



Long-term operation and financing strategy of the Tropical Forest Conservation Agreement (TFCA Colombia)

David Celis
Administrative and Financial Coordinator

October 2021

General information

Project or program name	Tropical Forest Conservation Agreement
Leading entity	Fondo Acción
Contact point	elfondo@fondoaccion.org
Author (s)	David Celis, Administrative and Financial Coordinator
Duration of the experience	2004 - current
Date of this version	October 2021
Suggested quotation	Celis, D. (December 2021). Fondo Acción. Retrieved from Aprender en Acción: https://fondoaccion.org/2021/10/27/la-logica-del-largo-plazo/

Introduction

In March 2004, the governments of Colombia and the United States and the world's largest non-governmental environmental organizations with recognized expertise in conservation—World Wildlife Fund (WWF), Conservation International (CI), and The Nature Conservancy (TNC)—agreed on a subsidized debt-for-nature swap under the Tropical Forest Conservation Agreement (TFCA). The swap was structured with a financing scheme proposed for Africa, Asia, and Latin America, which included not only resources for immediate investment in environmental projects, but also the creation of an endowment funds that would provide long-term sustainability.

The program's objective is the conservation, protection, restoration, and sustainable use of Colombia's tropical forests. It seeks to increase connectivity, sustainability and ecological integrity in prioritized forest areas. Its highest governing body is the Oversight Committee, which is made up of representatives from both governments and the three non-governmental organizations. They make decisions on resource management, the selection of intervention areas and the co-financing of projects. Since October 2004, Fondo Acción has acted as the Executive Secretariat responsible for managing and operating the TFCA in Colombia.

The TFCA in Colombia had two special features: the first was the involvement of the private sector in the program, and the second was the gradual accrual of swap funds, which were paid by the Colombian government in semiannual installments over a twelve-year period.

As of August 2021, seventeen years after TFCA Colombia began operations, the financing strategy has managed US \$10 million in debt swap, providing US \$8 million in resources to 40 projects and leveraging US \$4.2 million in counterpart funds from the executing organizations, participating communities, and some regional and local institutions with a presence in the intervention areas. As a result of active but prudent financial management, as of August 31, 2021, the balance in the endowment account exceeded US \$9.3 million, which is very close to the original value of the entire swap.

Between 2004 and 2016, the Colombian government completed all payments stipulated under the TFCA. Of the US \$10 million provided for in the swap, US

\$5 million were used to finance projects and pay administration expenses for the first five years, in accounts destined to be depleted (grants funds). The remaining 50% was used to set up the endowment fund, which in 2010 began directing returns to the grant fund for its continued operation.

This document outlines some of the factors that have been key to the effectiveness of the financing scheme, which has enabled the implementation of important projects for the conservation of the country's strategic ecosystems and which, with financial sustainability achieved, is expected to continue operating in the long term as provided for in the original design of the program.

► The implementation process

Initially, the program planned to intervene in the areas of influence of five of the country's protected areas, which serve as buffer zones: Ciénaga Grande de Santa Marta, Serranía de Los Yariguíes, Andean Oak Forest Corridor between the Iguaque and Cachalú Sanctuaries, El Tuparro Biosphere Reserve, and the Tinigua-Sumapaz Corridor. Subsequently, seeking greater investment impact and considering security restrictions, the intervention zones were reduced to three: Serranía de Los Yariguíes, the Andean Oak Forest Corridor, and the El Tuparro Biosphere Reserve. The latter was expanded in 2017 to include the entire Colombian Orinoco watershed.



In its first call for projects in 2005, the TFCA disbursed US \$300,000 from the grants account. The amount of resources delivered in each call was determined by considering the cash flow of the three years to come, meaning that the project developed according to the availability of money. The model foresaw that by the time the grant resources were exhausted, the consolidation of the endowment should have been achieved and the grants account would begin to be furnished with the returns of this endowment.

The projects developed between 2005 and 2009 received significant contributions from the TFCA—between US \$550,000 and \$750,000. These funds were awarded to consolidated and mature executing organizations that had the technical, administrative, and operational structure necessary to develop large-scale projects and were able to provide counterpart funds equivalent to the grants. These first calls for proposals supported local socio-environmental processes, strengthening the capacity of several community-based organizations that participated in these projects.

The requirement of counterpart contributions from the implementing parties contributed to ensuring greater commitment by the implementers to work together in the execution of the projects and reducing dependence on donation resources. The organizations contribute not only cash resources, but also in kind, in the form of their logistical operating capacity and their knowledge of the communities and the territory, which makes it possible to carry out the projects more efficiently.

During the execution of the projects, Fondo Acción provides comprehensive support to the organizations in the implementation of the initiatives, seeking greater efficiency and effectiveness to achieve the proposed objectives. This has mainly consisted of ensuring the greatest possible investment on the ground, positively impacting the living conditions of the communities, supporting sustainable productive and environmental activities. The ultimate purpose is to reduce the negative effects of human action on protected areas. Today we can affirm that a strategy that includes social benefits is one of the key success factors of TFCA Colombia.

Between 2010 and 2017, with support from Fondo Acción, the participation of small, youth, and community-based organizations in the calls for proposals increased significantly and several were selected as project implementers in the

Andean region. Applicant organizations demonstrated strengthened project management skills. Thus, the TFCA mobilized more resources for local organizations, consolidating ongoing processes, deepening the involvement of farming families, and improving the sustainability of forest conservation, restoration, and sustainable use processes.

Since 2017, TFCA has made significant efforts to reach out to local and community-based organizations. In this approach, it is the community leaders from peasant associations that are in charge of designing and implementing the projects co-financed with TFCA resources and partnering with large and medium-sized NGOs.

A far-reaching strategy

Fondo Acción is responsible for managing TFCA Colombia's accounts. The grants account is managed in the domestic financial market, in Colombian pesos through agreements with first-class fiduciary institutions since this is the currency of execution and because of the liquidity required. On the other hand, the endowment account is managed abroad, in dollars through financial specialists with experience in managing the portfolios of philanthropic entities. Since 2017, the administration of the endowment account has been entrusted to JP Morgan, which also manages the endowment account of the Initiative of the Americas. With the integrated management of the portfolio, Fondo Acción has achieved lower management fees and has opened access to better investment possibilities in sustainable portfolios that respond to environmental, social, and governance (ESG) parameters.

It is important to point out that in the TFCA Colombia agreement, it was explicitly established that it would only be possible to make use of the returns from the endowment account when the US \$5 million in grant resources had been disbursed. At any time during the execution of the program, the minimum balance in the endowment account had to be higher than the original capital contributed. Thus, in the event that its value were to drop beneath the original capitalization, this source of funds could not be used until the balance of the account exceeded US\$ 10 million.

This strict condition required the application of an investment policy that ensured the conservation of capital and sought to grow the portfolio. This strategy

for managing the TFCA's resources has obtained outstanding results beyond expectations during the first 17 years of the program. Such was the success that the first withdrawal of resources from the endowment account, planned for 2010, was postponed until 2017. In the intervening period, only the original grant resources were used (US \$5 million, equivalent to COP \$11,618 million), plus the yields obtained in the management of that account (almost US \$1 million, or COP \$2,094 million).

By the time the endowment was consolidated, the investment strategy approved by the Oversight Committee had proven its effectiveness: the balance exceeded US \$7,7 million by the end of 2016. Thus, with more than US \$2,7 million in accumulated returns, sufficient resources could be counted on to being feeding into the grant account, which enabled the funding of new calls for proposals. In 2017, the first resources were directed from the endowment returns to the grants account, according to the investment strategy established at the beginning of the program. Based on this model, Fondo Acción, as administrator of the TFCA, managed to maintain the capital contributed by the swap, consolidate the endowment, and become the source of long-term financing.

At present, the resources for the operation of the TFCA come from the yields generated in the endowment account. As of August 31, 2021, the account portfolio totaled US \$9,4 million, invested in different financial vehicles, within the ranges allowed by the investment policy approved by the Oversight Committee, as follows:

TFCA endowment account portfolio	Market value (USD)	Share of portfolio	Tactical range (investment policy)
Cash and equivalents	\$ 36,887	0,4%	16% - 46%
Fixed income	\$ 2,633,286	28,0%	
Stock markets, United States	\$ 3,143,308	33,5%	40% - 70%
Stock markets, Global	\$ 2,484,903	26,5%	
Alternative investments	\$ 2,361	0,0%	0% - 29%
Other investments	\$ 1,089,773	11,6%	
Total	\$ 9,390,518	100%	100%

Source: Calculations by Fondo Acción, based on JP Morgan reports.

The investment policy of the equity portfolio

Investment policies are a guide both for the selection of the financial manager and for the manager's administration of the portfolio's resources. The fundamental principles stipulated by the policy are:

- Transparency
- Professionalism
- Security
- Liquidity
- Profitability
- Financial, environmental, and social sustainability
- Inclusion
- Effectiveness
- Complete avoidance of conflicts of interest and insider trading

To ensure a portfolio completely aligned with the mission of the organization in the investments managed by Fondo Acción, all investments for which there is zero-tolerance must be eliminated and investments in instruments of companies that are characterized by good environmental, social, and governance practices must be included. Consequently, the policy also establishes exclusion or zero-tolerance criteria to avoid investments in sectors that go against the spirit and mission of the program and Fondo Acción, such as the following sectors:

- Fossil fuel industries
- Industries employing child labor
- Weapons industries, both conventional and unconventional
- Tobacco
- Alcohol
- Gambling
- Pornography or adult entertainment
- Highly polluting industries



Photo: © David Rugeles - Fondo Acción

During the years of operation of the endowment account, the investment policy has been adjusted three times: once to include tactical investment ranges, another time to admit alternative investments within the portfolio, and most recently to migrate the portfolio towards assets based on investments with environmental, social, and governance (ESG) performance measurement criteria. (For more details see the case study “Investment Portfolios that are 100% Sustainable ¹.”) The current investment policy for the endowment can be consulted on Fondo Acción’s website².

In conclusion, the investment policy is the roadmap that leads both the investor and the financial manager down the path of the financial and capital markets, with a long-term vision that allows for consolidation but at the same time provides the liquidity necessary to ensure operations and investment in projects that materialize the mission. This policy must be flexible enough to allow the manager to make the necessary tactical adjustments but totally clear as to the type of assets in which investment is allowed, all managed according to the risk profile that TFCA is prepared to tolerate.

1 <https://fondoaccion.org/2021/08/12/portafolios-de-inversion-100-sostenible-2/>

2 <https://fondoaccion.org/wp-content/uploads/2020/10/DA-MA-02-Politica-de-Inversiones-cuenta-de-las-inciativa-de-las-americas.pdf>

► Figures from the endowment account program indicators

Since its creation in 2004, TFCA had foreseen a financing scheme through an endowment fund. Payments of US \$4,99 million from the swap were paid into this account. As of August 31, 2021, yields of US \$6,3 million have been achieved with an average annual return of 7,58% and US \$2,04 million have been transferred to the grants account, bringing the balance to US \$9,4 million, as shown in the following table:

TFCA endowment account (USD)	2004 - 2016	2017	2018	2019	2020	2021 31 AGO 2021	TOTAL 2004 - 2021
INITIAL BALANCE	\$ 0	\$ 7,720,494	\$ 8,468,560	\$ 7,390,175	\$ 8,121,646	\$ 8,893,195	\$ 0
(+) Capital contributions	\$ 4,995,110	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0	\$ 4,995,110
(-) Withdrawals	\$ 0	\$ 309,000	\$ 550,000	\$ 440,000	\$ 140,000	\$ 600,000	\$ 2,039,000
(+) Net change in value	\$ 2,725,384	\$ 1,057,066	-\$ 528,384	\$ 1,171,470	\$ 911,549	\$ 1,097,323	\$ 6,434,408
BALANCE AT CUTOFF	\$ 7,720,494	\$ 8,468,560	\$ 7,390,175	\$ 8,121,646	\$ 8,893,195	\$ 9,390,518	\$ 9,390,518
Performance for the period	4,20%	14,82%	-7,73%	16,30%	10,75%	12,76%	7,58%

Source: Calculations by Fondo Acción, based on JP Morgan reports.

It is important to note that it is to be expected that in some years the portfolio closings will show devaluations, but the strategy of managing a four-year cash flow has allowed acquired commitments to be honored and thus the execution of the program in the long term. Between 2004 and 2021, the program received a total of 189 proposals, of which 40 (21%) were financed. Total investments amounted to US \$12,2 million, of which TFCA contributed US \$8,0 million (66%) and counterpart funds amounting to US \$4,2 million (34%) were leveraged from the implementing organizations and their local partners. The period from 2004 to 2016 corresponds to the phase financed exclusively with the original grant resources (Phase I). The period from 2017 onwards corresponds to the phase financed with returns from the endowment account (Phase II).

TFCA Indicators (thousand USD)	Phase I 2004 - 2016	Phase II 2017 - 2021	TOTAL
No. of proposals and profiles received	125	64	189
No. of projects approved	18	22	40
Resources committed by TFCA	\$ 5,424	\$ 2,598	\$ 8,022
Counterpart resources	\$ 2,520	\$ 1,656	\$ 4,176
Total value of approved projects	\$ 7,944	\$ 4,254	\$ 12,198
TFCA contributions	68%	61%	66%
Average TFCA contributions x project	\$ 301	\$ 118	\$ 201
Average TFCA contributions x year	\$ 452	\$ 520	\$ 472

The indicators show that the TFCA's financing strategy, which in the early years relied on significant grant resources to finance the execution of the projects and currently runs on the returns from the endowment, has provided the necessary cash flow to maintain an annual rhythm of program financing and guarantee its operation. We can thus say that the strategy has worked and has been sustainable over the long term.

Conclusions and recommendations

In these years of experience in the execution of TFCA Colombia, it has been demonstrated that what makes the program in Colombia special is its financing structure and its investment policy: a portion of the swap funds destined for investment in projects, and a capital endowment to continue making investments and operating the initiative over the long term. On this path, it has been key to have an active investment policy that is adjusted to the changing conditions of the financial and capital markets, but subrogated to the environmental and social mission that TFCA has had since its conception, together with

the clarity and transparency with which its resources must be managed and invested. In this way, the policy has sought not only the financial profitability of its investments, but also inherent risk management and a preference for responsible managers operating on ESG principles.

In order to achieve these objectives, the selection of a first-rate operating entity, Fondo Acción with its close ties to civil society organizations and experience in managing endowment accounts has been a wise choice. The financial results are to a large extent the product of the professional management provided by the financial administrators that Fondo Acción chose for the investment portfolio.

TFCA Colombia has been successful in committing grant resources through medium-term calls for proposals (3 to 5 years). In this way, it was possible to execute the program despite the fact that it would receive the totality of the resources in semi-annual installments over a twelve-year span. Prudence in acquiring commitments with projected cash flow worked and also made it possible to find suitable partners with the required technical expertise, the necessary operating capacity, knowledge of the territory and communities, commitment to providing counterpart resources that leveraged the projects and made them larger, with greater coverage and broader impacts.

We believe that the comprehensive approach provided by Fondo Acción to the executing organizations during the implementation of the projects has achieved a better and more transparent use of resources, effective achievement of the objectives set, and more positive impact on the participating communities, as well as on the strengthening of the organizations. In addition, the building of relationships based on respect and trust, gained over time, between Fondo Acción and the other stakeholders implementing the program has contributed to its success.

The work to strengthen the leadership and production capacities of smallholder organizations as well as the consolidation of an endowment fund respond to the same long-term strategy: constant savings for financial sustainability and the longevity of communities in their territories so as to maintain the positive impacts of their responsible care for the natural environment and human wellbeing.

In spite of the achievements and the evident benefits of a financing scheme that mixes short-term (grant) resources with long-term (endowment) funds, so far the multiple efforts to increase the endowment portfolio have been unsuccessful. A larger endowment would enable calls for proposals to be larger and have greater coverage and frequency. It is possible that we have not knocked on the right doors, those that harbor a long-term vision as a strategy. This is an issue that must be revisited and analyzed again in order to find a strategy of approach.

Finally, we must recognize that for all these achievements to be possible, permanent communication between Fondo Acción and the Oversight Committee has been crucial. The strategic vision of the members of the supreme governing body has allowed us to take the program in the best possible direction, despite the ups and downs that the day-to-day running of the program brings.

That is why today, 17 years after the signing of the TFCA, the achievements are evident and the financial resources are preserved as we continue investing in the strategic ecosystems that are Colombia's tropical forests.

References

- Arango, N. (July, 2020). *PORTAFOLIOS DE INVERSIÓN 100% SOSTENIBLE: Un Imperativo ético*. Recovered september 24th, 2021, from: <https://fondoaccion.org/2021/08/12/portafolios-de-inversion-100-sostenible-2/>





We are a Colombian private fund with 20 years of experience in sustainable investments in environment and childhood. We create opportunities and generate connections that facilitates learning and collective work within the organization and with other public and private institutions.

(+57) 1 285 3862 ext 101 • Cra 7 N° 32 - 33 27th floor • Bogotá - Colombia

     @FondoAcción • www.fondoaccion.org