from wind farms, which makes a fall in the carbon price less catastrophic to their business model as they have the potential to sustain operating costs while waiting for the price to rebound. Most REDD+ projects do not have this opportunity.

likely to have both direct and knock on effects to efforts to reduce levels of deforestation and degradation and indeed mitigate climate change. These impacts include:

- **Immediate deforestation**. At its most fundamental level, forest currently protected by REDD+ activities (in excess of 14 million ha) will be immediately subjected to the deforestation pressures which the projects were intended to mitigate. Without evidence of financial commitment or sufficient operational periods to complete transitions to alternative livelihoods or economic approaches, these areas of forest could rapidly disappear [21]. Regardless of the role of REDD+ as a mechanism the loss of support to existing projects would thus have a direct effect on levels of deforestation.

> *'If the price for REDD+ credits declines we have to cut back our programmes. The reality of this will mean a reduction in the level of benefits that communities get"*
> ***Christian Dannecker** – Director of Forestry, South Pole Carbon Asset Management Ltd*

- **Loss of skills and experience.** Donor funding and early market signals led to a rapid growth in the human and technical capacity for REDD+ at both the international and local level. We now know much more about deforestation trends, and the complex issues surrounding it, than just a few years ago. Should the market signals on the future of REDD+ weaken, the knowledge and experience base will move elsewhere with both individual and institutional capacity disbanding. Reenergising and realigning such skills to any future mechanism would require considerable time and further investment from donors.

- **Loss of political capital**. Developing countries, NGOs, communities and the private sector have invested time, energy, and political, social and financial capital in taking early action on REDD+. A collapse of these early initiatives would result in a significant loss of trust in the potential future of a REDD+ mechanism. Such a loss of confidence would make raising future financial capital challenging, while persuading national and local governments to commit to undertake REDD+ at the scale required to deliver transformational change would become almost impossible.

> *"What is holding back investors is that they don't know if they can make a return. If we want markets to provide incentives for REDD then we desperately need much stronger and reliable demand. Once you have that, everything else falls into place."*
> ***Johannes Ebeling** – Senior Manager BioCarbon Group*

What Can Be Done: Consolidate and Grow 2013-2020

The potential for REDD+ remains strong. Learning over the past decade has created a robust system of standards along with the individual and institutional capacity to develop and implement REDD+ activities. An initial supply chain of REDD+ emissions reductions and multiple social and environmental benefits has been established and must be sustained.

A failure to increase demand for REDD+ credits could result in the collapse of a number of high profile REDD+ projects while also limiting the success of many others. Such failures undermine trust in any future REDD+ mechanism, as well as existing initiatives for forest conservation and management. For this situation to be avoided further support is required to sustain project operations at subnational level while working to further integrate these activities into global efforts to scale up REDD+ activities to the jurisdictional level. For REDD+ to fulfil its promise it must attract financial flows from both the private sector and

[21] The nature of these challenges can be seen in Indonesia where a number of initiatives working at the project and provincial scale have struggled to maintain commitments to forest protection due to the extended periods of time it has taken to gain adequate financial support for the initiatives.

bilateral and multilateral development agencies in a way that has yet to be achieved.

In order to effectively "bridge the gap" to 2020, the stakeholders interviewed cited the need to provide near-term price support for existing REDD+ projects, including:

Advanced market commitments and increased ambition. Advanced Market Commitments (AMCs) and other incentive mechanisms are not uncommon and have been used by almost all developed countries to promote investment in clean technology and market areas of interest in the past[22]. They have also been discussed in the context of REDD+ by a number of donor governments including the UK which identified an AMC for verified emission reductions from forestry as a potential mechanism for use under the country's International Climate Fund [23]. Commitments to purchase high quality standardized REDD+ credits by donors countries would immediately help absorb some of the outstanding supply, even at low prices, and help bridge the financing gap for many projects. The private sector could support this initiative by increasing their ambition and focusing their voluntary offsetting activities around REDD+, thus leveraging public and private funding.

Expansion and Promotion of Risk Insurance Instruments. Existing instruments are offered by a host of development banks and organizations, including the Overseas Private Investment Corporation (OPIC), the World Bank Group's Multilateral Investment Guarantee Agency (MIGA), USAID's Development Credit Agency (DCA), amongst others. Traditionally focused on mitigating political and counterparty risk for investments or loans in developing countries, these mechanisms have been trying to expand to cover REDD+ market risk, yet uptake has been limited thus far. Increased risk appetite by these institutions and simplified contracts to reduce pure price risk for project developers would establish an effective "floor" until the broader REDD+ market is established.

Dedicated REDD+ project windows under existing climate funds. A number of existing climate funds, including REDD+ funds such as the FCPF, UNREDD, FIP, etc., could serve as potential offtakers for projects with hundreds of millions of dollars already pledged. Although currently none of these accept projects, dedicated funding windows focusing on purchasing (and retiring) high-quality VCUs from existing projects would serve to both support these pilots but also provide valuable lessons learned for these multilateral platforms.

Payment for performance based on the multiple benefits REDD+ projects provide. REDD+ projects have been successful in delivering a range of sustainable development and environmental outcomes, from improved health and livelihoods to the protection of critically endangered species. Existing and upcoming funds assigned to achieve similar outcomes need to look at REDD+ projects as a potential mechanism to deliver sustainable development results, thus moving away from "offsetting" and towards "paying for impact." In the case of REDD+ projects, this impact is quantified and independently verified through the use of standards, which should be attractive to a number of potential buyers, including major private sector groups such as the Consumer Goods Forum (whose combined revenues are worth $3trillion annually) and whom have pledged to achieve zero net deforestation by 2020[24].

[22] An outline of such examples with reference to forest finance is provided in Kanak D and Henderson I (2012) Closing the Gap: The Global Forest Finance Facility available at: http://www.theredddesk.org/sites/default/files/resources/pdf/2012/redd_discussion_paper-final-pdf.pdf

[23] UK Government (2013) Forests and climate change: Discussion paper on a proposed new set of UK interventions to tackle deforestation. Available at http://tinyurl.com/bf2n3od

[24] Under the Consumer Goods Forum's Sustainability Resolutions agreed in 2010. For more information see http://www.theconsumergoodsforum.com/sustainability.asp

'We need to make sure that any pledges to remove deforestation from supply chains are also paired with commitments and incentives to make sure that those same forests are protected. The only way to do this is by offering a visible price signal for intact forests and REDD+ projects are one way of doing that'

***Christian del Valle** – Managing Partner, Althelia Climate Fund*

How much will it Cost?

Current estimates of REDD+ market demand and supply provide an initial indication of the scale required from any immediate mechanism. These put the gap between supply and demand at between 7 and 52 $MtCO_2e$ per year in 2013 and 2014. If REDD projects under the VCS alone are identified, the gap between existing demand in the voluntary carbon market and supply comes closer to 11 $MtCO_2e$ based only on annual emission reductions of future credits. Using the average price for forest carbon credits in 2012 of $6.2, this would imply that the total value required to support just VCS REDD projects to be close to $68million per annum if backdating is not allowed. Although these may be best case numbers, in reality most stakeholders interviewed agreed that a comparatively small sum of guaranteed offtake – around $100 million – would be enough to place an effective floor in the market and provide price support for existing qualifying projects.

When should it happen?

Market oversupply of REDD+ credits within the voluntary carbon market is already happening with prices falling by close to 30% in 2011-12 per tonne CO_2e. This trend is likely to worsen as the number of projects verifying credits increases and the potential for backdating of supply enlarges. Such a situation could easily force prices down below sustainable levels within one to two years. Such increases in supply will also coincide with a period of uncertainty for private sector actors and donors as negotiations in the run up to 2015 provide only limited indications of the future of any REDD+ mechanism under the UNFCCC, and indeed its role in regional trading mechanisms.

It is thus in the most immediate term – the next two to three years – that clear financial support for REDD+ projects is required. Failure to provide support within this window could result in projects, and indeed the trust in any form of REDD+ mechanism, failing before any international agreement on REDD+ is even made.

Looking to the Future – A Question of Scale

REDD+ is currently at a crossroads. Early demonstration activities have provided evidence that not only can emission reductions be achieved and accounted for, but they can also be effectively linked to multiple environmental and social benefits. The question of scale still persists, however, and while emission reductions generated from voluntary REDD+ projects send a positive signal, they remain tiny in comparison to the scale required to accomplish global targets of a 50% reduction in deforestation.

As forests continue to be cut down across the globe, the urgency for these mechanisms to be established cannot be understated. To achieve the impact required it is clear that actions on REDD+ must be scaled up to jurisdictional, and eventual national levels and linked not only to performance-based payments but also to mechanisms to address demand for commodities and products driving deforestation. They must however be done carefully to prevent the creation of perverse incentives or other negative impacts. Existing pilot projects have done a lot to demonstrate the potential to effectively address drivers of deforestation and set up the institutional frameworks needed to manage implementation at a local level whilst feeding into the development of emerging national and international REDD+ mechanisms.

Maintaining a commitment to finance these successes will solidify their long-term impact by helping to build the trust at a national level that delivery of high quality results, both in terms of emission reductions and environmental and social benefits, will result in sustainable and predictable financing flows. If this trust is built and maintained

there is the potential for enduring and large-scale initiatives to develop and deliver transformational change within the forest sector, and to improve local people's lives for the better. If this trust is broken at the first hurdle by allowing projects to fail just as they are beginning to demonstrate their success, it becomes hard to imagine how much larger initiatives will be financed, and how that trust would ever be rebuilt.

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CONSERVATION INTERNATIONAL

conservation.org

2011 Crystal Drive
Suite 500
Arlington, VA 22202 USA
+1.703.341-2400

Contact:
Conservation International
Carbon Fund
+1703.341.2400
as@conservation.org