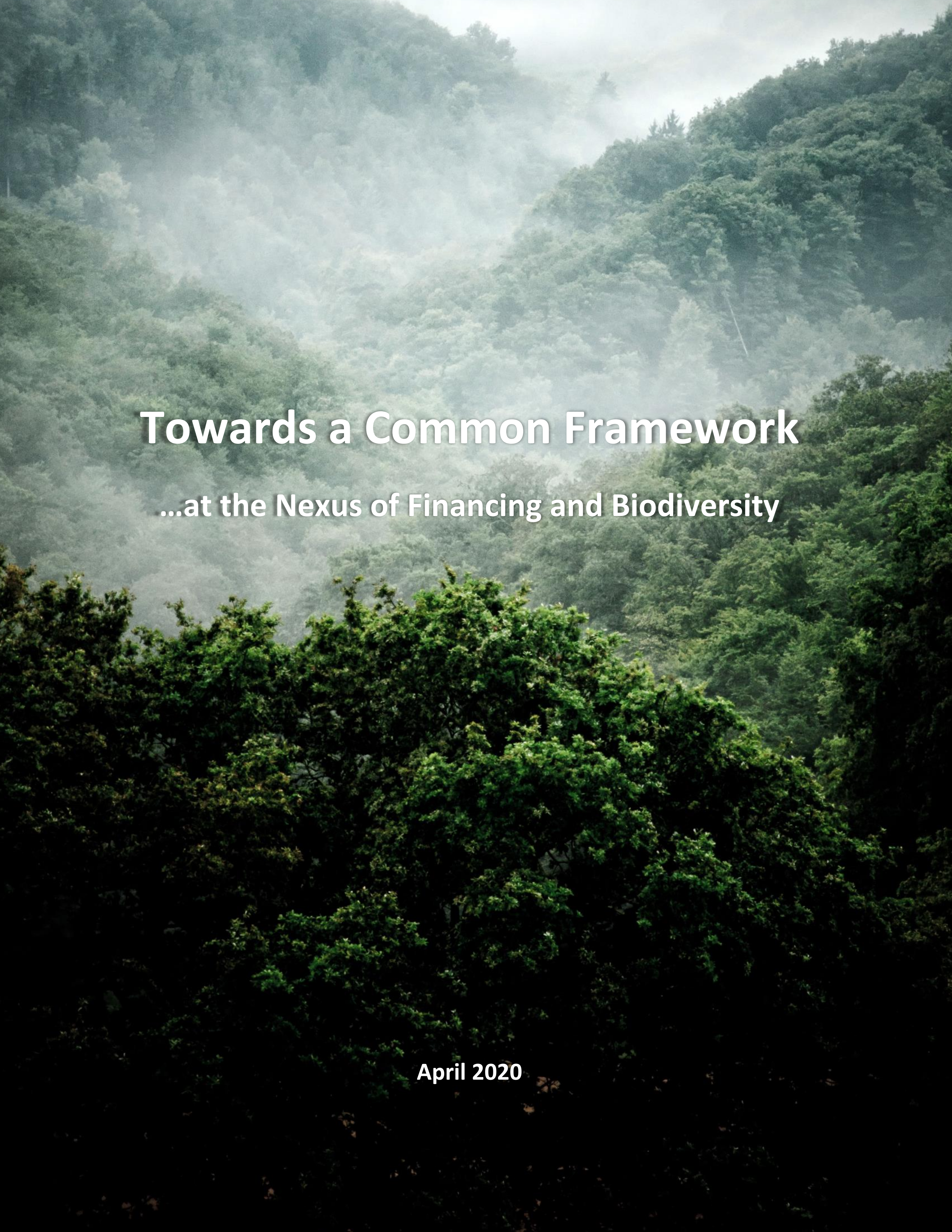

Towards a Common Framework

...at the Nexus of Financing and Biodiversity

April 2020

A common framework of systemic analysis with the purpose of identifying how to internalise biodiversity in financing and to enable dialogue between initiatives working in the space.

Comments are welcomed.

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[1] Note that the contributions of Geraldine Ang and Simon Buckle do not necessarily reflect the views of the OECD or its members

Biodiversity matters: it is fundamental to human survival, but not considered material to most financing decisions

Financing drives the global economy, and largely determines what and how we produce and consume, and thus our impact and dependency on the planet. Overwhelmingly, biodiversity impacts and dependencies are not taken into account in most financing decisions. This is true for private investors seeking to maximise risk-adjusted, financial returns. Moreover, it is also true for governments, business managers and private citizens. As a result of the lack of integration of biodiversity into financing decisions, our global economy is consuming and destroying the biodiversity that we depend upon for our survival. While specialised 'conservation financing' is welcome, it will never bridge the gap between current rates of biodiversity loss and restoration.

Biodiversity conservation is therefore fundamentally about making biodiversity material to financing decisions.

The growing focus on the nexus of finance and biodiversity has the potential to catalyse ambitious action, but could confuse, distract and mis-prioritise

A growing recognition of the importance of the nexus and the interconnectedness of finance and biodiversity, has precipitated a large number of analyses and initiatives. Some are focused on individual public financing mechanisms, some on the cost of inaction, and some on particular aspects of biodiversity, such as oceans, forests and large-scale food value chains such as soya and beef. Such breadth of scope, innovation and diversity of approach is to be welcomed. However, there is a danger that it seeds confusion, unhelpful disputes and, ultimately, unproductive competition between approaches and initiatives. In addition, the level of awareness and commitment to consider biodiversity in financing decisions remains low.

A common framework for understanding the nexus of finance and biodiversity is therefore needed

Our modest purpose in preparing this brief is to encourage a common, systemic framework in considering the nexus of biodiversity and finance. Today's conversation about biodiversity loss and its primary driver, the global economy, remains dangerously immature and inadequate. A common framework can emphasise the systemic challenge and systemic change, and how to advance such change, in order to overcome the fragmented and increasingly competitive, on-going efforts to achieve transformational change across mainstream finance.

The need is not for everyone to agree on the 'right' answer. That would, in any case, be inappropriate given the many aspects of biodiversity and financing, with its diverse contexts and interests. Rather, what is needed is a common framework. This would allow for greater agreement on key levers for change.

A common framework will be particularly helpful in the crowded and noisy run up to the Convention on Biological Diversity (CBD)'s 15th meeting of the Conference of the Parties (COP15) in late 2020, and in the context of the 'Nature Super Year'.

Biodiversity's perceived immateriality in financial decisions is a fundamental weakness of the current system

That biodiversity is immaterial in most of today's financial decisions is not a matter of neglect or error. Modern financing, and the business models in which it invests, has evolved as a chain of specialised parts, designed to ignore in practice what happens at the end of the pipeline, where, for example,- virgin forests make way for plantations. At the top end of the pipeline, it narrowly defines the interests of the owners of the world's financial assets, and at the bottom end, it marginalises citizens affected by changes in the natural environment, who are not (yet) empowered to fully exercise their legal rights. It also creates disincentives for local communities to protect biodiversity and ecosystem services. It fully ignores the young and future generations.

Indeed, for investors in specific sectors, financial returns actively depend on continuing free or underpriced access to ecosystem services and extraction of natural resources. The current system externalises the negative impacts of businesses on biodiversity. Governments are equally culpable. While being guardians of the public interest, they fail to deal with the longer-term consequences of their short-term policies and political interests. Citizens, as consumers, taxpayers, voters and investors, largely choose to turn a collective blind-eye, or are too far removed from and disempowered with regards to the use of their own money.

Biodiversity's perceived immateriality in financial decision-making is a system-level failure.

Climate change is entwined with, yet not a template for, financing and biodiversity

Action to align finance with climate goals, likewise, requires systemic changes in finance and its relationship with the real economy. Addressing climate change is part of the agenda of protecting biodiversity, and *vice versa*. Biodiversity loss is driven by climate change, in addition to land-use change, over-exploitation of natural resources, pollution and invasive alien species. Conversely, conserving, sustainably using and restoring biodiversity, is vital to achieve climate mitigation and adaption and disaster risk reduction. Loss of biodiversity and lack of action to restore it makes addressing climate change far more difficult. That said, there is a growing risk that efforts to tackle climate change are being seen as sufficient or 'as much as can be managed right now'.

No collective dialogue on the joint narrative of climate and biodiversity has taken place. This is reflected in the institutional arrangements, which are separated in government, in finance and in business. Meanwhile, political and economic resources are largely directed to climate change.

We can and must learn from the recent experience of action and inaction on climate, while recognising that there are some key differences. Carbon-emitting assets, such as coal fields and oil refineries, are the primary source of the public bad that is carbon dioxide. They are owned and can be priced through market valuation, allowing more easily for markets to react to policy measures. No analogous set of assets are being exploited to the detriment of biodiversity with homogenous and global effect. No equivalent set of prices find their way into market valuation. A key difference is the many and localised pressures on biodiversity. The way in which natural habitat, fertiliser and pesticides are being converted into domesticated animal biomass in ever-increasing amounts, or biomass in oceans is being extracted industrially from natural food chains, is not close in kind to the extraction and burning of fossil fuels. Much as it took a leap of imagination to make markets incorporate carbon, it takes another leap of imagination to see how they will incorporate biodiversity, to resolve the tension between unconstrained markets and natural processes that underpin survival. The measures in place to tackle climate change may not be the measures that will solve the biodiversity crisis.

Financial owners need metrics that reflect material liability

Measurement can make a major contribution to making financial markets work. However, metrics depend on a complement: material liability. Materiality does not inherently exist - a fact that needs to be explained more loudly and convincingly.

Risk-based metrics for investors, notably, are 'lagging', capturing at best what is already material. They become useful when risks count, once the circle is closed, by generating demand for biodiversity protection and restoration.

Indeed, metrics can only play a catalytic role if they are part of a process of 'creating' rather than merely seeking to demonstrate materiality. That is, if the metrics and standards make the benefits and liabilities of biodiversity more meaningful in the minds of decisionmakers.

The key is to create materiality in financing decisions that impact biodiversity

It is therefore not a matter of demonstrating, but instead of creating biodiversity's materiality in financial decision-making. Beyond physical risk, climate action tells us that materiality is a societal rather than a nature-based phenomenon. Indeed, even physical risks are often mediated through societal constructs in determining their impact on finance. Such constructs can be created by citizens making their views count as consumers, by demanding policies that variously penalise or incentivise those that impact biodiversity, and by ensuring there are consequences for those companies that fall short of expectations. Under current laws, corporate governance, judges and regulators can only act where the risk is material, which is a fact-based assessment. Material liabilities can be introduced by means including law, regulatory policy, broadening of fiduciary duties, and demonstrating the majority interests of pension members:

- Governments have the power to create financial materiality through formal levers of control and through moral suasion. They can create and defend rights, tax, subsidise, oblige and prescribe.
- Shareholders and lenders have some powers of control over corporations. They can pass resolutions on policy, write covenants, demand information and appoint directors.
- Company directors and trustees have direct involvement in the decisions of their organisations. They have wide executive powers to lay out the vision and objectives, set policy, design processes and allocate resources.
- Consumers and organisations representing groups of consumers and citizens can apply pressure. They can switch supplier, demonstrate and lobby.

An effective common framework considers feedback effects that make biodiversity count

An effective common framework describes the actors, points of control and feedback loops which internalise impacts, and the political economy of financing to make biodiversity count, namely:

- Values, so that established cultures of behaviour result in decisions that incorporate impacts on nature and biodiversity. This helps to overcome indifference or complicity in biodiversity loss and activates citizens and consumers, both individually and collectively, in biodiversity-sensitive financing decisions.
- Influence, so that influence is wrested away from concentrated interest groups who benefit from the destruction of nature. Consumers, corporate managers and financiers alike may not value nature and biodiversity sufficiently to drive biodiversity value into financial decision-making. These views are reflected and amplified in the media and subsequently in politics. Influence should be balanced and reflect the values of society.
- Rights, so that the public good character of biodiversity is embedded in national and international legal instruments, and so that entitlements to services are clarified, which will underpin more effective markets.
    - It is harder to establish new rights than to enforce existing ones. Goods and services, which are currently missing because they have already been lost, are more likely to be ignored and neither measured nor recorded. Weak rights for consumers of public goods may mean strong *de facto* rights for others.

- Governance, so that the rules governing finance, at the enterprise, product and market level, and at national and international levels, take biodiversity into account.
    - Many factors contribute to weakened or misaligned governance. Most obvious is the interest of incumbents, whose business or political standing depends on a world where biodiversity is not counted.
- Efficiency, so that capabilities of data and institutional structures are in place to support biodiversity-sensitive markets and financing decisions.
    - Data may not be readily available or might be too costly or not calibrated to the needs of financial decision making. New capabilities are costly to build and are often resisted by citizens, banks and ministries of finance.

Replace the absence of understanding the value of biodiversity, with agreement on principles that carry value

Collective action is underpinned by a shared understanding of value. There is a lack of clarity about the value of biodiversity. This refers to the intrinsic value of biodiversity, not in narrow economic or financial materiality terms, where the value is low relative to metrics such as Gross Domestic Product (GDP). Value can be anchored and reflected in principles such as: 'no net loss'; 'maintaining capital stock per capita'; having a 'duty of care'; and applying the 'precautionary principle' to the continued existence of species, the protection of wilderness, and the management of ecosystems within safe limits. A set of principles may be a useful way to articulate a common understanding of value.

Further decisions can appeal to the foundational principles of value, making it easier to build a consistent set of behaviours, rights and governance.

Any meaningful proposal needs to consider how the financial system can best be evolved

The nexus between finance and biodiversity has to be moved with urgency towards a systemic solution. It is not enough for an analysis or initiative or recommendation to claim to 'make a difference'. Any serious call for action will demonstrate how and when it would shift the system dynamics convincingly in the right direction, starting by making clear what the inherent value of biodiversity is, possibly expressed through principles. Moreover, any serious call for action will highlight potential risks and consequences and how these might be observed and dealt with.

All analyses, initiatives and recommendations should adopt a common framework of systemic analysis

There would be considerable value to the many laudable and important actions being taken in adopting a common framework. What would it mean for the outcome if one were to focus exclusively on risk-based metrics for investors, for example, or on a limited financial stability lens in considering action by central banks? Similarly, what would be the inter-dependencies between such initiatives and the need for shifts in public opinion, shareholder rights or adjustments in public procurement criteria?

Encouraging key initiatives to situate their efforts in a wider framework would enable greater comparability and more effective debate and choices. Moreover, it would discipline everyone to more fully explain their findings, insights and proposals within a fuller, systemic view of what needs to be changed, and how. Whether it is this framework being proposed here that is adopted is of course up for debate. What is important is that the debate gets moving, and it is hoped that others will read this contribution and build on it to accelerate change that enables biodiversity and finance to run side by side into a better/safer future. The race is on!