Blended Conservation Finance Reference Guide

A step-by-step guide to help you blend income from different sources into one conservation project

Photo A Ruzicka

THE CONSERVATION FINANCE INTENSIVE

TRUST FOR NATURE
Habitat forever

alca
Australian Land Conservation Alliance

Contents

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Purpose and primary audience

The primary purpose of this Guide is to help Australia's conservation sector bring a broader range of funding to land conservation projects. Specifically, the Guide is designed to provide readers with an easy to understand and practical explanation of key conservation finance terms, approaches and structures. It also has a focus on how to blend income from different sources into one project.

The intended audience of this Guide is land conservation project developers - particularly Australian not-for-profit organisations - who are interested in finding funding for their work beyond traditional government and philanthropic grants, but who have limited skills and knowledge to do so.

The Guide is structured to provide readers:

1. With an introduction to blended conservation finance;
2. A process for working through the conservation project development cycle (from concept to investment pitching phase); and,
3. Tricks, tips and checklists for developing and pitching a blended finance model.

Limitations of this Guide

The intention of this Guide is not to provide a templated solution for conservation organisations to fund their projects, but rather to help them understand the opportunities and process for developing projects that could tap into non-traditional funding sources or bring existing funding sources together in different ways.

While the guide outlines principles and processes for developing a blended conservation finance model, it is useful to seek expert advice on the feasibility of the proposed approach (including market appetite). As you work through this Guide, if you find yourself out of your depth at any stage, it may be time to ask an intermediary for help – that is, an entity or person (e.g. bank or advisor) that can work between a project developer and investors to help you.

Background

In October 2018, Trust for Nature (Victoria) on behalf of the Australian Land Conservation Alliance (ALCA) published a Scoping Paper which provided a high-level review of international and domestic finance approaches which may fund the restoration, conservation and management of Australia's environmental assets[1]. The Scoping Paper found that conservation and sustainable land management orientated finance was growing rapidly and identified at least 25 major finance models and approaches around the world – spanning philanthropic giving, government financing and private sector investment (and including carbon farming) – which were assessed as to their relative deployment complexity, scalability and local suitability to Australia.

[1] Available here: https://www.trustfornature.org.au/publications/conservation-finance-scoping-paper-2018

Following the release of the Scoping Paper, on behalf of ALCA, Trust for Nature (Victoria) hosted the inaugural Conservation Finance Intensive in November 2018. This two-day event was supported by the Australian Government Department of Environment and Energy, the NSW Government's Biodiversity Conservation Trust; the Victorian Government's Department of Environment, Land, Water and Planning; and, the National Australia Bank. Attendees came from almost all states and territories, and those from the private sector represented industries including sustainable farming, carbon markets, and biodiversity offsetting.

A key discussion point of the 2018 Conservation Finance Intensive was the need to educate Australian conservation professionals on financial concepts and models that extend beyond traditional philanthropic and government grant funding.

Concepts such as the difference between debt and equity, the concept of capital, operational expenditure and cashflow analysis, and how **blended finance** deals can be structured and pitched to investors.

This Guide attempts to help bridge this gap in knowledge on blended finance, which is the use of a mixture of public, philanthropic and/or private investment to fund a conservation project.

Conservation finance 101

Throughout this Guide you will see the icon next to important conservation finance terms – if viewing digitally, click on this to be taken to the glossary at the end of this Guide for more information.

What is conservation finance?

Good question. "Conservation finance" can be defined as the process of raising, harnessing and maintaining funding to support the protection, conservation, restoration and management of landscapes, ecosystems and ecosystem services, and the species which they support. Broadly, there are two categories of conservation finance: **direct finance** - such as support to permanently protect critical habitat of a threatened species – and **indirect finance** – such as investment in improved farm practices that benefit an adjacent waterway. "Direct financing" essentially describes projects where the predominant intent of a project is to gain a conservation outcome. "Indirect financing" describes projects where the primary intent of a project is unrelated to conservation, but a conservation outcome occurs. Likewise, socially-orientated financing, or funding with blended social, climate and/or conservation goals, such as the Aboriginal Carbon Fund's Reducing Carbon Building Communities Fund, or land purchased by the Indigenous Land Corporation, can provide indirect benefits for conservation, and effectively increase conservation financing flows.

Vast amounts of private-sector finance are currently being mobilised to support climate change mitigation and sustainable land management impact investing, as is demonstrated by the rapid increase in carbon farming, organic farming and Forest Stewardship Council-certified agricultural and forests land in Australia.

These finance flows typically target objectives other than conservation (e.g. climate mitigation, human health and economic benefits from lower fertiliser and pesticide use), but if conservation-orientated objectives and metrics are also considered, these types of funding can meet social, economic and environmental (or "triple-bottom line") objectives. These two categories (direct and indirect financing of conservation) encompass various **sources** of conservation finance (philanthropic, public-sector, private sector) and various **approaches and instruments** to conservation finance, such as loans, grants or payments for services.

The key challenges for attracting private-sector based conservation finance

Conservation organisations generally know how to apply for a government or philanthropic grant. However few know how to access private funding to support their work. Equally they may not know how to maximise government or philanthropic funding by blending different types of funding together in one project, with or without private investment.

Unlike the government or most philanthropic funders, typical private investors look for a financial return on their investment. That is, they typically want their money back, plus a profit of some sort. Therefore, the single most challenging aspect of accessing private sector support for conservation is to identify conservation projects that can generate an acceptable financial return – which is referred to as **return on investment** - this is explained later in this guide.

Many conservation-focused projects – notably the conservation of remnant habitat – are unable to generate a financial return. While there are exceptions, and the evidence base continues to build linking conservation outcomes with improved land ecological health leading to higher productivity, the fact that conservation is generally not a profit-making enterprise should not be overlooked. By contrast, sustainable land management projects (indirectly financing conservation) *can* generate a return.

Where there is potential for a financial return, there are four main challenges to attracting private investment in projects that create a conservation benefit:

i. **Generating an acceptable cashflow.** In the case of sustainable land management and conservation, many projects only start generating cashflows after several years of investment.

ii. **The unpredictability and inherent complexity of ecological systems.** - It can be challenging to predict conservation outcomes from managing an ecological system in a particular way, even with robust scientific knowledge.

iii. **Conservation and sustainable land management projects being complex**, particularly regarding governance, marketability and defining objectives, often requiring expertise in ecology, economics, project management, law and public policy. It is necessary to simplify many complex subjects in an easily digestible way for the investment community to understand.

iv. **Conservation and sustainable land management projects may also generate increased risks**, such as potential conflicts of interest between multiple

stakeholder groups, and regulatory risk. The bottom line is - investors don't like uncertainty, especially where small projects are concerned. Conservation and sustainable land management projects create a lot of risk in this respect.

It's not just about financial returns for private investors

Notwithstanding these challenges, Australia has a growing number of "impact investors" – private investors who are looking to generate environmental and/or social returns alongside their financial returns. In alignment with global impact investment trends, some participants in Australia's $5 billion **impact investment** market may be willing to accept a comparatively lower financial return from a project if it also provides positive environmental benefits (e.g. climate change or biodiversity) and social benefits (e.g. cultural heritage) that are measurable and verifiable.

Standardised frameworks exist to measure, verify and certify the environmental benefits of goods and services, providing third-party assurance of claims so producers can reduce reputational risk, access new markets and (ideally) gain a green price premium. Independent certification standards exist for forestry (e.g. Forestry Stewardship Council) and marine (Marine Stewardship Council) products in Australia, while emerging certification standards like those from the Savoy Institute for regenerative farming practices are gaining popularity at a global level. Additionally, new accounting standards, such as Accounting for Nature[2], and those being developed by the Australian Government to meet International UN standards are emerging to fill this need. However, such standards and practices remain largely immature and subject to variable take-up by sector participants.

Investments that reduce harm to (or improve) the environment can lower risk

In addition to verifiable environmental benefits, investors are increasingly sensitive to the **risks** associated with projects that degrade environmental assets. For example, such criteria may include a bank not investing in a project that has a risk to an endangered species. This is being reflected in assessments by **Credit Rating Agencies** (e.g. Moody's and S&P), statements by regulators (e.g. the Australian Prudential Regulation Authority), powerful investor disclosure initiatives (e.g. CDP), and ultimately, in higher insurance premiums.

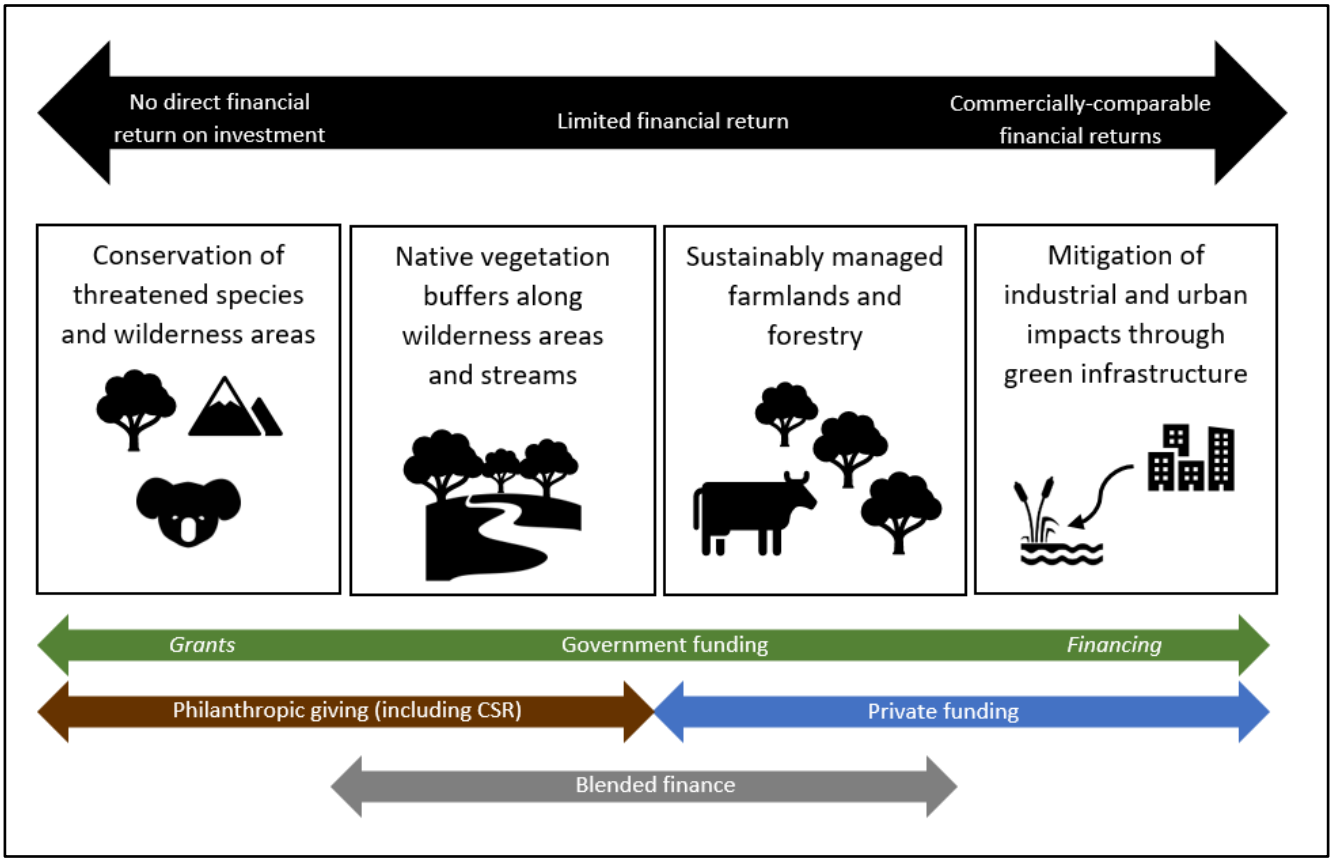
[2] Available here: https://wentworthgroup.org/2016/12/accounting-for-nature-2016/2016/

Which funding for which projects? The Conservation Finance Spectrum

Conservation finance can be represented across a spectrum, from the supply of funding with no expectation of repayment, let alone an acceptable return on investment (such as a government grant), to the payback of an investment with a minimal financial return or even a commercially-comparable financial return.

Figure 1 below illustrates this spectrum and tries to highlight that positive returns on investment are typically found where revenue can be generated through the sale of products and services (such as sustainably managed farmlands and forestry) and/or where government legislation creates a market for ecosystem service (e.g. carbon markets and biodiversity offsets). Conventionally, the conservation of threatened species and wilderness areas, and restoration of riverbank vegetation, does not generate a financial return, and so has been reliant on government grants and philanthropic donations.

Figure 1. The Conservation Finance Spectrum



Mixing and matching finance

Blended finance?

Blended finance uses a **mix of public, philanthropic and/or private investment.** The term does not refer to any particular blend of finance approaches, but rather where different finances have been blended together to support a project. Blended finance can occur at both the project and broader fund levels and can be used to mobilise private capital and increase finance for private sector activities. This Guide can be used for all blended finance projects but is particularly focused on how conservation organisations can attract private sector investment to support their work.

How blended finance can be a powerful tool to unlock private sector investment

Philanthropic, government and private sector finance suit discrete types of conservation and sustainable land management, depending on the returns provided. Together, they can be a potent mix that can fund a broad spectrum of projects with different returns. In this sense, blended finance can be used to create a wider conservation finance shift away from full reliance upon public entities, philanthropists and other grant giving organisations.

If a project can become self-sustaining, at least to some degree (e.g. the income generated by the project covers a material proportion of its expenses), conservation organisations can reduce some uncertainty associated with relying on ongoing philanthropic and public funding year-to-year. There will be some types of projects that will always rely on grant funding, but even partial private support of a project that was previously entirely supported by philanthropic or public funding will free up that philanthropic or public funding for other worthy projects.

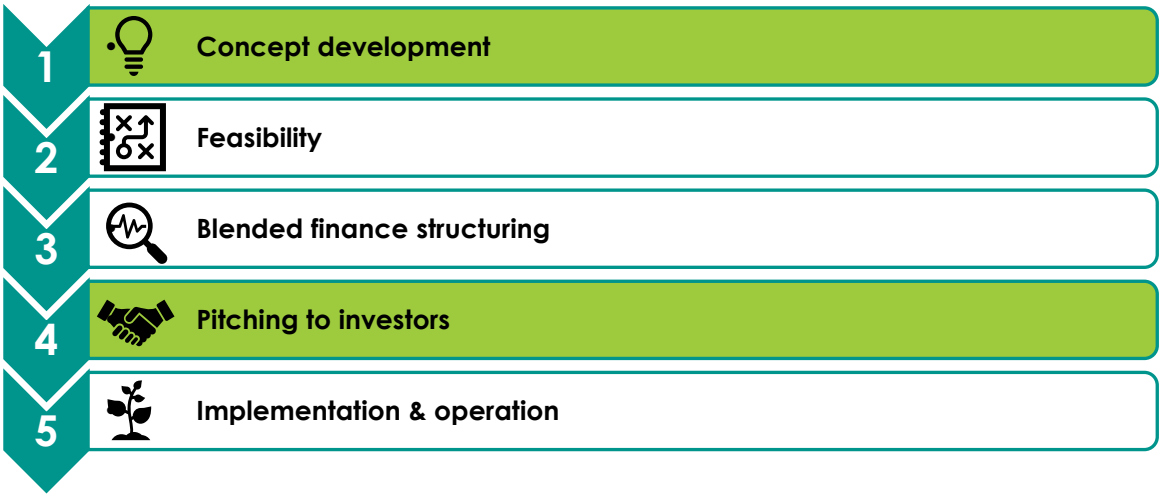
This separation of finance sources for the same project helps offer different levels of risk and financial returns that fit private investors' expectations, making it possible to raise funding for projects whose overall **risk-return profiles** might otherwise hold little appeal.

Project development & financing process

This Guide provides the key steps for developing a blended conservation finance model by adapting a standard project development process. Building a model in-line with the five project development phases below will assist in systematically developing a robust business case that can be confidently pitched to investors and for ensuring the greatest chance of securing a blended finance deal.

Figure 2 provides an overview of the five phases of our adapted project development process. The two key phases where project developers will need to obtain finance are highlighted in green. In the first instance, developers will often need to obtain finance to design and develop their concept further. Then later, the project developers will need to make another much more substantial pitch for finance in order to actually implement and operate the project – before it is capable of generating revenue to pay back investors.

Figure 2. Phases of the project development process



The following sections of this Guide provide more detail on what questions and information gaps need to be addressed at each phase of the project development process, with the intent of progressively building a strong business case/model and associated documents to pitch to prospective investors.

It is important to note that while this Guide presents a linear project development process, the reality of project development can be quite different. It can involve multiple iterations of a project that touch upon many or all stages of the process at different times. Project development is rarely, if ever, linear, but conceptualising it in a traditional project management framework is useful for articulating and explaining the key aspects that most projects will need to address at some point in their development.

Phase 1 – Concept development

The **concept development phase** focuses on describing an "idea" for a project and the various options for its development – this is outlined for high-level discussion via a **Concept Note**. This document is usually brief, with a simple version including an introduction, background, proposed objectives and results and initial budget overview. It should be no more than 2-3 pages, unless the potential early-stage donor or investor has specific requirements. Additional information is usually attached as an appendix.

Is your project a good candidate for a blended conservation finance deal?

Good question. Getting at least an initial understanding of the types of conservation finance approaches that will likely suit your concept will help you further develop your business case. It also helps to eliminate those that will not be applicable now.

The first and most fundamental question is: would somebody benefit from, and pay you for, doing the proposed project?

For example

You want to protect a forest along a river containing habitat for a rare bird. Others who might benefit from the project and be willing to fully or partly pay for it may include:

- A government environmental agency seeking to protect that same rare bird;
- A water authority that supplies drinking water from the river;
- A farmer that relies on water from the river; and,
- A philanthropic trust focussed on protecting carbon stores in mature forests.

Building your concept might involve approaching some or all of these parties. As soon as you combine one or more sources, you've got a blended finance concept. If you tap into only one of these sources, it's a more traditional fee for service project (for the water authority or farmer) or grants-funded project (for the government environmental agency or philanthropic trust). Part of the benefit of a blended finance deal is that multiple parties' objectives can be achieved at once, without anyone having to pay for the full project cost. When thinking about whether your project is a candidate for blended finance structures, it helps to think if any of your work (whether by type or geographic area) achieves results that others see as valuable.

The second fundamental question is whether your project could generate a financial return for investors?

Put another way – this question seeks to establish whether revenue streams (e.g. from the sale of carbon and biodiversity credits, or green certified products such as timber) could cover part or all of the project cost, and/or with a return beyond the project cost. If it can generate a financial return beyond the project cost then the private sector may be interested in funding it (eg if the project cost $1m and the water authority was willing to pay $800,000 and the Government was willing to pay $300,000 then it has a $100,000 return). If it can't generate any financial return at all then it may simply be a candidate for governmental or philanthropic funding (or both).

Choosing suitable project partners

Conservation finance projects are often complex endeavours, requiring a diverse range of skills and experience in the realms of finance, economics, law and governance, public policy, science and project planning. Most NGOs in Australia and around the world have limited capacity in this regard, with many being strong on science, governance and public policy but weaker on economics and finance. This therefore requires (in many instances) project developers to partner with specialist organisations to not only deliver the project but also shore up confidence in potential investors that the project team has the right skills and experience to give the project every chance of success.

For example, investment firm Encourage Capital is working with Blue Forest Conservation and the World Resource Institute (WRI) to develop the Forest Resilience Bond – a public-private partnership that enables private capital to finance much-needed forest restoration across the western U.S, where investors provide upfront capital with public and private beneficiaries then making contracted payments based on the water, fire, and other benefits created by the restoration activities. As the financial intermediary, Encourage Capital is responsible for the fundraising, financial structuring, and execution of the Forest Resilience Bond. It has partnered with Blue Forest Conservation to deliver the project, the WRI to provide research support and the US Government to help facilitate licensing, the transfer of local knowledge, and human resource / technical support.

A letter of in-principle support (or potentially a more formal **Memorandum of Understanding** document) from potential project partners is a valuable document to have at this stage. Though generally not legally binding such a document provides an important signal to potential investors that the project is being seriously considered by partners and can help show that the developer is addressing how to plug the skills/knowledge gaps it needs to fill to get the project delivered successfully.

Have we got the right people driving the project?

Like having the right project partners on-board, having the right management team also provides confidence to potential investors. Conservation finance orientated investors seek to invest in management teams who are committed to the organisation's long-term objectives.

An experienced and stable management team should not only have extensive knowledge about conservation, finance and related sectors, but (importantly) be capable of successfully implementing a business plan and managing the organisation's future operations.

If your organisation is light on experience in these and associated critical areas, it should consider employing or bringing in the right expertise (for example, as an Advisory Board) that can complement your existing skills and to give prospective investors confidence.

If the skills and knowledge needed to deliver a project vastly exceeds your management team's experience and the core objectives of your organisation, then perhaps you may need to partner with suitable organisations (see above) to fill this need - or ask the hard question - is this concept beyond the capability of our organisation altogether?

"You are a bus driver. The bus, your company, is at a standstill, and it's your job to get it going. You must decide where you're going, how you're going to get there, and who's going with you.

Most people assume that great bus drivers (business leaders) start the journey by announcing where they're going i.e. setting a new direction or by articulating a fresh corporate vision.

In fact, leaders of companies that go from good to great start not with "where" but with "who." They start by getting the right people on the bus, the wrong people off the bus, and the right people in the right seats. The same applies to developing a conservation finance business or project".

Jim Collins, Author.

Where to go for initial funding to develop a robust investment proposal

Progressing past the concept phase and onto developing a full Feasibility Study, Business Plan and then Investment Memorandum (more on these later in the Guide) can be a time and resource consuming endeavour. Project developers should consider applying for some initial upfront funding to support this stage, as is outlined below in **Table 1**.

In addition, non-financial support in the form of **Technical Assistance** can be sourced from government, private and other non-government organisations to support you in developing a Concept – this includes feasibility studies. For example, Australia's state and federal governments have supported programs (often delivered by NGOs, natural resources management groups and private businesses such as the Carbon Market Institute) that provide technical training and assistance to market stakeholders, and particularly those participating in the Carbon Farming Initiative and the Emissions Reduction Fund. Such programs include the Australian Government's Carbon Farming Futures Extension and Outreach Program. There are numerous business incubators focused on developing social enterprises, as recently summarised by Australian Incubators & Accelerators for Social Impact. The Coalition for Private Investment in Conservation (CPIC) also provides a useful Accelerator Selection tool for many jurisdictions around the world, including Australia.

Table 1. Opportunities for funding the Concept to Feasibility phases of developing a blended conservation finance project

Cash donations from individuals	Where an individual donates money (with no expectation of return, potentially on a tax deductibility basis[3]) to a project developer, including via a crowd-funding campaign (for example).
Cash donations from corporates	Where a corporate entity donates money (with no expectation of return, potentially on a tax deductibility basis[3]) to a project developer, potentially as part of a Corporate Social Responsibility program.
In-kind assistance	Where a corporate entity or individual donates time and expertise (e.g. in investment structuring), but not cash, to a project developer as part of a Corporate Social Responsibility program. Also known as "sweat' equity.
Government grants	Conventional government grant funding provided to a project developer for building a business model and/or project plan (e.g. via start-up or innovation grants) which require no repayment.
Grants from foundations	Corporate (e.g. Myer Foundation) and philanthropic foundations (Ian Potter Foundation) also provide conventional grants to help with the start-up of businesses/projects, with no requirement to pay back.
Technical assistance	Government, private entities and NGOs support project developers in building professional networks and capacity to structure projects (e.g. The Difference Incubator). Includes training, workshops, networking and business incubators.
Private sector finance	Angel investors ("seed funders") may provide funding during the early project development phases where there is less certainty if the project will succeed. To compensate them for their risk taking, they may be offered a high financial return once the project becomes operational.

[3] If the project developer has Deductible Gift Recipient (DGR) status

SUMMARY: Phase 1- Concept Development

The key question to answer by the end of this Phase:

First and foremost, the key question is, *would somebody benefit from, and pay you for, doing the proposed project? The second key question is whether (or not) the project can actually generate a return?*

Answering these questions at the initial Phase of project development is often tough – it can require deep understanding (and instinct) of government policies, market trends, business capacity and ecosystem dynamics and complexities.

If the answer to this question is "no" or "not sure", then the project developer should consider setting the idea aside, defining it as only suitable for grant funding, or engaging a suitably experienced and skilled third-party to assist in assessing, developing and/or redeveloping the concept.

Other questions that should be answered by the end of this Phase include:

- ☐ Are the potential benefits of the project "bankable" i.e. is there real market for buying these on a per unit basis (e.g. carbon offsets, water quality credits), either from the private sector or government?
- ☐ Could the project realistically provide a financial return for investors?
- ☐ What might be some significant risks that might stop the project delivering financial and environmental returns?
- ☐ Can you potentially measure and link your project objectives to an external framework (e.g. SDGs)?
- ☐ Is the above information clearly articulated/addressed in the Concept Note?
- ☐ Does this project fit with the core objectives of your business, or should you consider partnering with a third-party to develop and deliver it?
- ☐ Who are the right project partners? What about personnel?
- ☐ Do you need initial funding to proceed further? What are the potential options for obtaining this?

Checklist of important documentation to move to the next Phase

The Project Concept Note should aim to include (at least):

- ✓ A clear and concise concept overview that directly or indirectly has a net benefit for conservation.
- ✓ An overview of the potential market i.e. who (realistically) may be willing to pay for the goods (e.g. carbon) or services generated by the project.
- ✓ A high-level / indicative budget for the project.
- ✓ Letters of in-principle support from Project Partners or a MOU.

Phase 2 - Feasibility

If your Concept Note is supported by your organisation's Board and/or potential investors, it's time to move onto the feasibility phase which seeks to evaluate the project concept in more detail, including developing a **financial model** and **risk assessment**. This stage also involves looking at how to **track other project benefits** using frameworks such as environmental economic accounting.

Depending on the scale of the project, a **prefeasibility study** may be first used to undertake **due diligence work**, and determine whether to proceed with a more detailed **feasibility study**. A feasibility study is a more in-depth report that builds on the many of the same topics of the prefeasibility study. The feasibility study aims to be more accurate and therefore requires more resources to complete. Feasibility studies typically offer estimates within 10-20 percent accuracy, whereas prefeasibility studies are between 20 and 30 percent. Robust financial modelling adds credibility to any pitch for finance later in the process.

Developing a financial model

A **financial model** is a tool (often built in Microsoft Excel) to forecast a business' or project's financial performance into the future. This will be included in the prefeasibility and feasibility studies. The forecast is typically based on historical performance (e.g. historical biodiversity offset price), assumptions about the future (will these go up or down?), and requires preparing an income statement, balance sheet, cash flow statement and supporting schedules. Critically, it requires estimates for project costs and how revenue streams will pay these costs back. An example for a conservation finance project has been included in the **Appendices**.

A financial model is an essential element of any pitch to a potential investor. It takes years of experience to become an expert at building a financial model – so make sure whoever is building it for you knows what they are doing and understands the intricacies of the project they are modelling.

Identifying and estimating project costs

There are two types of project costs – capital expenditure and operating expenditure. You may hear investors using these terms to differentiate between categories of spending that you're asking them to invest in.

Capital expenditure (or "**CapEx**" refers to the purchase or upgrade an organisation's financially productive assets. In conservation finance, capital expenditures might include:

- Land acquisition;
- Equipment purchases;
- Building expansion and improvements;
- Hardware purchases, such as computers and drones; and,
- The purchase of company vehicles.

When the expense relates to an on-going and day-to-day item associated with running a business it is referred to as **operating expenditure (**or **"OpEx" ?)**. In conservation finance, operational expenditures might include:

- Staff salaries;
- Power and water use;
- Fertiliser use and seedling replacement costs;
- Fire and pest management;
- Government licenses; and,
- The running of company vehicles (e.g. fuel, servicing).

Cost estimating (as a part of a financial model) is one of the most important parts of a feasibility study as it establishes the baseline of the project's cost at different stages of the project. Cost estimation is a specialist job – if it's done poorly it could have major implications for the project developer, such as the financial model not being seen as credible or disgruntled investors if the project does not perform as modelled.

Identifying and estimating project revenue streams

Another key step in developing a financial model, estimating how much money will flow into the project (project revenue streams) is often one of the most difficult tasks when developing a conservation finance project. This is because revenue streams are often highly variable (e.g. carbon prices) or difficult to estimate in the first place (e.g. sales forecast for green products). A financial model can get especially complicated in this respect when multiple land uses are involved. Revenue streams are generally more visible and stronger with sustainable land management projects that indirectly support conservation projects, where they involve sales of goods (e.g. Forest Stewardship Council certified timber). Revenue streams from conservation finance projects typically include:

- Upfront provision of grants;
- The sale of carbon and other environmental credits (e.g. biodiversity offsets);
- The sale of green certified commodities e.g. Forest Stewardship Council certified timber, organic food;
- Revenue from leasing land e.g. for an ecotourism venture; and,
- Potentially, from government sources on meeting pre-defined performance benchmarks such as with respect to an Environmental Impact Bonds.

What's an acceptable return on investment (ROI)?

Return on investment ? (ROI) is a measure commonly used by investors to assess the benefit (i.e. **net profit** ?) or loss generated on an investment, relative to the amount of money (capital) that was invested in the first place. ROI is usually expressed as a percentage. For example, say $1 million in capital was invested to buy and restore an ecologically degraded farm, which was then sold for $1.1 million a year later – the ROI would be 10% per annum (ignoring anything spent in managing the farm for that year). Potential equity investors use ROI as a key measure (amongst others) to

compare different investment opportunities, be this sustainability/conservation related or in another sector (e.g. energy). ROI's on lower risk investments will typically be under 10% per annum (eg. Government bonds, bank deposits, investment grade debt), while higher risk investments offer the prospect of higher returns in exchange for bearing higher risks.

The whole idea of estimating project costs and revenue streams is to ascertain the return on investment for the project.

Depending on the project, ROI may refer to either annual anticipated income (e.g. a farm that sells produce and so generates money every year), or a profit anticipated at the end of the project (e.g. a conservation property that is sold for a higher price than it was purchased for). Different investors are interested in different types of returns. Some investors are most interested in receiving a stable annual income; others are willing to trade higher volatility or deferred returns for higher a ROI.

Undertaking a sensitivity analysis

A **sensitivity analysis** is often developed as a final step in this phase. The point of this analysis is to determine how much the ROI for the project will be impacted by changes in underlying assumptions. Such changes include (but are not limited to):

- Timing of cashflows;
- Interest rates on debt owed;
- Inflation and exchange rates;
- Fluctuations in the real estate market;
- Demand and prices for carbon and biodiversity offsets; and,
- Demand and prices for green certified goods.

Sensitivity analysis is a very useful tool for assessing the risk of an investment or for business planning purposes.

Assessing and managing project risk

Conservation projects often depend on scarce land or water resources, therefore, focusing on achieving conservation outcomes can be politically unpopular, as they can encumber land that might otherwise benefit the community (e.g. through food production), or generate less profit than other uses e.g. agriculture, resource extraction, or real-estate development. This type of community opposition creates political risk for the project.

Furthermore, if a conservation project depends on policy mechanisms such as a biodiversity offset regulatory system to generate revenue, the possibility that those policy mechanisms will change (as has often occurred in Australia) creates regulatory risk. Since many risks can affect blended conservation finance projects, developers must identify these comprehensively for prospective investors, which requires consultation with a range of stakeholders.

Table 2 provides an overview of the types of risks that blended conservation finance projects may be subject to and that need to be adequately identified during the feasibility phase.

Table 2. Risks for conservation projects and mitigation strategies

Type of risk	Questions to ask
Delivery (Performance) Risk: Whether the investment may fail to deliver the environmental good or service as expected	▪ Will conservation benefit be achieved, either directly or indirectly? ▪ Will the ecosystem service function as projected and in the forecasted timeframe? ▪ Will the goods and/or services be created, and valued by the market, as modelled? ▪ What internal factors might pose a risk for project delivery e.g. lack of adequate finance and human resource capacity and skills.
Market Risk: Whether the overall performance of a market will be negatively impacted	▪ Will the market be impacted by a shock to the system e.g. natural disaster (such as drought) or a higher interest rate? ▪ Will a buyer's or investor's participation be influenced by a recession?
Regulatory Risk: Whether policy changes will negatively impact the project or market	▪ Will regulatory changes affect the price for environmental credits or services? ▪ Will policies remain active, and be enforced? ▪ How significantly will a regulatory/ legal change effect who must purchase the outcomes of the project, or how many they are required to buy?
Political Risk: Whether community or political sentiment will negatively impact the project or market	▪ Will local communities object to the project? ▪ Will the project be unpopular with voters or politicians?

<u>Tracking other project benefits via environmental accounting</u>

In a market where "green claims" are becoming common, consumers and impact investors are demanding that environmental (and social) benefits be measured in a robust and verifiable way. Environmental accounting focuses on measuring the biophysical condition of an environmental asset e.g. rivers, soils, native vegetation, fauna. The information produced through environmental accounting can be an effective way to convey complex information to relevant managers and stakeholders and used in decision-making processes.

Investors, conservation managers, indigenous land managers, farmers and developers alike are beginning to utilise environmental accounting to improve the cost-effectiveness of their management practices and demonstrate the effectiveness of sustainability to shareholders, government agencies or finance institutions. These accounting processes may also assist in conducting environmental valuations and cost-benefit analyses, especially for finance institutions aiming to understand and limit their potential economic risks in a carbon and resource constrained world; therefore, potentially increasing their investment into environmental and conservation related activities.

Importantly for investors, an environmental condition accounting system for a conservation project can be used to support indicator reporting (via standardised and verified data provision) under finance-sector orientated impact measurement frameworks and international policy objectives, such as the IRIS Metrics and the UN Sustainable Development Goals (SDGs) respectively. Such systems are becoming more and more important for blended conservation finance projects, particularly for impact investors and governments who are increasingly trying to maximise not only financial returns, but also environmental and social benefits.

In 2018, an Australian Government stocktake found several different approaches to natural capital / environmental condition accounting in Australia[4]. You may consider adopting one of these approaches, or developing your own. The key thing is that you choose an approach which is **relevant to the reporting needs of investors**, and which allows **your project to be compared to others** with respect to environmental performance. In this respect, another important aspect for many investors is whether the approach can be independently certified against a standard.

SUMMARY: Phase 2 - Feasibility

Key questions to answer by the end of this Phase, as relevant to finance

- ☐ Have you developed a robust financial model, and identified project costs (capital and operational) and revenue streams?
- ☐ Have you done a sensitivity analysis to simulate the impact of different internal (e.g. wages) and external factors (interest rates) on the return on investment?
- ☐ How will the risk associated with the project be managed?
- ☐ Based on the financial model and risk assessments, do you have an attractive and resilient business model that provides an acceptable return on investment?
- ☐ Are you able to track other (non-financial) benefits of the project?
- ☐ What government licences are required to commence work? What other agreements (e.g. landholder access) are required?

Checklist of important documentation to move to the next Phase

Prefeasibility study, which aims to include:

- ✓ Detailed designs for the conservation project, including maps showing locations for environmental plantings versus sustainable agricultural zones (for example).
- ✓ An initial (project) finance model, showing upfront capital costs (e.g. purchase of a parcel of land), forecast revenues;
- ✓ A high-level assessment of delivery, market and political risks; and,
- ✓ A high-level framework for measuring and monitoring the project, including the condition of environment (if applicable).

An expanded full feasibility study, which should include:

- ✓ A detailed financial model (ideally that has been externally audited) with sensitivity analysis e.g. testing how different carbon prices and/or loan interest rates (etc) might impact the project's financial performance.
- ✓ Ideally, evidence of anticipated funding sources (e.g. Signed Forward Purchase Agreement documents for emissions reductions from a buyer).

[4] Australian Government, 2018. Environmental Economic Accounting: A common national approach. Strategy and Action Plan. Canberra.

Phase 3 – Blended finance structuring

The Blended Finance Structuring Phase seeks to bring together the detail generated from the Feasibility Phase (confirmed capital and operational costs, revenue streams, contracts, project team, timelines etc) into a full Business (Project) Plan that sets out a suitable blended financing structure and the associated investment opportunity. While the previous stages may have contemplated various types of finance structuring, this is where the proposed finance structure is settled.

Part A (blended finance approaches) of this section provides an overview of debt versus equity, as the two key finance pathways. It then looks at the scalability and timing for specific financing approaches (e.g. grants, environmental credits, green bonds) which could be in the blended finance mix.

Part B (blended finance structuring) is focused on the key elements required to structure a blended finance project, and how these are brought together/articulated in appropriate documentation. Part B begins by providing several examples of blended finance structures, then considers the use of credit enhancement tools to de-risk projects for investors. It goes on to outline project financing legal structures, before outlining governance considerations. It concludes by providing an overview for developing a business or project plan, Investment Memorandum and Shareholder Agreements – documents often used in the pitching phase.

Part A - Blended finance approaches

Debt versus Equity?

Often you will hear finance people refer to the provision of **debt** and **equity**. **Debt** is a loan. It is used by many corporations and individuals as a method of making large purchases that they could not afford otherwise. It's an arrangement where the borrowing party agrees to pay back the lender later, usually with interest. Banks are often a source of debt, for example in the form of a property loan (often secured by a mortgage), including for farms. To be successful in obtaining debt financing, a conservation finance project will be required to demonstrate that it has a relatively low **risk profile** – the better the business case and return on investment, the better chance of securing debt on favourable terms i.e. low interest rate.

Equity, on the other hand, essentially means taking some form of *ownership* in an investment. Equity investors share in the performance of a business or asset as owners (shareholders). The returns to equity investors are therefore contingent and there is no obligation to pay a return or even to repay capital. Owners may not only include the founder, but also **angel**, **institutional** and **retail**/**wholesale** investors. The offer of equity is different to an offer of debt in that it is usually provided knowing that the investment has more risk – that is, it has a higher chance of failing than debt. Equity providers therefore typically seek higher financial returns than those offering debt (loans) – i.e. they have a higher **risk-return profile**.

The raising of equity (capital) in Australia is regulated by the Corporations Act and depends upon the business structure that is used by project. It should also be noted that at some point in the project equity holders will want to get their money back out of the project, ideally with a return as well. Depending on the agreement made when they invested, if the project is unsuccessful, they may not be entitled to any/all of their original investment back.

Table 3. Advantages & disadvantages of debt and equity financing

	Debt	Equity
Advantages	• Loan size is flexible and can range from micro ($ '00's or '000's) to large scale ($'00's of millions to $'000's of millions) • Lenders usually have little or no governance role in the business, relationship with lender ends as soon as debt has been repaid.	• Does not divert capital from the business to repay debt • Investor shares in the risk along with the owner. • If the business fails, equity is subordinated to all debt and other liabilities. • The business may also benefit from guidance and access to the networks of its investors, or in some cases more hands on business management from experienced operators.
Disadvantages	• Businesses with limited cash flow may need to spend a sizable portion of their monthly revenues repaying the money they borrowed. • Debt must be repaid as per the repayment schedule, regardless of revenue, or how well a business is doing. Failure to repay loans on term can lead to a business being placed in administration or bankruptcy. • There are significant risks associated with guaranteeing a loan with collateral.	• Investors own a portion of the business, and will be due a portion of the profits. • An equity partner may expect a governance role associated with their equity (e.g. Board member). This can be an advantage or disadvantage depending on the value of their experience, effectiveness and alignment with the objectives of the existing management. • Business owners may have little control about when an investor decides to exit a business.

SOURCE: CPIC, 2018[5].

Investment risk changes investor expectations for ROI

As touched on above, the risk of a project failing can have significant bearing on the expected return. A high risk-return ratio is often a precondition for private sector investors providing equity, and not an opportunity banks will generally entertain via

[5] Conservation Investment Blueprints: A development guide. CPIC, 2018.

loans. Assessing the various forms of investment risk is a key **due diligence** activity part of structuring a conservation finance deal.

Concessional capital is also important and often features where the government or philanthropic investors accept a higher risk profile for the same or lower rate of return. Finance for technical assistance and concept-phase grants are not direct investments but improve a deal's chance of being **"bankable"** and achieving **financial close**.

Approaches suited to blended conservation finance

Trust for Nature (Victoria), on behalf of ALCA, and in collaboration with the Australian Government of the Environment and Energy and the US-based Conservation Finance Network (CFN), undertook a desktop review of both international and domestic finance approaches which may be deployed and/or expanded to support private land managers in restoring, conserving and managing Australia's landscapes, waterways and populations of threatened species.

All-in-all, 26 major finance approaches (**Table 4**) – spanning philanthropic giving, government financing and private investment - were assessed as to their relative deployment complexity, scalability and suitability in addressing Australia's conservation finance gap. These approaches include both financing approaches that directly benefit conservation and restoration (where conservation is the main objective), and those approaches that could indirectly benefit conservation on private land through sustainable land management practices (i.e. conservation is a secondary objective).

The analysis found that while government currently provides the dominant source of conservation financing to support Australia's natural environment, there are growing opportunities to use philanthropic and government sources to leverage private sector investment as part of a blended-finance approach. This is particularly the case where conservation indirectly benefits from impact investment in sustainable agricultural and forestland real-assets, or via urban green infrastructure and regional development funding.

The reason for this is that various international targets and agreements to which Australia is a party, such as the Sustainable Development Goals, the Convention on Biological Diversity, and international carbon targets such as those contained in the Paris Agreement, have spurred the private sector's interest in investing in social and environmental outcomes, alongside market returns. The business case for conservation has also been enhanced by Australia's strengthening brand as a global supplier of clean, healthy and sustainably grown food and fibre products, and of nature-based tourism opportunities.

Table 4. Approaches suitable for combining as part of a blended finance structure

Approach	Scalability	Ease of Deployment	Investor/donor type							
			Angel Investors	Wholesale & retail investors	Impact Investors	Institutional Investors	Government	Foundations	All types of business	Individuals
Donations by individuals	Moderate	Simple	-	-	-	-	-	-	-	Yes
Voluntary surcharges	Limited	Simple	-	-	-	-	Yes	-	Yes	No
Transfer fees	Limited	Moderate	-	Yes	Yes	Yes	Yes	-	Yes	Yes
Corp. Social Responsibility	Moderate	Simple	-	-	-	-	-	-	Yes	-
Corporate Cause Marketing	Limited	Simple	-	-	-	-	-	-	Yes	-
Grants	Moderate	Simple	-	-	-	-	Yes	Yes	-	Yes
Environmental Levies	Limited	Simple	-	-	-	-	Yes	-	-	-
Covenanted Land Tax Deductions	Moderate	Moderate	-	-	-	-	Yes	-	-	-
State Tax Concessions	Limited	Moderate	-	-	-	-	Yes	-	-	-
Municipal Tax Concessions	Limited	Simple	-	-	-	-	Yes	-	-	-
Bridge Finance	Moderate	Moderate	Yes	Yes	Yes	-	Yes	Yes	-	-
Revolving Land Fund	Moderate	Moderate	Yes	Yes	Yes	-	Yes	Yes	-	-
Seller Finance	Limited	Simple	-	-	-	-	Yes	-	Yes	-
Program related investment	Limited	Moderate	-	-	-	-	Yes	Yes	-	-
Environmental credit markets	High	Complex	Yes	Yes	Yes	Yes	Yes	-	-	-
Green bonds	High	Complex	Yes	Yes	Yes	Yes	Yes	-	-	-
Environmental impact bonds	High	Complex	Yes	Yes	Yes	Yes	Yes	-	-	-
Green product markets	Moderate	Moderate	Yes	Yes	Yes	Yes	Yes	-	Yes	-

How to read this table: Different approaches to conservation finance are provided in the first column. Next to each, its relative "scalability" (the potential size of the funding pool, compared to the other approaches listed), "ease of deployment" (how complex it would be to actually implement to achieve scale, compared to other approaches) and whether the approach is available to various investors or donors in the conservation finance spectrum. Definitions are contained in the glossary at the end of this Guide.

PART B - Blended finance structuring

Blended finance is a deal *structuring* approach, which can include two of more of the approaches as listed **Table 4**.

Blended finance is the use of catalytic capital from public or philanthropic sources to increase private sector investment in sustainable land management, including conservation. In a nutshell, a blended finance structure allows organizations with different objectives to invest alongside each other while achieving their own objectives (whether financial return, social impact, or a blend of both).

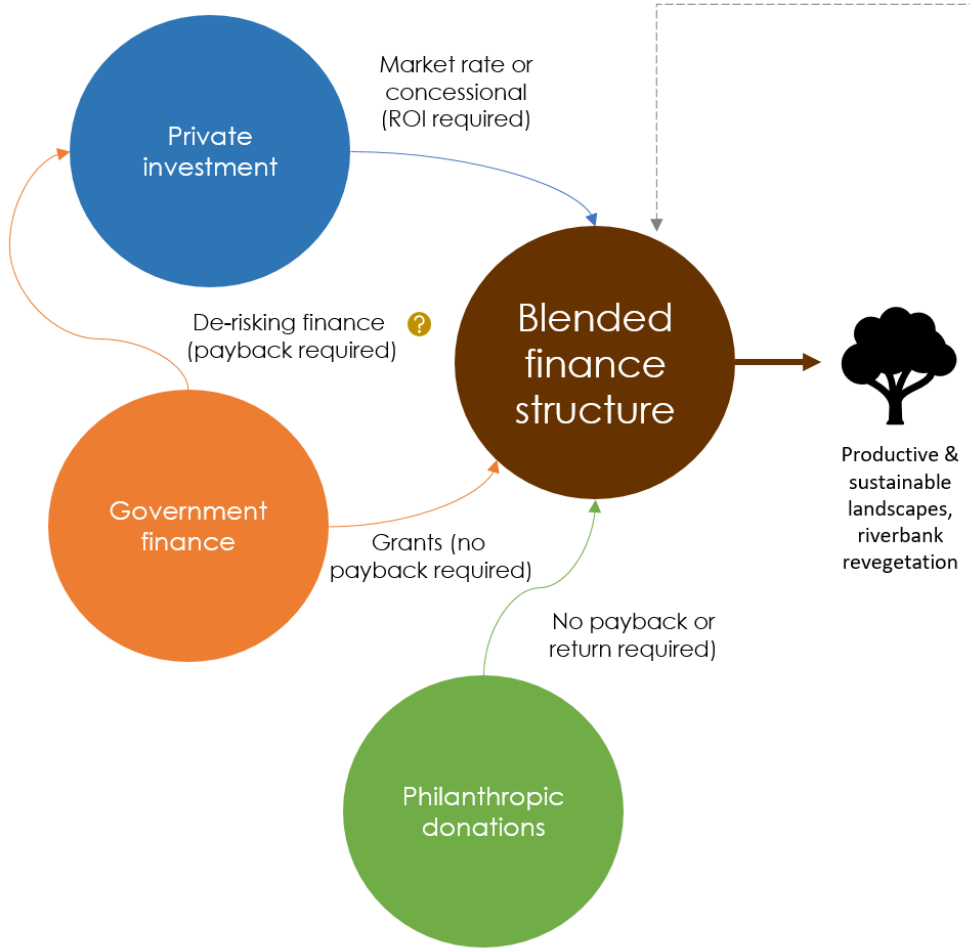
The three main investment barriers to conservation finance for private sector investors which are addressed using blended finance structures are (a) perceived high project risk, (b) below market returns for the high risk relative to other comparable investments and (c) lack of scale.

The finance approaches most commonly deployed in blended finance structures are concessional capital and technical assistance funds. Concessional capital is a wide-ranging category encompassing several forms of catalytic capital with the key characteristic being below-market finance to mobilize private sector investment e.g. repayable grants, first-loss capital, and concessional (low-interest) debt and equity. Technical assistance funds are deployed before and after investment occurs, often to improve the investment readiness of underdeveloped sectors or markets. Loan guarantees and/or insurance products (see credit enhancement tools in the following section) are growing in importance in helping to de-risk blended finance structures.

Four common blended finance structure examples can be found in **Figure 4**. These examples include:

i. Government or philanthropic investors provide funds at below market rates;
ii. Government or philanthropic investors provide loan guarantees or insurance products at below market rates (i.e. "**credit enhancement tools**", see following pages);
iii. A grant-funded technical assistance facility supports private sector investors to better understand and manage the complexities of ecological systems and new environmental markets; and,
iv. The design of conservation finance projects is grant funded.

Figure 4. Examples of blended finance structures



Adapted from: Convergence 2018

Example Blended Finance Structures

Private investment (debt or equity) combines with concessional government (e.g. first-loss capital facilities) and/or philanthropic funding to attract institutional investors.

Debt/equity
First-loss Capital Facility

Debt (e.g. concession loan) combines with loan guarantees or insurance products from government or philanthropic funders.

Loan guarantee
Debt
Equity

Grants from government or philanthropic funders helps build capacity (via a Technical Assistance facility) in private sector investors to achieve expected financial and environmental (and social) returns.

Debt
Equity
Technical assistance facility

Grants from government or philanthropic funders helps build the capacity of private sector investments to design or structure projects to attract institutional investors.

Grant
Debt
Equity

De-risking strategies for use in blended finance structures

As blended conservation finance projects are largely considered experimental by private sector investors – as there are relatively few – they are considered to carry more risk than more established transactional structures. Therefore, any strategies and tools that reduce this risk and uncertainty helps to make blended conservation finance projects more appealing to investors.

Credit enhancement tools are an important strategy to include in blended conservation finance structuring (given the relatively high-risk profile) and are often deployed to create an investment with acceptable risk-return profiles for the private sector through either "de-risking" the opportunity, or by improving the risk-return ratio.

Below (**Table 5**) are several **credit enhancement tools** which can assist project developers to attract investment that they could not otherwise access. Credit enhancement tools are especially critical at early stage project development, as market activity is particularly vulnerable to different sources of risk, including delivery risk, market risk, and policy risk.

Table 5. Credit enhancement tools

Catalytic first-loss capital	This can help to lower project risk by identifying an entity who will bear the first loss. The entity is often motivated by social and/or environmental outcomes or wants to demonstrate the commercial viability of investing into a new market. The capital is catalytic in that it enables the participation of investors that would otherwise not be able to participate. It includes instruments like grants, equity, and **subordinated debt**.
Letter of credit	A letter from a bank, foundation, or other entity that guarantees payment on behalf of a borrower up to a stated amount for a specific time
Loan guarantee	An agreement where the provider (e.g. government) takes responsibility for paying back a loan if the borrower cannot.
Over-collateralization	Where a borrower puts up more collateral (e.g. mortgage over land) than is necessary to secure financing. Assets are used to absorb losses if cash repayment falls through.
Insurance mechanisms	Any approach where the cost of potential loss is transferred to another entity in exchange for monetary compensation, or the premium.
Buyer of last resort mechanisms	An approach where an entity agrees to purchase the credits or benefits of a project, often at a minimum price, if no other buyer can be identified
Reserve accounts	These are often provided in the form of grants and serve as a first-stop for any losses incurred.

As summarised in **Table 6,** not all de-risking strategies suit every type of conservation project. For example, technical assistance is mostly applicable to projects that have complex management, technical and scientific requirements e.g. sustainable agriculture.

Likewise, collateral – that is, a property or asset that is given by a borrower to a lender to secure a loan – is possible to apply against projects where there is a property right e.g. sustainable forestry and agriculture, direct land ownership and conservation covenants. Forward trades are most appropriate for when a credit can be secured in advance if/when it is successfully awarded in the future e.g. carbon credit. The key point is that developers should consider the most appropriate de-risking strategy and tools for their conservation project.

Table 6. Availability of risk mitigation strategies for different conservation focus areas

Type	Conservation focus	Technical assistance	Collateral	Insurance	Forward trades	Guarantees
Food & Fibre	Sustainable Forestry	*Sometimes*	Yes	Yes	Yes	*Sometimes*
	Sustainable Agriculture	Yes	Yes	Yes	Yes	*Sometimes*
	Restoration	*Sometimes*	*Sometimes*	-	-	Yes
	Wild fisheries	*Sometimes*	*Sometimes*	-	Yes	Yes
Habitat	Ecotourism	Yes	*Sometimes*	-	-	*Sometimes*
	Direct land ownership	-	Yes	-	-	*Sometimes*
	Conservation covenants	-	Yes	-	-	Yes
Water	Watershed protection	*Sometimes*	-	-	-	Yes
	Water rights trading	-	-	-	-	Yes

Source: Credit Suisse, 2016.

Project financing

Project finance refers to the legal ownership and project management structure of an enterprise that is used to legally develop and operate a conservation finance project. Project financing is a framework in which ownership structure, project structure, risk structure, and financial structure decisions are made and tied together in the project's legal structure which, in turn, forms a foundation for financing the actual project on a limited recourse basis.

Within project financing, the ownership structure refers to how a **special purpose vehicle** (a separate legal entity which will run the project) is organised i.e. is it part of a corporation, unincorporated joint venture, limited liability partnership (etc)?

Project structure on the other hand refers to the agreements defining responsibilities and transfer of rights (benefits) and/or ownership of the special purpose vehicle between project partners e.g. build, own, operate, and transfer (BOOT) structures whereby the special purpose vehicle (for example) implements and operates a project before transferring its ownership and associated benefits (profits) to another party after it has made its required ROI.

Developing the right ownership and project structure for a blended conservation finance project is a challenging and risky endeavour – getting it wrong can have major consequences for project developer and investor alike. Professional legal advice should be sought in this respect.

<u>Ensuring there is an "exit strategy"</u>

An exit strategy is a plan agreed with investors to dispose of (sell) an investment to provide investors with a capital return. Exit strategies take on different forms e.g. initial public share offerings (when a company wants to raise equity from the share market), mergers (selling to bigger companies) and private offerings to venture capitalists.

It is essential that you put one in place for your investors – after all, they are also looking for a return on their investment within an agreed period of time. One of the key challenges for growing the conservation finance sector is that there is often no or an unclear exit strategy – this is a substantial barrier to investors, most of who will not want to be in the business forever.

<u>Business Plan</u>

This is an <u>internal document</u> where all the key information from the Concept Note, Feasibility Study, and the design of the blended finance and project finance (including ownership) structures comes together. A business plan is a very important strategic tool for project developers. A good business plan not only helps to focus on the specific steps necessary for a concept to succeed, but it also helps project developers and investors achieve both their short-term and long-term objectives. A business plan may contain the following standard headings:

- ✓ Executive summary;
- ✓ Company description;
- ✓ Governance systems;
- ✓ Market analysis;
- ✓ Organisational management (and Board) structure;
- ✓ Sales strategies;
- ✓ Funding requirements, including proposed blended finance structure;
- ✓ Financial projections (including financial model and sensitivity analysis);
- ✓ Risk analysis; and,
- ✓ Exit strategy.

Investment Memorandum

In addition to a business plan, an **Investment Memorandum (IM)** is commonly used when raising large amounts of money and/or for later stage investment after initial funding is raised. An IM is an external marketing document but must include comprehensive and accurate information about the prospective investment (much of which will come from the business plan – see above). An IM - a legal and outwards facing (public) document that an organisation presents to potential investors to explain the objectives, risks, and investment terms of the project. This document will include financial statements, management biographies, company details, and many more items that help give a detailed view of the business and financial plan going forward.

Under Australian law, an IM can only be used for certain types of equity offers e.g. shares. Section 708 of the Corporations Act sets "exempt offerings" and covers small-scale offerings as well as offers to sophisticated and professional investors. As a public document, professional legal advice should be sought in developing an IM.

Typically, an IM will contain the following detail:

- ✓ **Purpose, performance and goals:** What is the project's purpose and objectives? How will these be achieved?
- ✓ **Product or service:** How will the project make money? How will you keep innovating the business model? How will you extend the revenue flows?
- ✓ **Management team and Board:** Who's on your management team and Board of Directors? What is their expertise? Include a brief description of each key person including the skills they bring and relevance to the business' success.
- ✓ **Market:** Who is the target market? What are the opportunities within that market? It is important to not make generalised statements that the size of the market is $X billion, and you aim to capture X% of this market. Include realistic and detailed growth forecasts for the product or services that the company provides e.g. carbon offsets and organic food. Include progress, and how you will achieve projected benefits.
- ✓ **Legal:** Set out the company's intellectual property (IP) rights, including proprietary processes of technologies and trademarks e.g. What registered trademarks does the business have? Does it have any patents? Etc.
- ✓ **Financial:** Generally, 3 years of financial projections (sales, gross profit pre-tax results) should be provided. Ideally, these will have been audited by an independent auditor.
- ✓ **Funding:** Provide clear information about the proposed project financing and blended finance structures, and what you will spend the funds on and why, including milestones and timeframes.
- ✓ **Risks:** What are the key risks that can impact project or investment performance?

Investment or Shareholder and Partner Agreements

Organisations that enter into arrangements with any type of investor should always formalise those arrangements with a legal agreement. A typical investment agreement will include:

- ✓ Date, names and addresses of each of the parties entering into the agreement
- ✓ The amount of money being invested, how the investment will be used and what the investor can expect to receive in return for their financial contribution
- ✓ Payment terms e.g. when and how payment will be made, in one lump sum or multiple payments, listing the dates and amount of each payment to be made
- ✓ Any deliverables to be achieved by certain dates or products and services to be developed and when they are due to be delivered
- ✓ The term of the agreement and how long it is valid for, as well as the return on investment to be delivered and how the agreement will be terminated. Options for how each party can terminate the agreement early should also be outlined.

Depending on the type of investor, different agreements are typically made with them that specify the terms and clauses of their investment, for example to a **shareholders' agreement** , or an **angel** or **venture capital term sheet** .

SUMMARY: Phase 3 – Blended finance structuring

Key questions to answer by the end of this Phase, as relevant to finance

- ☐ Has the legal structure for the project been established? E.g. owner/s, types
- ☐ Do you really understand the advantages and disadvantages of different funding approaches, and have a clear preference and rationale for one particular approach over another?
- ☐ Do you have a well-developed blended conservation finance structure? Have you considered the role of credit enhancement tools in mitigating risks?
- ☐ Do you have an exit strategy in place?
- ☐ Do you have a robust business plan and information memorandum to support your investment pitch?
- ☐ Do you have the appropriate contracts (e.g. Emissions Reduction Purchase and Offtake agreements) in place to secure funding?
- ☐ Do you need external help in the next Phase to develop a blended conservation finance structure that can be confidently pitched to investors?
- ☐ Do you know who the potential investors to pitch to are? Have you got a pitch strategy, and a clear "ask"?

Checklist of important documentation to move to the next Phase

- ✓ Business Plan (see below for more information).
- ✓ Investment Memorandum.
- ✓ Draft Investor or Shareholder agreement.

Phase 4 – Pitching to investors

This section provides some handy hints on tailoring your pitch to the right investor and on delivering it on your bid day.

Who should you pitch to?

By now you will probably have a short-list of investors that you wish to pitch to. Often this short-list will be established through your professional network as you develop your project, and you may have already presented some early concepts to them for feedback. Australia is a relatively small market, and potential investors are generally well known. However, there is also a growing awareness, particularly amongst impact investors, of the positive returns that emerging blended conservation finance opportunities may provide. So, cast your net widely (including overseas), both among these well-known investors and more broadly in the mainstream finance community.

Joining networks (e.g. the Conservation Finance Network in the US and the Australian Land Conservation Alliance in Australia), attending conferences (e.g. Conservation Finance Intensive) and linking in with professional business organisations (e.g. Australian Institute of Company Directors) can help in this way. It's all about networks, and the (exciting) value proposition that you can bring to investors. As part of this you will inevitably play a market development and education role, after all conservation finance is relatively new in Australia and therefore not many investors know much about it.

Knowing what the investor you are pitching to is looking for is critical.

Is it to an angel investor who has a relatively generous term sheet, or a venture capitalist who wants their money-back fast (and with a substantial amount of interest)? Or, can you potentially go to a bank for a loan? Different investor types have different terms for repayment – you need to match your project's projected cashflows against the most suitable investor. This will be something you've already thought about in earlier phases.

Your presentation should be tailored to the investor's expectations.

What will private sector investors be wanting to know?

That will also depend on the type of investor. Getting investors to understand that there is money to be made from conservation and sustainable land management, is a key challenge to overcome when pitching for finance. Likewise, when communicating to government and the broader community, it is of critical importance to highlight the job creation, economic and socio-cultural benefits (such as those associated with indigenous land management) provided by conservation and sustainable land management projects, particularly when seeking access to mainstream funding.

It also extremely important for investors to understand that the management team has a clearly defined strategy (i.e. business plan) that is realistic to implement. This strategy should be the cornerstone of every investor presentation and include measurable milestones that management believe should be achieved throughout the various stages of the strategy. Investors use any communication (e.g. AGMs, press releases) provided by management to build a future project valuation model, and if these expectations are not met, investor confidence in management could significantly deteriorate.

One of the most important investor protections is the proper application of good corporate governance. It is critically important that compliance with government legislation and a minimum level of assurance of this is clearly communicated to investors.

Effective communication

The use of technical terms and jargon is often stated as a barrier to many industries – and this is very applicable to both the conservation and the investment sectors. For example, the use of the word "Riparian" (vegetation) by conservationists has been shown to be the least understood word in a survey of 415 community members - only 3% understood it well, and 75% did not understand it at all[6]. Moreover, the use of highly politicised and ideologically-entwined words, for example the word "environment", can be a powerful barrier to increasing investment in conservation.

The Forest Resilience Bond development team (Blue Carbon Forests, Encourage Capital and the WRI) acknowledged that the success of the Forest Resilience Bond "rests on the development team's ability to translate the language of forest restoration, ecology and hydrology, public resource management, and community engagement into the language spoken by investors". It further notes that "one of the most interesting and challenging aspects of this project has been to learn the languages of such diverse stakeholders. In addition to navigating unique languages, understanding and discussing the intricacies of forest restoration and private investment requires substantial technical knowledge".

As a project developer, talking the (finance) talk is critical if you want to attract private investment. Therefore, in your pitch, consider cutting the environmental jargon and emotive words and try to speak (or at least understand) the investor's language.

[6] Fielding et al, 2016. *Community understanding of water terminology: A survey of Australian community member's understanding of water-related terminology*. Melbourne, Australia.

Tips for a great blended conservation finance pitch

Figure 5 provides twelve tips worth considering to help you nail your pitch.

Figure 5. Twelve tips to help you pitch better

1	**Make your pitch interesting** The three rules of public speaking: Be interesting, be interesting, be interesting. As soon as you're at the front of the room, you have to earn the audience's attention.
2	**Practise and time yourself** If you have 10 minutes, plan for 8. If you have 20 minutes, plan for 16. It takes longer to say the lines out loud than it does in your read-through.
3	**Know who is in the room** Modify your pitch depending on your audience. Know who is in the room and avoid putting your foot in it, or wasting an opportunity e.g. focus on market validation and the financials for investors, and on growth/mutual benefits for partners.
4	**Have a clear and specific "ask"** You need to be crystal clear on what you are pitching for i.e. Why are you talking to these people? What's your desired outcome - Investment? A partnership? Advice? A grant? Make sure your final slide/point sets up the next conversation for this.
5	**Be ready with the answers for questions you might be asked** Getting questions is good – it means the audience is engaged. Not being able to answer these is… not good. Before the pitch, think about what the logical/common questions will be, and sketch out some responses.
6	**Look competent** There's no strict dress code for pitching (e.g. ties, jackets, skirts, heels), however there is one overall principle: "Look the part". Wear whatever you like, so long as it fits the context, and identifies you as being competent in your field.
7	**Pictures are great, but keep the slides to a minimum** A picture is worth 1,000 words. Make sure they are hi-res. Keep the slides to a minimum. 10 slides, 20 minutes, 30 point font is a good structure. Steve Jobs used predominantly images, plus 1-6 words that set the tone for what he was about to say.
8	**Know both the financial AND environmental benefits** Too often, pitchers don't know the financial return an investor is expected to make from a project. Or, the underlying detail on that calculation. Often, they are too focused on the "fuzzies" that will be saved. You must know all your numbers, even if they aren't amazing. Be ready for the questions, including how your investment stacks up against other opportunities in the market.
9	**Present a clear, visual example of how you will make money** Blended conservation finance ideas may be very confusing for your audience. By using diagrams, you can quickly clarify where your cashflows will come from (and who the buyers are, etc).
10	**Be able to explain why YOU will succeed where others have failed** If your concept sounds too challenging, your audience may lose focus or question your capability. If your concept sounds too good, your audience may assume that a cleverer/more powerful competitor will overtake you. You need to balance this.
11	**Have a great opener and closer** Start strong, end strong - the two parts the audience will remember. A powerful opener will help you build momentum, credibility, and keep the audience interested. A definitive closer will help you set the tone for the questions and your capability.
12	**Be ready for tech failure** Assume the tech will break, and you won't be caught unprepared. Develop a pitch that isn't 100% reliant on PowerPoint slides, that you can deliver in a room without a screen. You are the presentation. One last thing - streaming from YouTube is risky.

SUMMARY: Phase 4 – Pitching to investors

Checklist of important documentation to nail the pitch

- ✓ Pitch Pack, including a relatively simple but catchy set of slides, containing
  i. A clear investment "ask" (proposition);
  ii. Diagrams showing how the value chain will work;
  iii. Succinct figures on financial and environmental performance.
- ✓ Draft Investor or Shareholder Agreement.
- ✓ Hard copies of your Investment Memorandum.
- ✓ Due diligence pack on-hand (if asked for), which may include:
  i. Evidence of Offtake Agreements (e.g. carbon) and landholder consent.
  ii. Evidence of Loan Guarantees and other risk.
  iii. Financial modelling assumptions.
  iv. Partnership agreements, etc.

Phase 5 – Implementation & operation

Once final funding has been achieved, a project should be able to move into the implementation and then operational phases. The management team can breathe a sigh of relief at this stage and get going on putting a project in place - however this is likely to be short-lived. On signing an investment agreement, the clock will start ticking towards when a shareholder or loan must be paid back. It is also important not to take the eye off the ball and implement a periodic process for reviewing and improving your blended conservation finance structure.

As your project grows, additional funding requirements may also be necessary or debt restructuring (for example) may be required if sales are underperforming. The point is, financing is an on-going process that requires careful management to ensure the business (project) does not become insolvent. This is why you need the right people and the right partners to watch the business, and a suitably experienced Board to provide good governance.

Good luck

An exciting time to develop world-leading blended conservation finance projects in Australia.

A significant amount of capital is at work to address the world's social and environmental challenges - the impact investing market continues to grow rapidly, with new investors entering to establish impact investing practices and to allocate additional capital to positive impact.

The blended conservation finance market is currently worth approximately $50 billion globally and is expected to double within 5 years and be dominated by small-scale funds of around $100 million[7]. As society becomes progressively aware of existing and potential social and environmental issues, an increasingly large number of organisations, businesses and governments are becoming involved in creating solutions to these problems.

There's never been a better time to bring the right funding to important conservation projects – this Guide provides a great starting point for your blended finance project.

[7] Credit Suisse, 2016. Conservation Finance From Niche to Mainstream. Available at: https://assets.rockefellerfoundation.org/app/uploads/20160121144045/conservation-finance-en.pdf

Glossary

Angel Investor	Normally affluent individual who injects funds for start-ups in exchange for ownership equity or convertible debt.
Avoided-cost model	An approach to financing where investments into projects are made based on the assumption that the projects will avoid expected future costs.
Bankable	When a project or concept has enough future cashflows and high probability of success, to make it acceptable to institutional investors.
Blended finance	A mix of public, philanthropic, and/or private investment. It enables organisations with different objectives to invest alongside each other while achieving their own objectives.
Bond	A fixed-income investment, where an investor lends money to an entity which borrows the funds for an agreed period at a variable or fixed interest rate. Green bonds support sustainability-focused projects, including sustainable agriculture.
Ballot measures	Instruments of direct democracy, that allow voters to directly shape public policy in the voting booth. Common in the US.
Bridge financing	A temporary loan used to fill a gap in financing between the availability of permanent funding (or take-out funds) and the immediate need to react quickly and fund the purchase of an asset.
Capital	In finance, commonly refers to assets needed by a company to generate goods or services, as measured in terms of money value.
Capex	Capital expenditure is the money a company spends to buy, maintain, or improve its fixed assets, such as buildings, vehicles, equipment, or land.
Carbon offsets	A reduction in greenhouse gas emissions (e.g. via sequestering carbon dioxide in replanted forests) to compensate for or to offset greenhouse gas emissions made elsewhere.
Concept Note	A briefing document used to test and develop a prospective blended finance project
Concessional capital / loans	Loans that are extended (often by government) on terms substantially more generous than market loans i.e. the loan interest rate is lower.
Conservation covenant	An in-perpetuity legal agreement between a landowner and conservation organisation that permanently restricts usage rights of a property e.g. preventing real estate development, commercial and/or industrial uses, or clearing vegetation, and is recorded on the property's title. Known in the United States as a "conservation easement".
Conservation finance	The practice of raising and managing funding to support land, water, and natural resource conservation.
Credit enhancement	Includes various tools (e.g. letters of credit, insurance mechanisms, loan guarantees) which help project developers leverage capital they could not otherwise access.
Credit rating agencies	A company that assigns credit ratings, which rate an entity's ability to pay back a loan by making timely principal and interest payments and the likelihood of default
Crowdfunding	The practice of funding a project or venture by raising small amounts of money from many people, typically via the Internet.
Debt	A financing arrangement where the borrower has a non-contingent obligation to provide a future financial benefit to the lender. Debt financing includes funds that support the purchase of an asset via credit.
De-risking	Refers to the practice of entities taking on some portion of the project risk so that the risk to the remaining investors is lower.
Direct finance	Funds flow *directly* to a project for the primary purpose of supporting conservation.
Due diligence	A comprehensive appraisal of a business or project undertaken by a prospective investor to establish its assets and liabilities and evaluate its commercial potential.
Ecosystem services	The ability of an ecosystem to provide goods and services to people, which may be assigned economic value to help in economic decision-making processes.

Environment offsets	Like for carbon offsets, environmental offsets seek to compensate for impacts on the environment or biodiversity at one site through protection and management of biodiversity elsewhere.
Environmental Impact Bond	A form of bond that provides funding for ecologically sensitive green infrastructure. It is based on an "outcomes-based" or "pay-for-success" model.
Feasibility Study	Takes all of a project's relevant factors into account—including economic, technical, legal, and scheduling considerations—to ascertain the likelihood of completing the project successfully.
Financial close	The stage in a financial agreement where all conditions have been satisfied (or waived), documents executed, and finance becomes available for use.
Grants	An arrangement for the provision of non-repayable financial assistance gifted by one party to another, usually with the purpose of funding a specific project.
Green infrastructure	A network of natural landscape assets which underpin a certain function, e.g. the water filtration function provided by forests.
Impact Investing	Investments that combine financial returns with social and/or environmental benefits.
Indirect finance	Finance flows to projects for which the predominant purpose is something other than creating an environmental benefit (e.g. financial return on investment), but where environment benefits are created indirectly.
Interest rate	The percentage of the borrowed amount charged by a lender for the use of borrowed funds.
Institutional investors	An organisation whose primary purpose is to invest its own assets or those it holds in trust for others. Includes fund managers, superannuation funds, universities and banks.
Investment Memorandum	A legal document that an entity presents to potential investors to explain the objectives, risks, and investment terms surrounding a proposed investment.
Letter of credit	A guarantee issued by one bank to another to serve as a guarantee for payments made to a specified person under specified conditions.
Loan guarantee	A legally-enforceable agreement by a third-party to repay a loan on behalf of the borrower.
Memorandum of Understanding	A "MOU" is a formal document describing the broad outlines of an agreement that two or more parties have reached. It is not a legally binding document but signals the intention of all parties to move forward with a contract.
Net profit	Revenue remaining after all operating expenses, interest and taxes are deducted.
Offtake agreement	An agreement between a producer and a buyer to purchase or sell portions of the producer's *future* production e.g. carbon credits generated through planting trees.
OpEx	The costs a company incurs for running their day-to-day operation e.g. wages and salaries, business travel, electricity and water.
Outcome-based Model	A form of performance-based contracting that ensures governments limit their losses in case projects are unsuccessful, which encourages them to try novel solutions like green infrastructure.
Philanthropy	Charitable giving by an individual or organization.
Project finance	The financing of projects based upon recourse to the project only, rather than to a corporate entity.
Private equity funds	An aggregated amount of investor capital used to purchase an ownership interest in a non-public entity or entities.
Promissory note	A legally binding document representing a promise to pay an agreed upon sum to a specified person on a specified date or upon demand - a legally enforceable IOU.
Rate of return	The net gain (benefit) or loss on an investment over a specified period, expressed as a percentage of the investment's initial capital cost.
Real assets	Physical assets that have value due to their properties and substance e.g. precious metals, real estate, agricultural and forestry land, water and carbon rights, and machinery.
Retail Investors	An individual who purchases investments (e.g. shares) for his or her own personal account rather than for an organization.

Return on Investment	Measures the gain or loss generated on an investment relative to the amount of money invested – often referred to as ROI
Revolving loan fund	A pool of loans made to individuals or small-businesses which self-funds new loans via the repayment of existing loans within the portfolio.
Risk profile	An evaluation of an individual's willingness and ability to take risks when investing.
Risk-return profile	The expected financial gains of a given investment modelled against the risk of financial loss.
Secondary financing	A broad term for a secondary, junior or subordinated loan which stands behind the first, principal or senior loan.
Seller financing	Funding the purchase of an asset when the seller accepts only a portion of the price upfront and accepts a loan with periodic payments and interest for the remainder.
Shareholders agreement	A legally binding contract between shareholders of a company (project), which ultimately governs the relationship between the shareholders and specifies who controls the company, how the company will be owned and managed, how shareholders' rights may be protected and how shareholders can exit the company (project).
Special purpose vehicle	A legal entity which is legally segregated from its sponsor, particularly with respect to its balance sheet and/or operating risks. It is typically created for a limited business acquisition or transaction, and can be used as a funding structure.
Social Impact Bond	A contract with the public sector in which the issuer commits to use bond proceeds to fund improved social outcomes that result in public-sector savings.
Subordinated debt	A debt owed to an unsecured creditor that in the event of a liquidation can only be paid after the claims of secured creditors have been met.
Subsidies	An economic incentive granted to industry, businesses or the wider community by government to reduce the price of a good or service to encourage utilisation.
Surcharges	A secondary fee or other charge that increase the price of a good or service.
Technical assistance	Non-financial assistance provided by local or international specialists. It can take the form of sharing information and expertise, instruction, skills training, transmission of working knowledge, and consulting services and may also involve the transfer of technical data
Term sheet	Usually a bullet-point document outlining the material terms and conditions of a business agreement. For any given investment it could include terms relating to: anticipated maturity and return; security or ranking with respect to payments; a seat on the Board of Directors; the type of equity to be issued for the company; anti-dilution clauses (i.e. those designed to protect the value of the investor's interest); terms designed to ensure the investor gets their investment back in the event that a business owner decides to sell early and potentially at a loss to the investor.
Transfer fees	An additional fee paid into a stewardship account, such as via a land trust.
Transaction costs	Expenses incurred when buying or selling a good or service e.g. verification costs, brokerage fees and interest payments associated with carbon credits.
Transferable tax credits	Tax benefits that can be sold to other individuals or entities that allow the buyer(s) to realize the full advantages of these tax benefits.
Venture capital / capitalists	Capital invested in a project in which there is a substantial element of financial risk, typically a new business / business model. Venture capitalists often require a high rate of return compared to other investors.
Wholesale Investors	Legal entities that generally invest in larger amounts and more complex transactions. They are defined under the Corporations Act and are typically considered to be more financially sophisticated and have experience in investing and protecting their interests and therefore do not need all of the consumer protections that apply for retail investors.