

## SUMMARY OF THE PROJECT IN DESIGN \* (\*)

### Improving the climate resilience of micro, small and medium forestry, and agroforestry enterprises in Honduras

PITCH ELIGIBILITY DATE		COUNTRY(IES)
04/18/2022		Honduras
ALIGNED WITH COUNTRY STRATEGY?		
Yes		
PARTNER(S)		
Federation of Savings and Credit Cooperatives		
PRELIMINARY CLASSIFICATION ENVIRONMENTAL AND SOCIAL IMPACT		
FI-2 (**)		
TOTAL BUDGET	IDB Lab	LOCAL COUNTERPART AND COFINANCING
US 17,500,000	US 10,500,000	US 7,000,000
DESCRIPTION		

**The problem** The agricultural, forestry and fishing sector is vital to the Honduran economy. While overall the sector contributes to 12% to the Gross Domestic Product (GDP) (WB, 2020), employs to 35% of the economically active population, and represents the 36% of total exports (IADB, 2019), the forestry sub-sector contributes to 3% of the GDP specifically (Benitez y Valdez, 2002). In Honduras, each job generated in the forestry sector provides up to 1.32 indirect jobs, and each dollar of income for direct employees generates up to an additional US \$ 1.25 of labour income in other sectors (Li et al., 2019). In fact, Honduras is considered a country with a forestry vocation. Currently, 56% of the territory is covered by forests, that is, 5,398,324 hectares (Government of Honduras, 2021). But, despite the economic relevance of both forestry and agroforestry activities, they are highly extensive. Around 1.19 million hectares of forest cover (approximately 20% of the total) were lost in the period 2001-2020, with deforestation being the main cause (WRI, 2021). Likewise, the bark beetle infestation caused a pine forest loss of 500,000 hectares between 2016 and 2017 (CIF, 2017)

Additionally, the forestry and agroforestry systems in Honduras, contribute to 46% of the country's GHGs emissions. Honduras is also highly vulnerable to climate change. Globally, it was the second country most affected by extreme weather events in the period 1998-2017 (Eckstein, 2018), and the most affected in the period 1996-2015 according to the 2015 Global Climate Risk Index from Germanwatch. At the regional level, its vulnerability is consistent with that of the Mesoamerican Dry Corridor (CIF, 2017). As a result, the importance of the forestry sector and agroforestry activities for the country's climate action is highlighted in the Update of Honduras' Nationally Determined Contribution (NDC) to the Paris Climate Agreement, presented in 2021.

Climate events present specific challenges for small producers who lack the technical skill and financial resources to implement measures to mitigate or adapt to these effects. But climate vulnerability is accompanied by social vulnerability. Nearly 66% of the Honduran population lives in poverty, and in rural areas where agricultural activities take mostly place, approximately 20% of the population lives in extreme poverty. In fact, Honduras is among the most unequal countries in the world (IADB, 2019).

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\*\*The IDB categorizes all projects into one of six E/S impact categories. Category A projects are those with the most significant and mostly permanent E/S impacts, category B those that cause mostly local and short-term impacts, and category C those with minimal or no negative impacts. A fourth category, FI-1 (high risk) Financial Intermediary (FI)'s portfolio includes exposure to business activities with potential significant adverse environmental or social risks or impacts that are diverse, mostly irreversible or unprecedented, FI-2 (medium risk) FI's portfolio consists of business activities that have potential limited adverse environmental or social risks or impacts, FI-3 (low risk) FI's portfolio consists of financial exposure to business activities that predominantly have minimal or no adverse environmental and social impacts.

Being Honduras among the most vulnerable countries, and the forestry, agricultural and fishing sector among the most vulnerable sectors in its economy; promoting agricultural intensification through sustainable land and forest management that increase productivity and generate a sustained source of income for small farmers is a priority to overcome the poverty trap in the rural sector.

But promoting sustainable land and forest management requires attuned financing and technical support, and farmers and small-scale producers (MSMEs) are often not eligible for credit due to their informality, lack of collateral and income uncertainty and repayment capacity due to commodity prices fluctuations and currency devaluation. Given this risk profile, only a few financial intermediaries seek to provide financial and non-financial services to the forestry and agroforestry sectors. In fact, only 4.7% of the total credit available in the Honduran financial system is estimated to be directed to the agricultural sector (IICA – CEPAL, 2019). In addition, the technical assistance provided to these sectors is traditional and is carried out on an individual basis, which makes it very costly, unsustainable, and difficult to scale.

**The solution** The loans will channel financial services to forestry and agroforestry MSMEs. The participating financial institutions (FIs) include (i) second-tier institutions such as FACACH and FUNDER; and (ii) first-tier financial institutions such as banks, savings and credit cooperatives, anchor companies, rural banks, and agricultural cooperatives. The FIs shall prioritize sustainable land and forest management.

These institutions will be the main channels for the provision of financial services, thus democratizing the intermediation of resources. FIs will be able to offer both individual and associative financial products. The resources will be used mainly to finance: agricultural supplies, productive infrastructure, use of new technologies, and working capital. The latter will be aligned with those solutions that are aimed at the management of crop varieties tolerant to drought and climate variability, effective soil management practices, and agroforestry among others. The financial products to be offered will be tailored to the crop cycle, the needs of MSMEs, and independent producers. Potential sectors to be supported are cardamom, coffee, cocoa, and silvopastoral production systems, among others.

The innovation lies in the democratization of financial resources by reaching the beneficiaries of the last mile by promoting financing to MSMEs and small producers in sustainable forestry and agroforestry systems, sectors that have not been addressed due to their level of risk under the traditional financial system. This model proposes a strategic, comprehensive, and holistic approach that, on the one hand, will seek to increase the value of products, farmers' profitability, provide decent income to MSMEs and, on the other hand, improve resilience and contribute to the reduction of GHG emissions.

**The beneficiaries** Direct Beneficiaries: 3,000 MSMEs and small organized forestry and agroforestry farmers located in areas deemed critical for ecosystem services and climate action. The project will have the flexibility to intervene in other areas of critical importance, such as those at risk of land use change, or are important carbon stocks or reserve areas. Key beneficiaries will be MSMEs and small producers dedicated to forest management under concession schemes by the Honduran state, agroforestry systems, wood processors organized in cooperatives or individuals, cardamom, coffee, cocoa, livestock producers, among others, with at least 15 hectares of cultivation[9], silvopastoral production systems (to complement the sustainable livestock NAMA), who will have access to financial services (especially to credits in conditions that adapt in terms of terms and rates). These will also benefit community forestry and agroforestry development groups, which in addition to wood, work with other forest products, such as: honey, seed extraction, sweetgum resin and pine, which have specialized markets and which, in some cases, constitute, ancestral productive practices of indigenous and afro-descendant communities. Indirect Beneficiaries: 15,000 families that manage to improve their productivity and quality of life through access to financing and business development services, which represent the workforce of agroforestry enterprises in Honduras.

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The project will have an emphasis in addressing the gender gap. In Honduras, there is a gender gap of the employment in the agriculture sector that is due to gender roles: while women's employment in agriculture accounts for 8.3% of their total employment, this figure is 42.3% for men. Although there are no restrictions for women to have access to land, there are still restrictions for them to acquire ownership or legalization; in other words, there is a patriarchal culture that makes men make decisions regarding land.

Hence, the project will define specific targets on women participation that will be achieved through gender considerations in the implementation of the proposed activities. Similar efforts will be made to guarantee indigenous peoples' participation.

**The partner** The Federation of Saving and Credit Cooperatives (FACACH), the Foundation for Agricultural Development (FUNDER), banking institutions, or anchor companies will provide loans. To this end, potential partners will be assessed based on eligibility criteria, and will be subject to a capacity analysis and due diligence, at which point the project team will be able to reconfirm the selection of a maximum of three financial institutions.

The selected institutions must have a specialized technical unit to carry out the corresponding credit and risk analysis and present it to the investment committee (IC), which will be responsible for approving all loan operations. This IC will be composed of representatives of the financial institution intermediating the resources.

**The IDB Lab's contribution** IDB-Lab, through a facility, will leverage a total amount of US\$500,000 is non-reimbursable TC, in addition to the US\$10 million loan resources to provide financing to the forestry and agroforestry sector through a group of financial institutions.

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