

## Sixth Policy Forum on Natural Capital Data for Better Decision Making

### Background Note on Financing for Nature

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#### 1. Making the case for nature positive financing

Expansion of economic activity has come at the expense of natural capital on a planetary scale. Deforestation is occurring at unprecedented and increasing rates. Each year woodlands roughly equal to the size of Costa Rica is lost, and as carbon sinks disappear, reaching the Paris climate goals will be harder<sup>1</sup>. ‘Biodiversity loss’ is now ranked among the top three most severe risks over a 10-year horizon by governments and business leaders.<sup>i</sup> Sectors that depend on ecosystem services provided by nature generate half the world’s global value-added, or US\$44 trillion annually<sup>ii</sup>. The collapse of selected ecosystem services is estimated to cause a 10% loss of 2030 GDP in low-income economies, compared to business as usual<sup>iii</sup>. Biodiversity loss represents a material risk to investors and asset owners<sup>iv</sup>, which could significantly affect their financial performance. The implications of nature-related risks leave governments, including central banks and ministries of finance, exposed to fiscal and financial instability. Finally, at the local level, communities are at risk, as they rely on nature for food, shelter, livelihoods, and safety nets. Three socioeconomic systems are driving much of biodiversity and ecosystem services loss globally: food, land use, and ocean use; infrastructure and the built environment; and energy and extractives<sup>v</sup>. Shifting them to sustainable practices could deliver US\$10.1 trillion in annual business opportunities and 395 million new jobs by 2030.<sup>vi, vii</sup>

The world currently spends only US\$120-140 billion on biodiversity conservation<sup>vii</sup>, much of it in the form of domestic public spending with limited private sector investment. There is a significant and growing financing gap for nature investments, currently estimated at an average of US\$711 billion per year. There are several challenges contributing to this gap. In the public sector, many governments have limited access to affordable market-based or concessional financing to fund a holistic, nature positive investment portfolio. Sovereigns are not rewarded for prioritizing and mainstreaming nature positive investments, and there is an overreliance on government budgets, donor grant-funded projects, and niche, small-scale transactions. In the private sector, there is a lack of bankable and financially profitable or commercially viable projects. Financial products that directly target nature are nascent, while Environmental, Social, and Governance (ESG) and impact investors have limited options to channel capital to directly support projects that deliver nature conservation outcomes, especially in lower- and middle-income countries. Potential investors in nature-oriented action are often discouraged by the lack of a direct financial return and a lack of common standards for measuring risks.

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<sup>1</sup> 2019 IPCC special report on Climate Change and Land.

## 2. Two pathways to address the challenge

There are two channels for overcoming these challenges: incentivizing improved management of biodiversity risks (greening finance); and monetizing cashflows from the provision of ecosystem services (financing green).

- **Greening finance.** Governments are estimated to spend at least US\$800 billion on fossil fuel, fishing, and agricultural subsidies. While important for immediate concerns such as food security, livelihoods and incomes, they are harmful to biodiversity and will compromise longer-term development outcomes.<sup>viii</sup> “Greening finance” refers to efforts to direct financial flows away from projects and programs that detrimentally impact biodiversity and ecosystem services, toward investments that mitigate such negative impacts or deliver positive environmental co-benefits. Examples include creating fiscal incentives for incorporating nature-related risks into investment decisions, or repurposing subsidies harmful to biodiversity towards nature-friendly programs and projects.
- **Financing green.** While a substantial portion of the nature financing gap could potentially be addressed through subsidy reform<sup>ix</sup> or other “greening finance” measures, direct investments in nature-based solutions will also play a key role. “Financing green” involves investments in projects and programs that contribute to conservation, restoration, and sustainable use of green and blue biodiversity and ecosystem services. Examples include the use of concessional finance to de-risk and scale private investment and pilot financial solutions. For instance, fixed income products linked to forestry, non-timber forest products, wildlife, and fishing, can help channel financing from the capital markets. Another example is investing domestic public finance in nature-based solutions that generate nature co-benefits while meeting other development objectives.

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## 3. The role of data and analytical tools

To mobilize financing for nature at scale requires a comprehensive approach, with adequate coordination between governments, the private sector, and development partners. Addressing such challenges will not happen overnight. In the near to medium term, until nature emerges as an asset class of its own, concessional financing will need to be deployed to help de-risk nature investments, or provide potentially higher returns, for private capital to flow to nature-friendly investment options.

As part of the transition towards nature-smart finance, there is a key role for better knowledge, data, and decision-support tools. Together they facilitate the systematic incorporation of nature-related risks and opportunities into investment decisions of governments, financial institutions, and companies. Improved data and analytics can support “greening finance” by documenting the economic and financial costs of inaction, and by underpinning assessments of alternative policy options to re-orient finance towards improved management of nature. Similarly, “financing green” requires standardized, widely accepted metrics for nature-positive outcomes, to which financing can be linked.

Coordinated efforts towards nature financing guided by data and analytics will be needed to unlock public and private investments. Box 1 provides an overview of selected initiatives that promote financing for nature, leveraging in different ways the creation, harmonization or disclosure of data.

*Box 1. Selected Initiatives to Promote Nature Finance*

The Task Force on Climate-related Financial Disclosures (TCFD) is developing recommendations for climate-related disclosures to promote informed investment, credit, and insurance underwriting decisions. This will, in turn, enable stakeholders to better understand the concentrations of carbon-related assets in the financial sector and the financial system's exposures to climate-related risks. The TCFD has over 1,000 supporters and is currently engaged in helping companies implement measures to advance the availability and quality of climate-related disclosure.

A United Nations Climate Action Summit and COP26 flagship initiative, The Coalition for Climate Resilient Investment (CCRI) represents private financial industry commitments, in partnership with private and public institutions, to foster integration of physical climate risks (PCRs) in investment decision-making.

Nature Finance (formerly Finance for Biodiversity -F4B) aims to increase the role of biodiversity in financial decision-making and align global finance with nature conservation and restoration. Nature Finance is a dual-purpose platform, implementing its own activities across five work streams and making grants to support others. Work stream areas include: (i) market efficiency and innovation; (ii) biodiversity-related liability; (iii) catalyzing nature markets; (iv) citizen engagement and public campaigns; and (v) responses to the COVID crisis. Nature Finance has recently launched the Sustainability-linked Sovereign Debt Hub.

The G20 Sustainable Finance Working Group (SFWG) is working with private financial actors and market regulators on improving the consistency, comparability, and reliability of broader sustainability reporting. SFWG is working with the Financial Stability Board (FSB) to deliver a multi-year G20 Roadmap for sustainable finance.

The joint Study Group on 'Biodiversity and Financial Stability' was launched in 2021 by the Network for Greening the Financial System (NGFS) and the International Network for Sustainable Financial Policy Insights, Research, and Exchange (INSPIRE) to assess linkages between biodiversity loss and the macroeconomic and financial systems. INSPIRE considers both the dependency of the financial sector on ecosystem services, and the impact of the financial sector in exacerbating the degradation of natural systems.

The Nature, People and Climate Investment Program of Climate Investment Funds (CIF) focuses on integrated solutions for the impacts of climate change. New donor commitments in 2022 allowed the CIF to call an expression of interest for countries looking for a potential allocation for the investment plan of up to approximately \$50 million. Fundraising is ongoing.

#### **4. Focus on Natural Capital Data and Analysis**

Despite recent efforts to enhance nature risk disclosure and information sharing, there is still the need to: (a) develop a shared set of standards to quantify nature outcomes for suppliers and users of resources so it can be

linked to financing; (b) strengthen country-level capacity to adopt standards, establish and enhance its frameworks, and design and deploy innovative financing instruments; and (c) access financial incentives to catalyze investments at scale for nature positive action. Without these efforts, there is a high risk that governments, donors, and investors will continue down the path of fragmented actions. Use of internationally recognized standards for specific asset classes can help countries achieve transformational changes. One example is Natural Capital Accounting (NCA)/System of Environmental Economic Accounting (SEEA) (see Box 2), which could be leveraged to strengthen existing initiatives and scale nature investments. The use of established NCA and SEEA efforts can support broader efforts to: (1) strengthen the political case for countries to invest in nature; (2) market natural assets and help access performance-based financial instruments that provide a nature-smart financial incentive to borrowers and investors; and (3) leverage established international and country-level statistical systems, processes, and knowledge networks.

*Box 2. Tapping the potential of Natural Capital Accounting (NCA) to Accelerate Finance for Nature*

Over the last ten years, a global statistical standard for NCA, the System of Environmental Economic Accounting (SEEA), has been developed and adopted by international organizations and governments around the world. SEEA can be applied at different spatial scales, can help quantify perverse incentives towards mismanagement of nature; and can underpin policies aimed at greening finance. SEEA has a potentially important role to play in the nature finance agenda, as it can:

- **Strengthen coalitions for nature financing:** SEEA can help facilitate the formation of coalitions by providing a “common language” for closer cooperation on crucial solutions such as blended finance.
- **Encourage alignment:** Global demand for measuring economies’ dependence on biodiversity (and the economic impacts of its depletion) is likely to grow in the near future through the post-2020 Global Biodiversity Framework (GBF), the update of the Global Reporting Initiative (GRI), the final report of the Taskforce for Nature-related Financial Disclosures (TNFD) and the E.U.’s Corporate Sustainability Reporting Directive (CSRD). Adoption of the SEEA standard by these initiatives can facilitate convergence and promote synergies.

To fully seize the potential of SEEA, a few key steps are required:

- **Assess data needs:** A better understanding of the data and analytical needs of the public and private sector can promote a shared understanding of how SEEA can meet such needs.
- **Enhance data availability and access:** Public data providers need to improve availability of high-quality biodiversity information linked to socio-economic data; access to data on the private sector also needs to be improved through disclosure efforts, such as those listed in Box 1.

## **5. The Way Forward**

Knowledge products, tools, technical assistance, and financing is needed to help countries implement policy reforms and investment programs that shift the balance from an overreliance on limited government budgets and grants towards a longer term and holistic approach that attracts domestic and foreign private capital. With corporates and investors starting to pay more attention to the environmental, social, and governance aspects of their investment decisions, there is an opportunity to scale up efforts, especially in the following areas:

- **Global and national level coordination** is required to efficiently deploy a combination of policy and financial instruments, including grants and concessional finance from donors and private foundations.
- **A mix of policy, debt, and non-debt products** already available in the market can be used to incentivize private sector participation, secure funds for nature action, and test new instruments, including performance-based instruments and capital markets products tailored to domestic and foreign markets.
- **Knowledge sharing and capacity building platforms** for financial sector regulators and industry associations in countries are needed to enhance the ability of decision-makers to integrate risks and opportunities associated with nature.
- **Development and adoption of standardized taxonomies, reporting and disclosure frameworks** are needed to promote acceptance, broad adoption, and systematic use of new instruments that efficiently mobilize capital for direct nature investments in priority biodiversity hotspots and for transitioning economic sectors to sustainable production practices.

<sup>i</sup> WEF (World Economic Forum). 2022. Global Risks Report 2022. Geneva: WEF. 2022.

<sup>ii</sup> WEF (World Economic Forum). 2020. Nature Risk Rising: Why the Crisis Engulfing Nature Matters for Business and the Economy. Geneva: WEF.

<sup>iii</sup> Johnson, Justin Andrew; Ruta, Giovanni; Baldos, Uris; Cervigni, Raffaello; Chonabayashi, Shun; Corong, Erwin; Gavryliuk, Olga; Gerber, James; Hertel, Thomas; Nootenboom, Christopher; Polasky, Stephen. 2021. The Economic Case for Nature : A Global Earth-Economy Model to Assess Development Policy Pathways. World Bank, Washington, DC. © World Bank. <https://openknowledge.worldbank.org/handle/10986/35882>

<sup>iv</sup> Materiality refers to the significance of a matter in relation to a set of financial or performance information. If a matter is material to the set of information, then it is likely to be of significance to a user of that information (OECD). Materiality is rarely determinable by a bare quantitative equation; rather, it requires an assessment of whether a reasonable investor would consider the information relevant to its decision whether or not to invest in a company. That assessment may require consideration of both quantitative and qualitative factors. (Commonwealth Climate and Law Initiative)

<sup>v</sup> The World Economic Forum estimates that together with climate change, three socioeconomic systems – food, land use, and ocean use; infrastructure and the built environment; and energy and extractives – endanger 80 percent of threatened or near-threatened species (WEF 2020b).

<sup>vi</sup> World Economic Forum. 2020. “The Future of Nature and Business.” WEF, Geneva, [http://www3.weforum.org/docs/WEF\\_The\\_Future\\_Of\\_Nature\\_And\\_Business\\_2020.pdf](http://www3.weforum.org/docs/WEF_The_Future_Of_Nature_And_Business_2020.pdf).

<sup>vii</sup> Deutz, A., G. M. Heal, R. Niu, E. Swanson, T. Townshend, L. Zhu, A. Delmar, A. Meghji, S. A. Sethi, and J. Tobin-de la Puente. 2020. “Financing Nature: Closing the Global Biodiversity Financing Gap.” The Paulson Institute, The Nature Conservancy, and the Cornell Atkinson Center for Sustainability, Chicago, IL.

<sup>viii</sup> OECD (Organisation for Economic Co-operation and Development). 2021a. Biodiversity, natural capital and the economy. OECD Environment Policy Papers, No. 26, OECD Publishing, Paris, <https://doi.org/10.1787/1a1ae114-en>.

<sup>ix</sup> Convention of Biological Diversity. 2021. Estimation of Resources Needed for Implementing the Post-2020 Global Biodiversity Framework. CBD/SBI/3/5/Add.2/Rev.18 December 2021