

# BIODIVERSITY: A NEW CHALLENGE FOR SUSTAINABLE FINANCE

Note written by Jean-François Pons, ALPHALEX – CONSULT GEIE

## INTRODUCTION

The reduction in the number of living species on Earth, deforestation, the degradation of the oceans and overfishing are examples of the degradation of biodiversity and ecosystems.

Protecting and restoring biodiversity is one of the 17 United Nations Sustainable Development Goals published in 2015. It is also one of the six goals from the European Union Green Deal, alongside the climate and other environmental objectives (circular economy, fight against pollution, etc).

For the financial sector, this represents a new challenge that will need to be met despite its specific difficulties.

## 1. BIODIVERSITY CONSERVATION IS AN INCREASINGLY PROMINENT POLITICAL PRIORITY

The preservation and restoration of biodiversity was the theme of two major international events last year:

- The International Union for Conservation of Nature (IUCN) World Conservation Congress, which was held last September in Marseille (France) and was attended by many political leaders from across Europe;
- COP 15 in November 2021, which brought together the United Nations members in Kunming under the Chinese Presidency in an attempt to make joint progress, similar to the consecutive COPs on the climate (such as COP 21, which led to the Paris Agreement, or COP 26 in Glasgow).

These two gatherings presented a worrisome picture of the biodiversity situation around the world and underlined the economic and social risks involved.

The first event gave rise to interesting statements describing the issues at hand and outlined possible solutions, particularly for businesses. They included the development of tools for business impact assessments on biodiversity in order to set targets and define relevant policies.

The Kunming conference resulted in a statement committing to halt the degradation of biodiversity and to begin restoring it by 2030. It also defined 17 general objectives to be included in the new World Conservation Code. These 17 objectives will be further discussed in the second part of the Kunming Conference — which was scheduled for April-May 2022, but has been deferred to another date that has not yet been set.

## 2. BIODIVERSITY DEGRADATION HAS IMPORTANT ECONOMIC AND FINANCIAL CONSEQUENCES

At a microeconomic level, we understand that certain activities are adversely affected by biodiversity degradation. For example, the extinction of an essential plant in perfume production, the disappearance of wild animals in regions where this was a source of tourism, the reduction of fish stocks, the pollution of a coastal tourist site, etc.

**The Dasgupta Report (1), commissioned by the UK government in the run-up to COP 26 in Glasgow, describes an alarming situation that includes macroeconomic and financial considerations:**

- “Nature [...] is an asset, and we have failed to manage our natural capital in a manner that maintains resilience and productivity.”
- The value of this asset is declining, which means that instead of generating income, it will increasingly generate additional costs.
- This trend must be reversed: “The quantity and quality of our stocks of natural assets need to increase significantly.”
- Finally, biodiversity loss also contributes to global warming: deforestation and ocean degradation, for example, reduce their carbon storage capacity.

A recent study (2) by Swiss Re, one of the world’s largest reinsurance groups, estimated the value of biodiversity at \$33 trillion per year — slightly less than the combined GNP of both the United States and China. Another worrying figure is that 20% of countries have fragile ecosystems affecting at least 30% of their surface area.

The Dasgupta Report’s recommendations include transparency in production chains, accurate measurement of the direct and indirect costs of degradation, and increased funding to protect and restore biodiversity.

**Funding for biodiversity conservation and restoration needs to increase significantly:**

- **It is currently around \$100 billion per year**, or 0.1% of global GNP, primarily from the public sector.
- But just 30% of protected areas on land and at sea would require \$140 billion each year.
- In a report published in April 2020 (3), the OECD estimates that **the annual funding requirements linked to the preservation and restoration of biodiversity range from \$722 billion to \$967 billion.**

### 3. FOR THE FINANCIAL SECTOR, THIS REPRESENTS A NOVEL CHALLENGE WITH DISTINCT DIFFICULTIES, BUT ONE THAT INSPIRES AN INCIPIENT MOBILIZATION

Faced with the growing economic and financial risks of biodiversity loss, the financial sector has a role to play — in much the same way as it is increasingly doing for climate and other environmental and social objectives.

#### 3.1 Firstly, it should include biodiversity as a regular reporting topic

The financial sector is increasingly doing so for climate or other ESG (Environmental, Social and Governance) objectives, but not without difficulties.

Policymakers and financial regulators will ask financial institutions to assess their financial risks relating to nature and their own impacts on nature. Central banks and financial supervisors are starting to assess these risks, although they have so far focused on climate change.

It should be recalled that **financial investors in the European Union already have to publish data on the sustainable aspects of their assets**, starting with those relating to climate change. This is required by the Sustainable Finance Disclosure Regulation (SFDR) (4) since March 2021. That said, investors find it difficult to collect the necessary data from companies that they finance (particularly SMEs) and suffer from a lack of harmonization in standards and methodologies, including for assessing portfolio alignment with the Paris Agreement objectives. It is likely that there will also be difficulties with collecting and processing meaningful data in the field of biodiversity.

**In France, financial investors — who had already initiated climate-related reporting — will have to do the same in the field of biodiversity.** In fact, the French government's decree of 27 May 2021 (5) includes biodiversity in the annual report to be published by investors in accordance with the 1975 energy transition act (Article 173), in addition to the information that is already compulsory with regard to the climate. From 2022, financial investors will have to measure their alignment with the objectives of the Convention on Biological Diversity, analyse their portfolio's impact (positive and negative) on biodiversity, and publish the resulting biodiversity footprint.

At EU level, **biodiversity is the 6th objective from the Taxonomy on Sustainable Finance.** The Platform on Sustainable Finance, which is advising the European Commission, published a first document on the four objectives not related to the climate in August 2021 for consultation (6). This document recalls the objectives of the EU Biodiversity Strategy and, to give guidance on the significant contributions linked to this Strategy, provides a questionnaire to be applied to the economic activities that will be considered.

### 3.2 An increase in private funding is also necessary, but will need to have a specific *modus operandi*

**The funding of projects to preserve and restore biodiversity is more complicated than for conventional investment financing:**

- For example, the regeneration of a marine protected area — unlike a traditional investment project — does not involve a private owner of the asset in question; the sea is a public good and therefore requires the involvement of public authorities.
- This regeneration must also be accompanied by the further development of profitable activities to attract private capital, alongside public or NGO funds which are of a limited nature.
- It should also result in job creations to compensate for the inevitable job losses in sectors linked to polluting activities, over-exploitation of the seabed, etc. Opportunities for job creations include areas such as recycling, efficient resource exploitation (e.g. algae) and responsible tourism.
- To guarantee the environmental, social and financial security of such complex projects, it is ideal to build public-private partnerships that also involve NGOs and specialists in the field.
- There is also often a need to support small and highly localised projects, which should be clustered to make their financing easier. The World Bank's intervention in Seychelles in 2018 involving a \$15 million private finance package is one such example.

### 3.3 Financial actors are beginning to mobilise on the theme of biodiversity

**The Finance for Biodiversity Pledge (6)** was launched in September 2020 at the UN Nature for Life Conference. In one year, this commitment saw the number of signatories double to 55 financial institutions, with a combined USD 9 trillion of assets under management. In March 2021, some thirty of these institutions created the **Finance for Biodiversity Foundation** to strengthen their collective work. It concerns the pooling of different methodologies for measuring biodiversity among investors. In addition, investors must adopt a policy for proactive dialogue with the companies in which they are shareholders so as to reduce their negative impacts. Signatories must also assess the biodiversity impacts of their portfolios and set targets to both increase positive impacts and decrease negative ones.

There are also **some interesting examples of targeted financing:**

- Specialised funds launched by numerous financial players (World Bank and other public development banks, private banks, asset managers), such as the Global Fund for Coral Reefs;
- Green bonds linked to biodiversity, "blue bonds" which follow the same rules as "green bonds" but for positive impact investments in the maritime sector, etc.

**Several financial actors already publish information on their biodiversity actions alongside their annual reports.**

Quantitative indicators for measuring the biodiversity footprint of investments are starting to be tested. For example, several French financial investors use MSA.km<sup>2</sup> as a unit of measurement, which is equivalent to one km of fully developed land (without any biodiversity present).

**Many financial players are refusing investments that would result in the degradation of biodiversity.**

A Novethic Market Data study (7) examined such exclusions by the 429 European green funds. As a result, some 100 funds exclude one or more themes due to environmental damage, representing a total of €85 billion in assets: for instance, 59 funds exclude palm oil on the grounds of deforestation, destruction of animal habitats and human rights violations, while 46 funds exclude GMO cultivation. Some European banks also refuse to finance activities linked to soja or beef in Brazil because of deforestation.

**Several banks and asset managers have entered into regular dialogue with their clients (notably the agro-industry) over biodiversity.**

Financial actors and some non-financial corporates are also involved in **the development of an ecosystem of high-tech firms, startups and specialist consultants, as well as investment in Research and Development**, notably for ensuring traceability and reducing the negative impact on biodiversity.

Lastly, **the creation of the Taskforce on Nature-related Financial Disclosures (TNFD)**, which — similarly to the Taskforce on Climate-related Financial Disclosures (TCFD) — **will provide financial and non-financial companies with a reporting framework** to assess, manage and report their dependencies and impacts on nature, identify their risks, and thus contribute to the redirection of financial flows in a manner that ensures positive outcomes for nature. The Taskforce includes many representatives from the financial sector.



## CONCLUSION

The inclusion of biodiversity in sustainable finance stems from the severity of its situation in the world and the need to actively preserve and restore it, as recognised not only by scientists, but also by economists and financiers alike.

This is a new challenge for the financial sector, which already faces the issue of integrating climate change along with the difficulties of collecting data and assessing impacts and trajectories.

Major financial players are starting to mobilise through a number of concrete actions: increase in funding (with innovative public-private partnership), in dialogue with non-financial corporates, in regular reporting and collective commitments, such as the Finance for Biodiversity Pledge and the Taskforce on Nature-related Financial Disclosures.

For this mobilisation to succeed, it will have to be integrated within a partnership with public authorities (particularly for forests and for marine and coastal activities) and local stakeholders, as well as NGOs and development banks in the Global South.

It will be essential to exchange data, methods and good practices as widely as possible between financial actors and non-financial companies, as well as with the public sector. An essential element will be to identify common measurement and evaluation methods. Given that the field is particularly broad, it will be necessary for the public and private sector to agree on progressive priorities and agendas in order to avoid fragmentation and wasted efforts.

## BIBLIOGRAPHY

- (1) "The Economics of Biodiversity: The Dasgupta Review", February 2021, p. 1.
- (2) Patrick Raaflaub, "Do we know the true value of biodiversity – and the cost of losing it?": Swiss Re. October 2021.
- (3) OECD, A Comprehensive Overview of Global Biodiversity Finance, April 2020
- (4) Regulation (EU) 2019/2088 of the European Parliament and of the Council of 27 November 2019 on sustainability-related disclosures in the financial services sector
- (5) Decree no.2021-663 of 27 May 2021
- (6) Platform on Sustainable Finance Technical Working Group: Taxonomy pack for feedback, August 2021
- (7) Finance for Biodiversity Pledge, 2021.
- (8) CP Novethic "Une centaine de fonds durables appliquent des exclusions liées à la biodiversité", September 2021.