CITY OF LONDON | THE GLOBAL CITY | pwc

A global centre for nature finance

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Contents

Foreword

Chris Hayward

Policy Chairman,
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The natural world is essential to our livelihoods and wellbeing. But at present, its value is not fully recognised by the global financial system. As custodians of a world leading financial centre, the City of London Corporation recognises the pressing need for financial and professional services to address the global environmental challenges we face today.

Our ambition is for the City of London to become the one-stop-shop for countries and companies looking for capital and expertise to meet their climate goals. Failure to incorporate nature into financial decision-making risks the future vibrancy of the global economy and it would see us fail to recognise our most powerful tool in the fight against climate change.

This report showcases the transformative potential of scaling up investments in nature. By leveraging financial resources, expertise, and innovation, we can harness the power of nature to tackle climate change, preserve biodiversity, and build more sustainable communities. From mitigating climate change and enhancing natural carbon sinks to protecting ecosystems and safeguarding biodiversity, investment in nature offers both immediate and long-term value.

Furthermore, scaling up investment into nature can foster job creation, stimulate economic growth, and improve public health and well-being. The City of London Corporation believes that by aligning financial markets to recognise the value in nature, we can address environmental challenges and unlock new business opportunities to drive sustainable development.

The purpose of this report is to develop a vision and roadmap for the UK as a global capital for nature finance. Our recommendations seek to inform public and private sector action, as we work together to recognise the risk posed to the economy by nature and biodiversity loss, and the opportunity for the UK to be at the centre of the financial flows required to bridge the global funding gap for nature.

I am grateful to the PwC team for their expertise and commitment to this report and would like to thank the Green Finance Institute for contributing case studies and providing their valuable insights. I hope this report serves as a catalyst for meaningful action, inspiring governments, businesses, and individuals to prioritise and increase investments in nature as a cornerstone of sustainable development.

David Croker

Financial Services Sustainability Lead,
PwC UK

The natural world provides the air we breathe, the water we drink and the essential goods and services that enable our societies and economies to thrive. A recent report by PwC's global Centre for Nature Positive Business has revealed that over half the world's GDP (USD 58 trillion) is highly or moderately dependent on nature.[1] Despite this, human impact on nature is increasingly putting our planet's vital ecosystem goods and services under pressure, threatening the very foundations of our economies, livelihoods, food security, health and quality of life worldwide.

In December 2022, leaders from across the world came together in Montreal to agree on a new Global Biodiversity Framework (GBF) paving the way for a vision of living in harmony with nature. The GBF highlights the urgent need to close the biodiversity finance gap, leveraging private finance and blended finance instruments alongside innovative schemes such as payment for ecosystem services, green bonds and biodiversity credits.

Building on the GBF, the UK's Green Finance Strategy[2] acknowledges the need for a "step change in levels of investment" to enable a global transition to a resilient, nature-positive, net zero economy. The strategy also highlights the huge opportunities for the UK's financial and professional services industry in supporting this transition.

In collaboration with the City of London Corporation and Green Finance Institute, this report showcases the unique position of the UK to drive nature-related investment and to secure its place as a world leader in green finance. We explore the multiple opportunities and challenges to scaling nature finance and present a vision and roadmap for the UK to position itself as a global centre for nature finance.

I am thankful to the multiple organisations and individuals who contributed to the development of this report and hope it provides a useful launchpad to drive meaningful action, foster collaboration and harness the opportunities inherent within our transition towards a nature-positive future.

1. PwC (2023) Managing Nature Risk: From Understanding to Action
2. HMG (2023) Green Finance Strategy

Executive summary

Halting and reversing the depletion of the natural environment will require a coordinated response at a global scale, in order to solve a vast series of inherently local and interconnected crises. The 2022 Kunming-Montreal Global Biodiversity Framework (GBF) agreement was deemed a watershed "Paris moment for nature", compelling businesses and economies worldwide to take action to protect and restore the ecosystems upon which they rely. Businesses and financial institutions in the UK and across the world are becoming increasingly aware of nature-related risks within their supply chains and the emerging regulatory, consumer and investor response.

The City of London Corporation and PwC, with support from the Green Finance Institute have collaborated to outline our vision for an innovative and world leading global centre for nature finance that supports the ambition of the GBF. This report evaluates the readiness of the UK to take on this role and the required next steps. Under the themes of "financing nature" and "integrating nature into the financial system", the report presents a roadmap for the UK to build on its position as a leading centre for green finance and become a global centre for nature finance.

The case for action on nature

Global demands and pressures on nature have dramatically increased, posing significant economic risks as companies rely directly and indirectly on nature's resources and ecosystem services. By 2030 nature loss could cause global GDP reductions of £2.1 trillion each year.[3] To halt biodiversity loss, limit global average temperature rises to 1.5°C, and achieve land degradation neutrality, annual investments in nature-based solutions will need to more than triple by 2030.[4]

This finance gap represents a clear opportunity for investors, with several factors pointing to the long-term value of investing in nature-related projects. This includes investing defensively to safeguard existing businesses and revenue streams, but also to leverage the opportunities from changing demands from consumers for nature-positive goods and services.

The UK as a Global Centre for Nature Finance

The UK's existing strength as a global leader in green finance positions it strongly to develop into a global centre for nature finance, for example:

- London currently sits at the top of the Global Green Finance Index (GGFI), while Edinburgh has climbed eight places, from 22nd to 14th.[5]
- In England alone, there are an estimated 70,000 people working in the fields of conservation, environment and adjacent areas.[6]
- The UK is the world's largest centre for international bond issuance and trading, and has a strong base of highly engaged ESG investors; approximately £5tn of investment fund assets managed in the UK are done so using ESG principles.[7]
- The UK is a leader on sustainability regulation; it was an early adopter of a carbon emissions trading scheme and the first G20 country to announce that it would make disclosures in line with the Task Force on Climate-related Financial Disclosures (TCFD) recommendations fully mandatory across the economy.

The current nature finance ecosystem in the UK benefits from existing expertise in finance and innovation, alongside the strength of its supporting legal and regulatory environment. This ecosystem is summarised with a market-mapping diagram in Section 3 "The current state of UK nature finance", including a depiction of the capital flows for nature and the enabling environment of standard setters, industry coalitions and providers of trading infrastructure.

By 2030 nature loss could cause global GDP reductions of

£2.1tn[3]

3x

current annual investments in nature-based solutions needed by 2030[4]

70,000

people in England estimated to be working in the fields of conservation, environment and adjacent areas[6]

3. WEF (2022) Scaling Investments in Nature: The Next Critical Frontier for Private Sector Leadership. (original value reported in US$)
4. United Nations Environment Programme (2022) State of Finance for Nature
5. Z/Yen (2023) The Global Green Finance Index 11
6. HM Government (2023) Environmental Improvement Plan 2023
7. The Investment Association (2022) Investment Management in The UK 2021-2022: The Investment Association Annual Survey

Recommendations for financing nature and integrating nature into the financial system

Despite this emergent ecosystem, the current enabling environment in the UK falls short of the action needed to overcome some of the key barriers to scaling nature finance with integrity.

Financing nature

To mobilise finance for nature, the UK Government should consider establishing sector-specific targets and roadmaps for nature protection and restoration. These targets, aligned with commitments under the GBF, are pivotal in signalling a commitment to a nature-positive future, and providing certainty to investors and project developers alike.

Innovation will be required from all parts of the nature finance ecosystem. For example, the UK Government could leverage existing blended-finance models for climate and explore financial incentives to foster a pipeline of investible opportunities. Innovative mechanisms for valuing and financing nature will be required, such as the development of high-integrity nature credit markets at pace. This innovation must be matched by a willingness from UK financial institutions - especially those managing large volumes of patient capital - to test out and further develop the growing suite of innovative new financing mechanisms for nature. It is also essential that indigenous peoples and local communities are consulted throughout the development of this market, and that its progression feeds into social and economic benefits for these groups.

Integrating nature into the financial system

Integrating nature into the UK financial system will require both a bottom-up and top-down approach.

At an organisational level, transparently disclosing decision-useful information about nature-related impacts, dependencies, risks and opportunities will facilitate the mainstreaming of nature into business and financial decisions. The UK Government can create expectations and requirements to support this bottom-up integration, for example through the regulation of nature-related disclosures and by integrating nature considerations into transition planning requirements.

To fully integrate nature into the UK financial system, nature-related financial risks should be better understood and assessed at a macro level. Supported by a growing commitment to nature-related disclosures, appropriate supervisory measures which support the stability and viability of the sector should be implemented to safeguard the UK's long-term sustainable growth.

The report recommendations are summarised in the following diagram. These recommendations are fully explained in Sections 4 and 5 of the report, along with accompanying sub-recommendations for each of the headline points presented on the following page.

Summary of report recommendations

	RECOMMENDATION	APPLIES TO	UK MATURITY*	TERM**
Financing nature	**1. Signalling & policy certainty (Page 19):** Develop sector-specific targets and roadmaps for nature restoration and protection and provide clarity on how the UK will operationalise its key commitments under the Global Biodiversity Framework.	Government		6–12 MONTHS
Financing nature	**2. Project pipeline creation (Pages 20–21):** Support the development of a pipeline of sufficiently large investible opportunities, including by accelerating the supply of supporting monitoring, reporting and verification products and services.	Government; Financial & professional services sector		3+ YEARS
Financing nature	**3. Concessional capital and financial guarantees (Page 22):** Develop and utilise solutions that de-risk nature-related investment opportunities.	Government; Financial & professional services sector		1–3 YEARS
Financing nature	**4. Facilitate UK nature credit markets (Pages 23–26):** Lead the way in developing robust and high integrity nature credit markets.	Government; Regulator; Financial & professional services sector		3+ YEARS
Financing nature	**5. Develop long-term nature investment strategies (Page 27):** Financial institutions should utilise the growing suite of innovative market tools to invest in nature at scale.	Financial & professional services sector		1–3 YEARS
Integrating nature into the financial system	**6. Build on the UK's already world leading regulatory architecture for sustainability (Pages 29–34):** Seek out opportunities to strengthen or accelerate the deployment of nature-related regulation that supports the UK Government's Roadmap to Sustainable Investing, including encouraging businesses to voluntarily align their reporting with the Taskforce on Nature-related Financial Disclosures (TNFD) Framework and incorporating the anticipated Transition Plan Taskforce (TPT) guidance on nature.	Government; Regulator		6–12 MONTHS
Integrating nature into the financial system	**7. Advance Central Bank oversight (Page 35):** The Bank of England and Prudential Regulation Authority (PRA) should consider the supervisory steps needed to ensure that the safety and soundness of regulated firms are not impacted by nature-related financial risks, while also securing an appropriate degree of protection for insurance policyholders from those risks.	Regulator		1–3 YEARS

Government Regulator Financial & professional services sector

* **UK maturity** provides a qualitative assessment of how well developed each recommendation area already is in the UK against the level of maturity required from a global centre for nature finance.

** **Term** denotes the indicative time period it might take for the UK to reach the level of maturity required from a global centre for nature finance for each respective recommendation area.

Section 1
The case for action on nature

Global demands and pressures on nature have dramatically increased. Over 75% of the world's land surface has been significantly altered by humans since the Industrial Revolution; combined with similar degradation of oceans and wetlands, this is threatening around a million plant and animal species.[10]

This poses significant risk given that every company depends on nature to some extent - nature provides resources, such as wood and water; nature's services include protection, as when a wetland mitigates floods, and purification, as when trees remove pollutants from the air; and nature supports production and livelihoods by various means, such as providing fertile soils for planting crops and insects for pollinating their flowers. It is therefore unsurprising that nature loss by 2030 could cause global GDP reductions of £2.1 trillion each year.[11]

10. IPBES (2019) The global assessment report on biodiversity and ecosystem services: summary for policymakers
11. WEF (2022) Scaling Investments in Nature: The Next Critical Frontier for Private Sector Leadership. (original value reported in US$)

Finance for nature is falling far short of the levels required to reverse these trends. The estimated funding gap for climate adaptation and resilience finance, biodiversity and nature-based solutions is £260-484 billion per year up to 2030.[12]

In the UK, the Green Finance Institute found in 2021 that there is a £44 - 97 billion finance gap which needs to be met in the next 10 years to deliver nature-related goals[13]. Meanwhile, global investment in nature-based solutions in 2022 from public funds was estimated to have been £105 billion, compared with £21 billion from private funds[14]. The relatively small share of private finance reflects the novelty and perceived returns and associated risks from nature-related investments, as described in Table 1 which outlines some of the key barriers for scaling private finance for nature.

This finance gap represents a significant opportunity for investors. Several factors point to the long-term value of investing in nature-related projects. This includes investing defensively to safeguard existing businesses and revenue streams, but also to leverage the opportunities from changing demands from consumers for nature-positive goods and services. For example, a 2022 UN climate change high level champions report concluded that "developing and tapping solutions for a net zero, nature-positive, resilient food system... could generate up to US$4.5 trillion of new business opportunities annually by 2030". To bring these opportunities to fruition, an enabling environment must be created through supportive policies and regulation alongside the development of bankable opportunities that lenders and investors can understand.

There is a global commitment to protect nature as demonstrated by the landmark Kunming-Montreal Global Biodiversity Framework (GBF). Heralded as the "Paris Agreement for Nature", the GBF aims to protect 30% of the world's land and sea, and restore 30% of degraded ecosystems by 2030. It also seeks to catalyse significant finance for nature with Target 19 seeking to mobilise at least $200 billion per year by 2030. Governments have an important role to put in place the legal, administrative and policy measures to facilitate this.

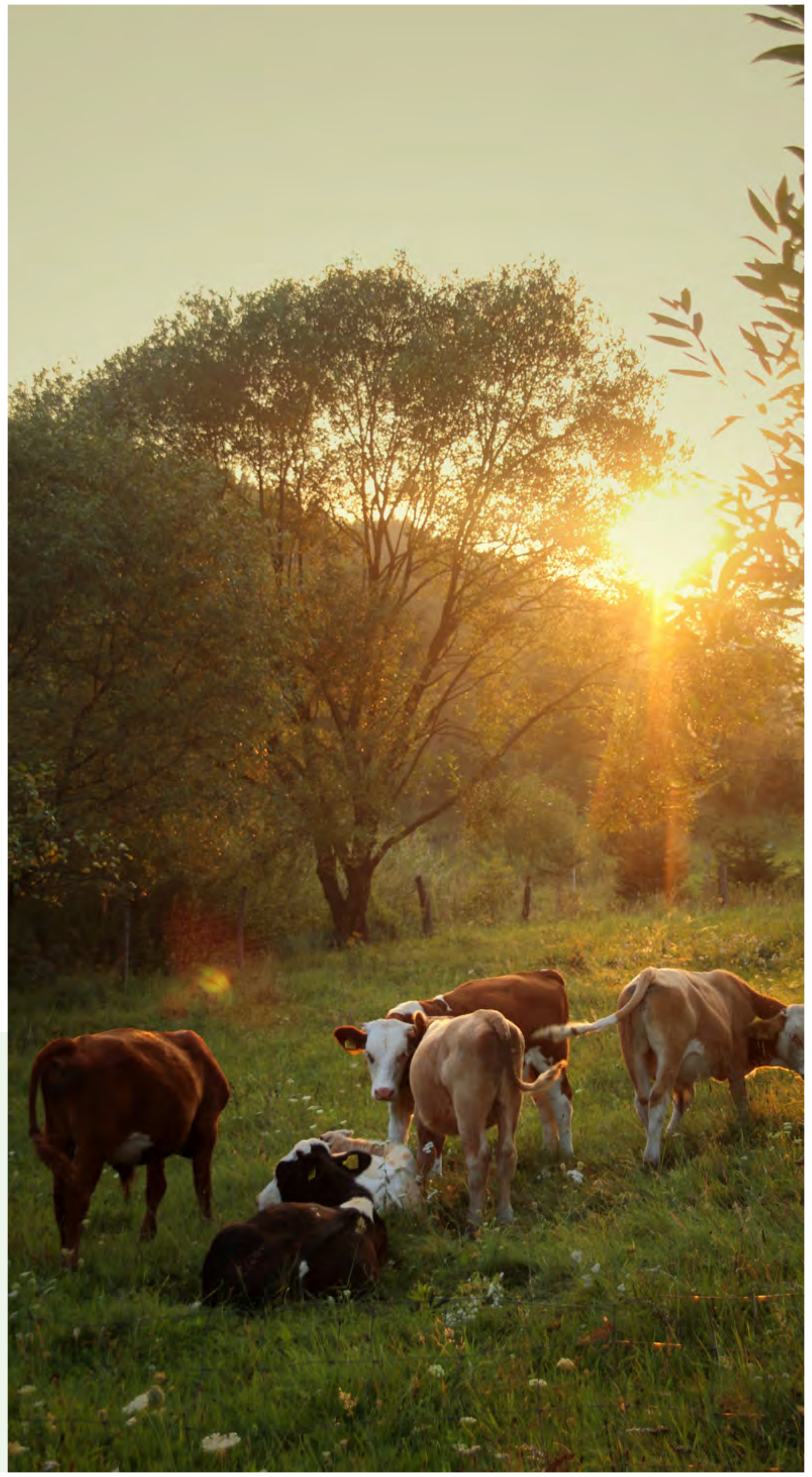
Governments and international organisations are consequently responding with action and initiatives to limit nature loss. The UK has adopted targets from the GBF into policy, such as halting the decline in species populations by 2030 and restoring 70% of designated features in Marine Protected Areas. New regulation in the UK will require businesses to report on nature-related issues, supported by initiatives such as the Science Based Targets Network's (SBTN) corporate targets for nature and the Taskforce on Nature-related Financial Disclosures' (TNFD) framework for organisations to report on evolving nature-related risks.

Protecting and restoring nature is crucial for tackling the climate crisis. It is essential for governments and businesses to consider that there can be no net zero without nature. Indeed, natural climate solutions - "actions that avoid greenhouse gas emissions and increase carbon storage in forests, grassland and wetlands" - can provide around one-third of the emissions reductions needed to limit warming to 1.5°C.[15] It is therefore crucial that the global climate and nature crises are not siloed as topics, and the importance of tackling nature loss is elevated within public and private sector strategies to decarbonise economies.

The estimated funding gap for climate adaptation and resilience finance, biodiversity and nature-based solutions is

£260-484bn

per year up to 2030.[12]



12. One Planet Labs (2021) Blended finance for scaling up climate and nature investments
13. GRI (2021) The Finance Gap for UK Nature
14. UNEP (2022) State of Finance for Nature
15. United Nations Climate Change High-Level Champions (2021) NCS could deliver up to 33% of net emission reductions needed by 2030

TABLE 1 - KEY BARRIERS TO SCALING NATURE FINANCE FROM THE PRIVATE SECTOR[16]

CURRENT INVESTMENT MODELS GENERATE LOW RETURNS	AVAILABLE INVESTMENTS ARE CONSIDERED RISKY	DATA AND TRANSPARENCY	THE PIPELINE OF SUFFICIENTLY LARGE INVESTIBLE OPPORTUNITIES REMAINS SMALL
With economic systems continuing to undervalue the products and services provided by nature, investments that provide nature-positive outcomes can struggle to articulate clear revenue streams. As well as the perception of low returns, there is a concern that investments take a long time to generate returns. Land owners and service providers will require income streams that support nature-positive outcomes and an environment that fosters confidence and transparency.	Due to the nascency of nature financing solutions, investments are still considered higher risk. As well as the issues with low returns and long-lead times to generate revenue, investments in nature-related projects can also present novel risks for financiers, especially with regards to Gender Equality and Social Inclusion (GESI). Large-scale restoration and expansion of protected areas, if not properly managed, can cause significant tension with local communities who rely on the land for their livelihoods and in many instances lack secure land tenure or resource rights.[17] Whilst nature markets are beginning to develop, principles, standards and the required infrastructure are still lacking and investors and service providers are hesitant to direct capital towards nature-positive outcomes without clarity on the emerging regulatory and policy frameworks and how these could impact returns.	Access to data, which is essential for monitoring progress and accrediting environmental services, alongside a consensus around nature-related metrics are also lacking. Without clear monitoring, reporting and verification (MRV) mechanisms in place, investors, consumers and service providers will be hesitant to shift towards nature-positive solutions due to the high cost of measuring nature-positive outcomes and fear of being accused of greenwashing.	Whilst capital is available that can be channelled towards nature, investment opportunities of a sufficient scale remain sparse, resulting in high transaction costs. In a survey conducted by The Nature Conservancy, access to investment opportunities with a sufficiently large ticket size was the number one barrier to scaling investments in natural capital.[18]

For more detail on these barriers, please see PwC's report: Accelerating Finance for Nature: Barriers and recommendations for scaling private sector investment

16. PwC UK (2023) Accelerating Finance for Nature: Barriers and recommendations for scaling private sector investment
17. UNCCD (2022) Global Land Outlook Second Edition: Land Restoration for Recovery and Resilience
18. The Nature Conservancy (2019) Investing in Nature: Private finance for nature-based resilience

1.1. Economies are facing a myriad of nature-related risks with potentially significant cost implications for businesses and financial institutions

Businesses can be directly dependent on nature if their activities are, for example, reliant on crop yields, minerals or water, to produce outputs. They can also be indirectly dependent; sectors such as consumer and professional services, finance and technology, all rely on a stable natural environment with a sustainable stock of natural assets to function.

55%

of global GDP, equivalent to about US$58 trillion, is moderately or highly dependent on nature.[19]

These dependencies mean businesses face physical and transitional risks. Using the TNFD framework[20], nature risks can be defined as outlined in Table 2.

Upcoming regulation is requiring businesses and financial institutions to invest to remain compliant, alongside growing demand from investors and customers for nature-positive products. The Corporate Sustainability Reporting Directive (CSRD) in the EU, for example, will drive businesses to report on nature-related issues. Article 29 in France already requires investors to monitor their portfolios by measuring both their alignment with the Convention on Biological Diversity and their share of investments contributing to reduced biodiversity impacts (as outlined by IPBES), ultimately calculating a "biodiversity footprint".[21] Businesses and financial institutions therefore need to develop strategies that transform their relationship with nature and safeguard their operations in order to mitigate this regulatory risk. This requires support to determine their impacts, dependencies and possible levers for transitioning to nature-positive business models.

TABLE 2 - NATURE-RELATED PHYSICAL AND TRANSITION RISKS

PHYSICAL RISKS	TRANSITIONAL RISKS
Physical risks from nature loss originate from dependency on ecosystem services, the impacts of economic actors on those services, and the corresponding exposure to their loss. They are categorised as:	Transitional risk from adapting to a "nature-focused" economy includes the effects of legal, regulatory and market changes from public or stakeholder demands. They are categorised as:
Acute risks: event-driven risks, such as increased severity of extreme weather events. For example, the destruction of wetlands or mangroves removes natural flood defences, therefore increasing the size of impacts from extreme weather events.	**Policy and legal risks:** regulatory changes which aim to achieve nature-positive outcomes e.g. taxes and permits to mitigate nature loss.
Chronic risks: long term shifts in nature, such as changes in the supply of natural inputs. For example, reduced availability of water resources or lower stocks of timber.	**Market risks:** investor preferences shift to focus on nature-positive businesses e.g. cost of capital increases for organisations that are not sustainably managed.
	Technology risks: transition to more efficient, resilient and less environmentally damaging technologies will impact a business' production and distribution costs e.g. preparation for novel technologies such as precision agriculture.
	Reputational risks: sentiment towards businesses may change due to their impacts on nature e.g. customer preferences shift, impacting revenue.

19. PwC (2023) Managing nature risks: From understanding to action
20. TNFD (2023) A1: Risk and opportunity identification
21. Novethic (2021) The new decree under article 29 of the french law on energy and climate keeps its promise to strengthen requirements

There is a significant opportunity for the UK, acting as a global centre for nature finance, to drive the investment and tools needed to transition to an economy that is decarbonised, fair and balanced with nature. Businesses will need access to a range of products, skills and services to meet their nature-related targets and align with emerging regulation. The UK can take a leading role in helping to develop these products and services and the ecosystem to support businesses to understand and act on their nature-related impacts, dependencies, risks and opportunities as part of the transition to a nature-positive economy.[22]

This report's vision is for the UK to develop into a global centre for nature finance, with a world-leading ecosystem which supports the UK as a place where finance flows towards nature-positive outcomes in the UK and globally. The set of recommendations outlined to achieve this are focused especially on the domestic considerations, recognising that on the journey to becoming a global leader, the UK must first ensure its own house is in order with respect to nature. The standards, tools and innovations developed to achieve this can then be exported globally to support other countries' transitions to developing nature-positive economies.

The incentives for the UK taking on this role are clear. According to the UK's Green Finance Strategy, exports from low carbon and renewable energy industries increased by 67% from 2020, compared to total exports which increased by 6%[23]. Although exports are currently strongest within more established green sectors, such as low emission vehicles and offshore wind, channelling investment into emerging areas of nature innovation and technologies, as well as the development of a skilled workforce able to drive this agenda, could unlock significant export opportunities. Furthermore, there is extensive evidence to show the crucial role that protecting and restoring the natural environment will play in helping the UK to achieve its net zero ambitions.[24]

Nature-based solutions are estimated to provide

37%

of climate change mitigation until 2030.[25]

22. IUCN (2022) Towards an IUCN nature-positive approach: a working paper
23. UK Government (2023) Mobilising Green Investment: 2023 Green Finance Strategy
24. Natural England (2021) Carbon storage and sequestration by habitat: a review of the evidence (second edition)
25. IPBES (2019) The global assessment report on biodiversity and ecosystem services: summary for policymakers

Section 2

The UK as a global centre for nature finance

In the context of climate finance, the UK has consistently ranked at or near the top of global leaderboards.

London currently sits at the top of the Global Green Finance Index (GGFI), while Edinburgh has climbed eight places, from 22nd to 14th.[26] The "areas of competitiveness" assessed included Sustainability, Business, Human Capital and Infrastructure, covering capabilities such as green finance activity, availability of skilled personnel, labour market flexibility, and institutional and regulatory environment. London came out on top for three out of the four macro areas and a close 2nd in Business, demonstrating the broad spectrum of skills that the city has to offer for climate. Many of these areas of competitiveness already translate well into the drivers of success for a global centre for nature finance.

1st

London currently sits at the top of the Global Green Finance Index (GGFI).

26. Z/Yen (2023) The Global Green Finance Index 11

In England alone, there are an estimated 70,000 people working in the fields of conservation, environment and adjacent areas.[27] This represents a significant workforce with expertise of value to corporates and financial institutions. From ecologists that could consult on nature-based solutions project developments, to conservation finance experts that can communicate the nature-related risks and dependencies of business activities and investment portfolios. As nature finance gains traction, increasing interaction between these parties will be essential to maintain the competitive edge seen in climate finance circles.

The UK Government is also supporting the development of key skills that will enable the domestic market to deliver a suite of green services to the global economy. In 2020, the UK Government launched its £40 million Green Recovery Challenge Fund to help create up to 3,000 jobs and safeguard up to 2,000 others in areas such as protecting species and finding nature-based solutions.[28] From September 2023, 16-19 year olds will be able to study Agriculture, Land Management and Production T-Levels. Since the 25 Year Environment Plan was published in 2018, the UK Government and employers have also been working together to develop a series of new apprenticeships in forestry, countryside management, agriculture and horticulture advice, the water environment, environmental sustainability, ecology and recycling. These Government led initiatives are paving the way for new green industries and are helping to position the UK as a world leader in nature recovery.

£40M

Green Recovery Challenge Fund launched in 2020 by the UK Government

The UK is the world's largest centre for international bond issuance and trading, and has a strong base of highly engaged ESG investors. In 2022, over £900 billion of international bonds were issued in the UK and the outstanding value of the UK's international bonds was the largest in the world, totalling more than £2.6 trillion.[29] Complementary to this is high engagement with ESG investment in the UK; approximately £5tn of investment fund assets managed in the UK are done so using ESG principles.[30] The UK is in an opportune position to leverage this wide access to international markets to advocate for - and encourage investment in - nature-related projects across a diversified portfolio of geographies and industries.

The UK is leading the way on sustainability regulation. The UK was an early adopter of a carbon emissions trading scheme and the first G20 country to announce that it would make disclosures in line with the Task Force on Climate-related Financial Disclosures (TCFD) recommendations fully mandatory across the economy. In April 2019, the UK Prudential Regulation Authority (PRA) became the first prudential regulator to publish a comprehensive set of supervisory expectations for how banks and insurers should manage climate-related financial risks.[31]

27. HM Government (2023) Environmental Improvement Plan 2023
28. HM Government (2020) Government's £40 million Green Recovery Challenge Fund opens for applications
29. The City of London Corporation (2023) State of the sector: annual review of UK financial services 2023
30. The Investment Association (2022) Investment Management in The UK 2021-2022: The Investment Association Annual Survey
31. Bank of England Prudential Regulation Authority (2019) Supervisory Statement | SS3/19 Enhancing banks' and insurers' approaches to managing the financial risks from climate change

Building on its world-leading climate regulation, the UK is now well placed to lead the way on nature and has already begun to do so through flagship regulatory and standard-setting initiatives such as the UK Sustainability Disclosure Requirements (SDR) regime and the recently launched Nature Investment Standards Programme being led by the Department for Environment, Food and Rural Affairs (Defra) and the British Standards Institution to help boost market confidence and increase private sector investment into nature recovery.[32]

The UK has been a pioneer in developing nature credit markets, a key driver for mobilising private finance. The UK Government's Biodiversity Net Gain (BNG) policy is one of the world's first mandatory markets for biodiversity credits which requires developers to avoid habitat loss in their operations. The UK has also recently published a new Nature Markets Framework[33] which sets out principles and priorities for the development of high-integrity markets. The new framework indicates the UK's focus on market mechanisms and their international leadership in developing nature markets. This builds on the UK's reputation as an early leader in developing voluntary carbon markets to support woodland creation and peatland restoration. Furthermore, at the Summit for a New Financial Pact in Paris in June 2023, the UK and French Governments launched the UK – France Global Biodiversity Credits Roadmap. This aims to *"facilitate the sharing of best practice on the governance mechanisms for credit funding, monitoring regimes to ensure biodiversity improvements, and the fair distribution of income to indigenous peoples and local communities"*.[34]

Whilst the UK's expertise across finance and innovation, alongside the strength of its supporting professional and legal services, provides it with strong foundations on the path to become a global centre for nature finance, the current enabling environment falls short of the action needed to overcome some of the key barriers to scaling nature finance (Table 1). The following sections address the current state of the UK nature finance ecosystem, under the themes of "financing nature" and "integrating nature into the financial system", and present a roadmap of recommendations intended to support the development of the UK into a leading global hub for nature finance.

32. BSI (2023) BSI and Defra launch Nature Investment Standards Programme
33. HM Government (2023) Nature markets: A framework for scaling up private investment in nature recovery and sustainable farming
34. HM Government (2023) UK - France Global Roadmap launched to mobilise global nature finance

Section 3
The current state of UK nature finance

The previous section illustrated that the UK already has a well-developed climate finance ecosystem which can be leveraged and built upon to support the development of a world-leading nature finance hub. The diagram on the following page provides a non-exhaustive overview of the UK's current nature finance ecosystem, which relies on a broad range of actors.

UK's current nature finance ecosystem overview

GUIDING PRINCIPLES
- Global Biodiversity Framework
- UN Sustainable Development Goals
- Dasgupta Review

STANDARDS AND FRAMEWORKS
- Science-based Targets Network
- Taskforce on Nature-related Financial Disclosure
- International Sustainability Standards Board
- Transition Plan Taskforce

DOMESTIC POLICY AND REGULATION
- HM Treasury; Department for Environment, Food and Rural Affairs (Defra); Department for Energy Security and Net Zero; Natural England
- Financial Conduct Authority; Prudential Regulatory Authority; Bank of England

CAPITAL PROVIDERS
- Banks
- Asset managers
- Private equity
- Impact investors
- UK public finance institutions
- Asset owners:
  - Long-term savings providers (pension funds, insurance funds)
  - Corporate investors

NATURE-BASED SOLUTIONS (UK AND GLOBALLY)
- Project developers
- Public and private conservation / restoration

CAPITAL FLOW

CAPITAL FLOW

MARKET TOOLS

DEBT INSTRUMENTS
- Sustainability-linked loans and bonds
- Green loans and bonds
- Nature-related perpetual bonds
- Conservation bonds
- Debt for nature swaps

CONCESSIONAL FINANCE
- Guarantees
- First loss positions
- Risk insurance
- Technical assistance funds
- Design-stage funds

CAPITAL PRODUCTS
- Nature credits
- Equity investments
- Nature-related insurance
- Nature-related impact funds
- Nature-related exchange-traded funds

SUPPORTING ECOSYSTEM
- Data and metrics providers:
  - Geospatial monitoring
  - Nature impact monitoring and eDNA
  - Natural capital accounting
- Academia, science and research
- Non-governmental organisations
- Professional services:
  - Legal
  - Auditing
  - Consulting
  - Insurance
- Industry coalitions (e.g. Natural Capital Investment Alliance, Business for Nature, Coalition for Private Investment in Conservation)
- Trading infrastructure:
  - Exchanges
  - Credit issuers
  - Ratings agencies
  - Registries

This overview flowchart is non-exhaustive and subject to change as the market continues to evolve rapidly.

UK’s current nature finance ecosystem overview

A key element of growing and consolidating this ecosystem is the need to strengthen the interactions between the various actors, for example, connecting science and research to policymakers and ultimately investors. Meanwhile, some elements of the ecosystem in particular will require further development on the road to creating a global centre for nature finance:

– **Market tools:** novel and innovative financial products will need to be developed to align with nature targets (see Table 3). For example, there is a need to develop well recognised and agreed metrics by sector that relate to nature targets for sustainability-linked loans and bonds.

– **Data and metrics providers:** datasets, metrics and analysis will need to be developed to support the growing need for understanding nature-related impacts, dependencies, risks and opportunities.

– **Trading infrastructure:** as nature finance gains traction there will be a growing need for exchanges and trading infrastructure to help investors purchase nature related financial products. This will also require rigorous and credible methodologies and standards to ensure that projects and issued credits deliver high-integrity nature protection and restoration.

The innovative market tools required to overcome some of the barriers to investing in nature (Table 1) are still being developed, tested, and in some instances scaled. Table 3 provides a selection of some of the emerging products being used to channel finance towards nature.

TABLE 3 - EMERGING MARKET TOOLS FOR NATURE

SUSTAINABILITY-LINKED LOANS AND BONDS	DEBT FOR NATURE SWAPS (DFNS)	PERPETUAL BONDS	NATURE CREDIT MARKETS	NATURE FUNDS
Sustainability-linked loans and bonds are financial instruments designed to incentivise and reward companies and organisations for achieving predefined sustainability targets. The interest rates or terms of these loans and bonds are tied to the borrower’s or issuer’s sustainability performance, and can be linked to nature targets.	DFNS are mechanisms to restructure the external debt of a country to provide debt relief by investing in national nature-related projects. DFNS involve the buy back of the debt on more favourable terms, provided that the debtor country redirects the funds to local nature conservation projects, and that it makes interest payments under the restructured terms, usually in local currency.	Perpetual bonds drive non-equity investment without maturity dates. This allows them to be treated as equity, with debt issuers paying coupons on these bonds in perpetuity with no requirement to redeem the principal. Eliminating short-term project impact deadlines through the provision of such bonds allows sufficient time for nature-related projects to reach maturity or start generating reliable returns.	**Nature-specific credits[35]:** Units of ecosystem services which are delivered by nature restoration or improvement projects and are being developed under both voluntary and regulated standards. Examples include biodiversity credits, water quality credits and reef credits. **Nature-related carbon credits:** Carbon credits resultant from nature-based solutions. These can be voluntary, or compliance driven in the case of credits traded between countries under elements of Article 6 of the Paris Agreement.	Nature funds provide a mechanism to raise capital for nature-recovery and mitigation programmes whilst simultaneously providing investors with a return. Funds allow diversification throughout a portfolio of nature-related investments which can reduce risk.

35. Taskforce on Nature Markets (2022) Global Nature Markets Landscaping Study

Section 4
Financing nature

Mobilising and creating opportunities for nature investment

As outlined in Section 1, there is a significant finance gap for nature and public investment alone will not meet this gap. This section sets out how financial flows for nature can be incentivised and enabled to unlock the investment flows required for a nature-positive transition.

4.1. Signalling & policy certainty

Develop sector-specific targets and roadmaps for nature restoration and protection and provide clarity on how the UK will operationalise its key commitments under the Global Biodiversity Framework.

Setting robust, transparent and credible targets for protecting and restoring nature sends a clear message to the private sector that the UK Government is committed to a nature-positive future. Policy certainty will stimulate innovation and investment in the products and services required to drive the transition to achieve this future. In this regard, the UK has signed up to the Global Biodiversity Framework (GBF) committing to a suite of international targets (including scaling private sector investment) to live in harmony with nature by 2050.[36]

One of the cornerstones of the GBF is countries committing to protect 30% of land and sea for nature by 2030 (30 by 30). A report published in July 2023 by the House of Lords Environment and Climate Change Committee illustrated the pace at which the UK will need to increase its action on nature in order to meet its international commitments.[37] Just 6.5% of land in England currently meets the criteria for 30 by 30, which supports the report's view that "The Government is clearly not on course to meet 30 by 30. Achieving the target requires urgent action." It is therefore important that the Government signals what its national response and action plan will be for meeting the terms of the GBF. Companies will especially be seeking clarity on how the UK Government will respond to Target 18 of the GBF which covers subsidies: *Identify by 2025, and eliminate, phase out or reform incentives, including subsidies, harmful for biodiversity, in a proportionate, just, fair, effective and equitable way, while substantially and progressively reducing them by at least $500 billion per year by 2030, starting with the most harmful incentives, and scale up positive incentives for the conservation and sustainable use of biodiversity.*[38]

Although there have been positive developments in understanding the UK Government's policy direction of travel on nature (Box 1), many of the UK's national goals and targets on nature remain high-level and sector agnostic, and the pathways to achieving them are not well defined. On their own, they will not incentivise specific industries to invest in nature recovery. Acknowledging the crucial role of the private sector in achieving the UK's nature targets, policymakers should consider developing sector specific targets and plans to incentivise and guide businesses on how to transition and develop new services and technologies that address nature loss. For example, in 2022 the UK Government published a series of sectoral roadmaps summarising Government policies and opportunities towards a net zero aligned future. The UK could replicate this, and develop sector specific goals, targets and roadmaps to encourage the nature-positive transition.

BOX 1 - KEY UK COMMITMENTS ON NATURE

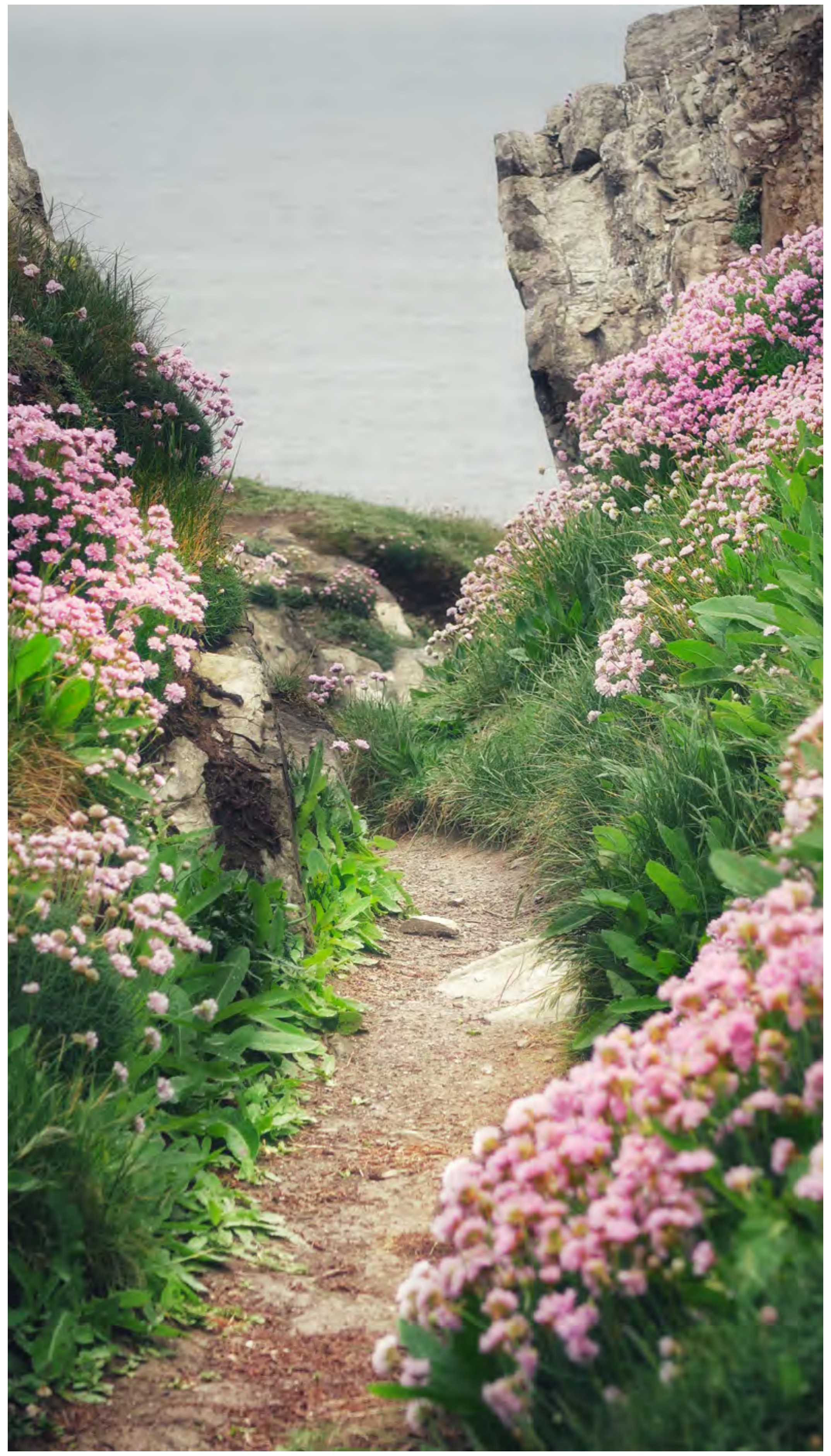
The UK has made a number of commitments in recent years outlining its intention to transition towards a nature-positive economy. These goals and targets send a clear signal to markets that the UK is committed to its nature-positive agenda and the role of the private sector in achieving its ambition. The UK Environment Act, which came into force in 2021, set a legally binding target to halt the decline in domestic species populations by 2030 and then increase populations by at least 20% to exceed current levels by 2042.[39] The new Environmental Improvement Plan, the first update to the 25 Year Environment Plan, sets out a range of additional targets and goals for the natural environment in England. For example, the plan set a target to raise at least £500 million in private finance to support nature's recovery every year by 2027 in England, rising to more than £1 billion by 2030.[40] At COP26 in 2021, the UK was one of the more than 140 nations which pledged to halt and reverse forest loss and land degradation by 2030.

RECOMMENDATIONS

1. Provide clarity on how the UK will operationalise the commitments it has signed up to under the Global Biodiversity Framework, especially with regards to 30 by 30 and phasing out subsidies which are harmful for nature.
2. Develop sector-specific targets and roadmaps (focusing on high impact industries) for reducing pressure on nature and facilitating nature restoration and protection - drawing on appropriate inputs from industry bodies, the private sector, academia, and NGOs - to support the delivery of the UK's national nature-related targets and international commitments and provide certainty to the real economy and investors.

36. GBF (2022) Kunming-Montreal Global Biodiversity Framework
37. House of Lords (2023) An extraordinary challenge: Restoring 30 percent of our land and sea by 2030
38. GBF (2022) Kunming-Montreal Global Biodiversity Framework
39. HM Government (2021) Environment Act 2021
40. HM Government (2023) Mobilising Green Investment: 2023 Green Finance Strategy

4.2. Project pipeline creation



Support the development of a pipeline of sufficiently large investible opportunities, including by accelerating the supply of supporting monitoring, reporting and verification (MRV) products and services.

The UK Government has launched several initiatives to support project developers to create a pipeline of investible opportunities in nature. For example, Defra's Big Nature Impact Fund uses £30 million of seed funding to attract private sector investment that accelerates high-integrity nature projects in England that generate revenue from ecosystem services.[41] Similarly, the Natural Environment Investment Readiness Fund (NEIRF) is a £10 million fund that provides grants up to £100,000 to 75 environmental groups, local authorities, businesses and other organisations to help them develop nature projects in England to a point where they can attract private investment.[42] Meanwhile, the Scottish Government and NatureScot, have launched the Facility for Investment Ready Nature in Scotland (FIRNS) which will provide grants of up to £240,000 to organisations to help them develop business models that attract private investment in projects that restore and improve the natural environment.[43] As described in Box 2, the UK Government is also investing heavily in its Environmental Land Management scheme (ELMs), which could, with sufficient policy support and signalling, create a significant collection of land units suitable for nature-related financial products, such as nature credits.

BOX 2 - THE ENVIRONMENTAL LAND MANAGEMENT SCHEMES

The UK's Environmental Land Management schemes (ELMs) seek to dovetail public and private sector investment into landscape recovery. As 70% of the UK's land is managed for agriculture, there is a great opportunity for farmers and landowners to protect and restore natural capital. However, without financial incentives and mature nature markets in place, landowners are unlikely to adopt sustainable practices that sacrifice short term gains. ELMs seek to address the untenable balance between farmed and natural land in the UK by financially incentivising landowners to recover nature. The schemes aim to bring up to 60% of agricultural soil under sustainable management by 2030.[44]

Whilst ELMs currently rely on public sector subsidies, the schemes create an enabling environment for 70% of managed land in the UK to implement sustainable practices and create a mechanism for landowners and farmers to assess, monitor and restore nature which will be an essential component to any credit based trading scheme in the future.

Although Government intervention is helping to increase the supply of investible nature-related opportunities, more needs to be done to increase price certainty to provide developers with the confidence to further invest in project origination. The Woodland Carbon Guarantee, for example, provides £50 million of support to accelerate woodland planting rates and to develop the domestic market for woodland carbon for the removal of carbon dioxide from the atmosphere.[45] By guaranteeing a price for verified carbon credits, the scheme guarantees revenue for project developers while still providing project developers with the opportunity to trade carbon credits on the open market. Government intervention which provides price certainty to project developers generating biodiversity credits would support the rapid scaling of this growing, but still nascent, market, for example by drawing on the Government's use of Contracts for Difference to support low-carbon electricity generation.[46]

41. HM Government (2022) Update on the Big Nature Impact Fund
42. GFI (2023) Natural Environment Investment Readiness Fund
43. NatureScot (2023) FIRNS - The Facility for Investment ready Nature in Scotland
44. HM Government (2022) Government unveils plans to restore 300,000 hectares of habitat across England
45. HM Government (2019) Woodland Carbon Guarantee
46. HM Government (2022) Contracts for Difference

4.2. Project pipeline creation

The Government can further support the growth of a pipeline of investible nature-related projects by advancing the development of supporting products and services that facilitate project investments, in particular relating to MRV. In its Spring Budget (2023), the UK indicated its continued support towards the country's most innovative companies by extending the British Patient Capital programme until 2033-34 and increasing its focus on R&D intensive industries, providing at least £3 billion in investment.[47] However, the budget remains climate-focused with public support channelled towards energy and carbon capture. The UK could leverage this opportunity to step up its R&D commitments that support the sectors and technologies required to deliver the nature-positive transition.[48] As well as direct support through R&D funding programmes, the Government could seek to encourage innovation in this regard through tax incentives for investors supporting nature-positive businesses to scale, building on the precedent set by schemes such as the The Venture Capital Trust (VCT) scheme.[49]

RECOMMENDATIONS

1. Provide price certainty to project developers investing in emerging solutions, for example by implementing a guaranteed price for project developers investing in the creation of biodiversity and nature-based carbon credits.
2. Develop clear long-term guidance outlining how subsidised programmes (such as ELMs) will be linked to nature markets in the future.
3. Integrate nature into existing R&D funding models (such as the British Patient Capital Programme) and consider utilising tax incentives for investors to encourage the development of new technologies and nature-related solutions, as well as developing bespoke new funding models.

47. HM Treasury (2023) Spring Budget 2023
48. UKRI (2023) Farming Innovation: find out about funding
49. HMRC (2020) Venture Capital Trusts: Introduction to National and Official Statistics

4.3. Concessional capital and financial guarantees

Develop and utilise solutions that de-risk nature-related investment opportunities.

Under current policy and regulatory settings, the risks of investing in nature at scale often outweigh the potential benefits, primarily driven by low returns and high transaction costs (Table 1). A global centre for nature finance should work to address investor concerns and de-risk nature-related investment opportunities while the market is still scaling. Blended finance mechanisms in particular offer a clear tool to de-risk investments and consequently catalyse private sector finance.

Blended finance can take many forms including concessional capital, guarantee or risk insurance, technical assistance funds and design stage funds that help to provide the necessary risk/return profile to mobilise additional private sector investment. For example, in 2020 Defra supported Mirova's Land Degradation Neutrality Fund through the UK's International Climate Finance Programme. With an anchor investment of £10 million, the public capital provided a protective cushion to significantly reduce the risk profile for private investments in the sustainable land-use sector. The fund was used to support over £40.5 million of additional investment from the private sector inspiring confidence for environmentally sustainable operations.[50]

The UK Government may consider leveraging similar models from climate finance to de-risk nature-related investments; this is crucial for achieving its stated ambition of mobilising at least £1 billion per year of private finance to support nature's recovery by 2030. A clear signal to the market would be the establishment of a major domestically focused impact investing organisation for nature, akin to Big Society Capital.[51]

Development Finance Institutions (DFIs) have historically provided invaluable interventions in some of the biggest natural capital transactions to date, namely the U.S. International Development Finance Corporation, which provided political risk insurance on both the Ecuador[52] and Belize[53] debt-for-nature swaps (see Box 3), and the Inter-American Development Bank, which provided a £67 million guarantee to the former. These interventions were cumulatively responsible for more than £270 million in savings being diverted to conservation activities between the two countries. Other de-risking solutions such as the offering of favourable interest rates, taking first-loss or junior positions on investments have also been successfully deployed to de-risk investment.

UK public financial institutions have a foundation in supporting climate finance which can be built upon and extended to nature finance. British International Investment (BII), the UK DFI, committed in 2021 to over £3 billion of investment to combat the climate crisis[54], and UK Export Finance (UKEF) was the world's top export credit agency for sustainable financing in 2021.[55] In 2023, UKEF announced an increase in capacity from £50 billion to £60 billion to support UK exporters and supply chains with increasing support in clean growth and climate adaptation. Whilst UKEF has made significant progress in mobilising private investment for the net zero transition by offering finance and de-risking investments, it remains focused on the climate agenda. UKEF and BII's impact could be increased by integrating the role of nature into their existing climate strategies to help build a business landscape that simultaneously supports nature-positive outcomes.

RECOMMENDATIONS

1. Leverage similar models from climate finance to de-risk nature-related investments, for example by establishing a major domestically focused impact investing organisation for nature.
2. Increase the availability of concessional capital or financial support for nature-related transactions through existing UK public financial institutions, especially BII and UKEF.

BOX 3 - BELIZE'S DEBT FOR NATURE SWAP

In 2020, Belize's tourism-dependent economy contracted by 16.7% and national debt reached 133% of GDP due to the effects of COVID-19. Furthermore, the Governments' "Superbond" of £432 million, representing all commercial debt, was trading at a heavy discount due to doubts over repaying bondholders, while interest rates on borrowing money were too high to mitigate the issue.[56]

In November 2021, the Belize Blue Investment Company (BBIC, a subsidiary of The Nature Conservancy) partnered with the Belize Government to announce a £266 million debt conversion which funded marine conservation, allowing the country to pay back most of its Superbond. The debt conversion took the form of a 19-year loan, to be paid back by 2041. The loan was partially funded by BBIC, and as the loan was used completely to fund marine conservation, was largely funded by Credit Suisse's Blue Bonds scheme and Blue Loan of £198 million, which was borrowed at a 45% discount with additional coupons that increase annually.

The refinancing relieved Belize's national debt by 12% and set up considerable funding for marine conservation projects. This debt conversion proves an innovative model for refinancing sovereign commercial debt and using conservation to create debt stability.

50. Mirova (2020) Defra commits £10m to Mirova's Land Degradation Neutrality Fund
51. Big Society Capital (2023) is the UK's leading social impact-led investor, and was formed in 2012 using capital from dormant bank accounts in the UK
52. IDB (2023) Ecuador Completes World's Largest Debt-for-Nature Conversion with IDB and DFC support
53. CFFA (2022) Debt-for-nature swaps and the oceans: The Belize Blue Bond
54. BII (2021) CDC Group to invest over £3 billion over the next five years to combat the climate emergency
55. UK Export Finance (2022) UKEF provides record £3.6bn to help UK businesses construct hospitals, electric railways and offshore wind across the globe
56. GFI (2022) Government of Belize Debt Conversion for Marine Conservation

4.4. Facilitate UK nature credit markets

Lead the way in developing robust and high integrity nature credit markets.

Scaling private investment for nature could be supported by the establishment of high integrity nature credit markets, both voluntary and compliance driven. Biodiversity and nature-based carbon credits enable private investment in nature by creating units that can be bought or sold. Credits are delivered by nature restoration projects and can ensure that those who benefit from nature pay a fair price for the services it provides. By internalising the costs of conserving nature, nature markets help rebalance the demand for products and services from nature.[57] These markets also incentivise farmers and landowners to protect and restore nature and reward efficient MRV through new sources of income generated by project activities that can support them and their communities.

Demand for nature credits may be voluntary, driven by companies wanting to meet their nature-positive targets or improve resilience within their value chains, or regulatory, whereby companies are regulated to deliver or finance nature-related improvements. An important example of compliance driven markets in the UK is the establishment of Biodiversity Net Gain policy (see Box 4).

Whilst the UK Biodiversity Net Gain policy has been innovative, land is only one component of the UK's nature recovery and more needs to be done to build a robust market led mechanism to protect marine biodiversity. Although the UK has set out its intent to develop a new net gain policy to apply to the marine landscape, it needs to accelerate its efforts to address marine biodiversity as a matter of urgency. Furthermore, BNG requirements are only mandatory for developers and the UK Government could assess incorporating additional high impact sectors (such as energy, chemicals and transport) that can help channel private finance towards nature-positive outcomes; this is the case in other jurisdictions, such as Colombia (see Box 5). Equally, although the UK has made credible progress in establishing compliance-driven nature credit markets, other jurisdictions are more advanced in their market design and have incorporated broader elements of nature within their markets such as water (see Box 6) and soil carbon (see Box 7).

BOX 4 - UK NATURE CREDIT MARKETS: BIODIVERSITY NET GAIN

The UK's Biodiversity Net Gain (BNG) policy, which was legislated by the Environment Act 2021, will establish a mandatory market for biodiversity units from November 2023 requiring developers to avoid habitat loss in their operations and bring about a 10% improvement. Land managers who can enhance habitats will be able to sell their resulting biodiversity units to property developers who cannot avoid loss of habitat on their land and must therefore purchase credits. For landowners, the BNG market provides a long-term source of income which is already expected to be worth £135 - 274 million annually[58]. BNG is one of the first mandatory policies of its kind and shows international leadership in developing nature credit markets.

57. GFI (2022) Financing Nature Recovery UK
58. HM Government (2023) Natural England: What landowners can do now to gear up for the biodiversity net gain market

4.4. Facilitate UK nature credit markets

BOX 5 - COLOMBIA'S BIODIVERSITY OFFSET AND CREDIT MARKETS

In 2012, the Colombian Government introduced the requirement for companies applying for environmental licences in the mining, hydrocarbon, infrastructure, electrical and maritime sectors to quantify biodiversity offsets with a "No Net Loss" approach (NNL) – wherein biodiversity loss in one site can be offset at another - with the adoption of the Manual for Allocating Offsets for Loss of Biodiversity (MACPB).[59]

In 2016, biodiversity offsets were taken to a new level through the introduction of habitat banks. Colombian company Terrasos launched the first habitat bank in Latin America in 2016 with an initial investment of £1.1 million from the Inter-American Development Bank.[60] The Colombian Ministry of Environment then issued the administrative act regulating Habitat Banks in 2017.[61] Habitat banks comprise private conservation and restoration sites generating biodiversity credits. They act as aggregate offsetting schemes, providing a solution to otherwise high transaction costs and uncoordinated offset purchases.

In contrast to the UK, Colombian habitat banks allow companies across the infrastructure sector to offset impacts – such as mining, oil, and gas projects – in line with the NNL policy.[62] Habitat banks have been recognised by UN BIOFIN as having the potential to mobilise £3.5 billion for the country.[63] As of 2023, Terrasos has eight habitat banks of about 3,000 hectares in total and has helped companies with more than 40,000 hectares of offsets.[64] Their Meta Habitat Bank recently sold out its 600 credits - each representing one hectare conserved for 30 years. Credit purchasers included oil pipeline operators OCENSA, transportation firm CENIT and Grupo de Energía de Colombia.[65]

BOX 6 - AUSTRALIA'S REEF CREDIT SCHEME FOR WATER QUALITY

Launched in 2017 as a feasibility study by Terrain NRM and NQ Dry and funded by the Queensland Government,[66] the Reef Credit Scheme is a voluntary scheme encouraging the development of nature projects that improve water quality in the Great Barrier Reef catchment. These projects create Reef Credits - tradable units representing 1kg of nitrogen, or 538kg of sediment, avoided from entering the catchment - that can be sold to organisations looking to improve ESG performance or to offset their own impacts.[67] The scheme is administered by Eco-Markets Australia and credits are registered on a registry managed by IHS Markit.

BOX 7 -NATURE MARKETS IN THE UNITED STATES

The U.S. has multiple nature markets including soil carbon markets, mitigation banking markets, and water credits markets, in addition to regional markets that provide private sector investment opportunities like stormwater retention credits for urban green infrastructure.

While the UK has not yet embraced soil carbon markets, the U.S. has started to embed soil carbon sequestration into policy alongside other on-farm carbon sequestration practices. The Growing Climate Solutions Act was passed by Congress in December 2022, which provides the U.S. Department of Agriculture (USDA) with oversight of markets, offering a certification programme for third-party verifiers and providing technical assistance on generating and selling carbon credits. The USDA is investing more than £2.5 billion for 141 initial projects, to support projects that produce "climate smart commodities", with an upcoming second round to reach £2.8 billion in total.

A climate-smart commodity is defined as an agricultural commodity that is produced using agricultural (farming, ranching or forestry) practices that reduce greenhouse gas emissions or sequester carbon.

Soil carbon markets are still relatively nascent in the U.S. A 2022 report[68] showed that, of 500 farmers surveyed, only 3% participated in the carbon markets, although nearly a third expressed interest and said they were monitoring developments. The low price of soil carbon (around £17 to £35), will need to increase substantially for the market to take off.

59. WRM (2017) Colombia: Environmental Offsets, Legitimizing Extraction
60. Friends of the Earth International (2018) Regulated Destruction: How biodiversity offsetting enables environmental destruction
61. Terrasos (2023) Habitat banks
62. Partnership for Forests (2023) Habitat Banks: Scaling biodiversity protection in Colombia with an innovative financing mechanism
63. BIOFIN (2023) Habitat Banking in Colombia: Preserving Biodiversity and Creating Economic Opportunities
64. Environmental Policy Innovation Centre (2023) Terrasos and the evolution of habitat banks in Columbia
65. Carbon Pulse (2023) Columbian habitat bank sells out biodiversity credits
66. GFI (2023) Green Collar Reef Credit Scheme
67. EcoMarkets (2020) What is the Reef Credit Scheme?
68. AgWired (2022) Research Reveals Farmer Concerns About Carbon Markets

4.4. Facilitate UK nature credit markets

One way for the UK to incentivise sector specific action could be through the development of a voluntary biodiversity credit market. Once sector and company specific goals and targets have been set, a voluntary credit market could assist businesses to deliver on targets to create and restore local habitats. Such a market could create a sustainable source of finance to incentivise the development of nature restoration and protection projects. When developing a voluntary biodiversity credit market, it is essential that lessons learned from the development of voluntary carbon markets are considered.

Lessons learned from the development of voluntary carbon markets

1. Nature-based solutions are complex and varied and therefore clear and strong integrity standards are required to ensure the quality of underlying projects and credibility of buyers claims.
2. Standards need to be sufficiently ambitious and robust, but must also be cognisant of current technology, data and scientific understanding and flexible to adapt to new developments and learnings over time.
3. Strong linkages must be developed between players in the ecosystem including the science and research sector and NGOs, with robust feedback loops.
4. Clear guidance on best-practice for voluntary demand is required to ensure credibility, provide certainty to buyers, and ensure transparency in the market.
5. Buyers must conduct appropriate due diligence, and should develop a comprehensive understanding of the market, and the available tools, data and labels necessary to assess credit quality.
6. Independent assurance processes are crucial for avoiding perverse incentives.
7. Indigenous peoples and local communities must be included in the development of the market, with fair and transparent agreements with regards to benefit sharing.

4.4. Facilitate UK nature credit markets

In addition to scaling nature credit markets, the UK has mature compliance-driven carbon markets which can also be used to drive nature-positive outcomes. In 2002, the UK developed Europe's first Emissions Trading Scheme (ETS) and has a goal to make it the world's first net zero consistent cap and trade market.[69] Acknowledging that addressing climate change and reversing nature loss are mutually supportive goals, there is a huge opportunity for the UK to integrate carbon credits with nature co-benefits into its more mature carbon markets. This requires robust standards and principles - building on existing codes such as those outlined in Box 8. With twin outcomes of climate mitigation and nature protection and restoration, such projects could attract a higher premium from buyers. In the UK's new Environmental Improvement Plan, the Government has already set out its intention to explore the inclusion of high integrity woodland carbon in the UK ETS. Equally, the UK ETS Authority stated in its Response to the Developing the UK Emissions Trading Scheme consultation, that "[w]e believe the UK ETS may offer an appropriate long-term market for high quality nature-based GGRs [Greenhouse Gas Removals]" and that the Authority would explore the inclusion of nature-based GGRs in the UK ETS.[70]

BOX 8 - EXISTING GUIDANCE: CARBON AND NATURE INTEGRATION

UK Woodland Carbon Code: The Woodland Carbon Code is the quality assurance standard for woodland creation projects in the UK.[71] Backed by the International Carbon Reduction & Offset Alliance (ICROA), the Woodland Carbon Code provides reassurance to carbon buyers that they have invested in high quality carbon mitigation projects.

UK Peatland Code: The Peatland Code is a voluntary standard for UK peatland projects which proves assurances to voluntary carbon market buyers that the climate benefits are real, quantifiable, additional and permanent.[72]

RECOMMENDATIONS

1. Expand and develop the regulatory market for nature credits, for example, by:
   - Broadening the scope of BNG to include additional high impact sectors outside of property development, e.g. mining, hydrocarbon, infrastructure, electrical and maritime, as is the case in Colombia.
   - Accelerating efforts to introduce marine net gain legislation, akin to that produced for terrestrial Biodiversity Net Gain.
2. Consider integrating nature based carbon credits into the UK ETS, provided appropriate MRV requirements are included to ensure integrity.
3. Lead the development of voluntary demand for biodiversity credits, including appropriate standards and claims guidance.

69. HM Government (2023) Mobilising Green Investment: 2023 Green Finance Strategy
70. HM Government (2023) Developing the UK Emissions Trading Scheme (UK ETS)
71. WCC (2019) UK Woodland Carbon Code
72. IUCN (2023) Introduction to the Peatland Code

4.5. Develop long-term nature investment strategies

Financial institutions should utilise the growing suite of innovative market tools to invest in nature at scale.

As outlined in Table 3, there are a growing number of emerging market tools which have been designed to facilitate investments in nature. Recognising the potential benefits to the financial sustainability of their balance sheets, UK based financial institutions should consider investing in the deployment and scaling of such innovative nature financing solutions, positioning themselves favourably to capitalise on expected market demand.

Given the typically long-return windows associated with nature-related projects, insurance companies and other long-term savings providers such as pension funds, who hold significant sums of comparatively patient capital, are especially well positioned to help address the global financing gap for nature.

Within the UK, there is a concentration of highly impactful pension funds and insurance providers that command a significant global presence. As key constituents of the UK market infrastructure - the UK insurance industry manages investments worth £1.8 trillion, equivalent to 25% of the country's total net worth[73] and UK pensions assets stood at £1.89 trillion in 2022[74] - the respective industry bodies of these sectors should consider how they can support their members (for example through building skills and knowledge and securing a supportive policy environment) to formulate and execute ambitious natural capital investment strategies to develop a comparative advantage for the UK in terms of deploying patient capital and innovative insurance solutions for nature.

The insurance sector in particular can play a pivotal role in unlocking private finance flows for nature-related projects. Insurance companies can incentivise green projects by offering reduced premiums to at-risk sectors and industries based on their adoption of nature-based measures that mitigate environmental risks, increase the resilience of ecosystems and the supply chains that rely upon them, and provide wider environmental benefits.

Insurance companies will also benefit from boosting the physical climate and ecological resilience of their insured assets through investments in nature-based solutions within their portfolio, such that the frequency, intensity and impact of natural disasters are reduced, resulting in fewer, less expensive payouts to affected customers. Innovative insurance solutions were integral to the success of the Belize Blue Bond, (see Box 3) and also in the Quintana Roo Coral Reef Insurance policy (see Box 9).

RECOMMENDATIONS

1. UK based financial institutions should invest in the deployment and scaling of innovative nature financing solutions, to capitalise on expected market demand. This could be supported through relevant industry forums sharing best practice examples of when such solutions are launched in the UK or other jurisdictions - drawing on the work of GFI Hive.[75] In the immediate term, insurance firms and sources of more patient capital may be better placed to lead on this.

£1.8tn

worth of investments managed by the UK insurance industry

BOX 9 - THE QUINTANA ROO CORAL REEF INSURANCE POLICY

Launched by Swiss Re in 2018 and based on a model conceived by The Nature Conservancy, this parametric insurance solution was designed to offer coastal property owners in the region greater protections from tropical storms, while also opening a source of capital for reef protection and restoration. The area as a whole is insured, funded by federal taxes paid by local property owners and local government contributions into a trust fund that purchases the insurance policy. The policy is triggered based on extreme wind speeds, with payments made for reef restoration varying based upon the strength of the winds.[76]

73. ABI (2023) Insurers as investors
74. Thinking Ahead Institute (2023) Global Pension Assets Study
75. GFI Hive's mission is to increase private investment in nature restoration, nature-based solutions and nature-positive outcomes in and for the UK. GFI Hive works with the finance sector, government, academia, environmental NGOs and land managers to identify and unlock barriers to this mission, and act as a knowledge hub on private investment in nature to increase shared learning, best practices and investment appetite.
76. GFI (2023) Quintana Roo Reef Protection (Parametric Insurance)

Section 5
Integrating nature into the financial system

Aligning the financial system with UK nature goals

Regulation plays an important role in supporting the growth of the UK's nature finance market by ensuring transparency about the nature-related impacts, dependencies, risks and opportunities of investments. This transparency will foster market integrity and consumer confidence in nature-positive investments, will support the mainstreaming of nature into financial decision making, and will enable financial flows across the economy to align with the UK's nature-related commitments. This section outlines how UK regulation supports alignment of the financial system with key goals on nature, and provides recommendations on how regulation could be enhanced to ensure greater alignment going forward.

5.1. Build on the UK's already world leading regulatory architecture for sustainability

Seek out opportunities to strengthen or accelerate the deployment of nature-related regulation that supports the UK Government's Roadmap to Sustainable Investing.

In its Roadmap to Sustainable Investing,[77] published in October 2021, the Government set out its ambition to green the financial system in three phases:

1. **Informing investors and consumers**: Addressing the information gap for market participants, ensuring a flow of decision-useful information on environmental sustainability from corporates to financial market participants.
2. **Acting on the information**: Creating Expectations and requirements that this sustainability information is mainstreamed into business and financial decisions, for example in risk management and investor stewardship.
3. **Shifting financial flows:** Ensuring that financial flows across the economy shift to align with the UK's net zero commitment and wider environmental goals, including on biodiversity.

In advancing its regulatory framework, the UK has sought to prioritise international interoperability and intends to base its regulation on leading international standards. In the Government's updated Green Finance Strategy[78], it confirmed that it would draw on the International Sustainability Standards Board (ISSB) standards and the Taskforce on Nature-related Financial Disclosures' (TNFD) Framework where appropriate in designing domestic regulation. As a result, UK regulation can serve as a model for other countries looking to incorporate nature into their own regulatory frameworks, establishing the UK as the leading centre for nature finance globally.

Acknowledging the UK's already strong position on nature-related regulation, this section provides an overview of key elements of the three phases in the Roadmap to Sustainable Investing, and recommendations for how these regulatory initiatives could be enhanced.

77. HM Government (2021) Greening Finance: A Roadmap to Sustainable Investing
78. HM Government (2023) Mobilising Green Investment: 2023 Green Finance Strategy

5.1a. Informing investors and consumers

The UK Government is introducing requirements for businesses to disclose decision-useful information on their nature-related impacts, dependencies, risks and opportunities.

Transparency about nature-related risks and opportunities will incentivise investment in companies and assets that are effectively managing their nature-related risks and capitalising on the opportunities presented by the transition to a more nature-positive economy. Meanwhile, transparency about the nature-related impacts and credentials of investments will facilitate genuinely nature-positive investments. Transparency about nature-related impacts, dependencies, risks and opportunities can additionally create an enabling environment for innovation, including MRV solutions.

To incentivise the flow of nature-related information to market participants, the UK is developing several landmark regulatory initiatives that build on its world-leading climate-related regulation to target sustainability issues more broadly and position nature as a key component of UK sustainability regulation.

79. HM Government (2023) Mobilising Green Investment: 2023 Green Finance Strategy
80. IFRS (2023) Sustainability Disclosure Standards: Consultation on Agenda Priorities

UK Sustainability Disclosure Requirements

UK Sustainability Disclosure Requirements (SDR) is intended to elicit disclosures on sustainability factors, including nature, across the economy. The nature-related components of SDR are expected to be based mainly on the TNFD Framework.[79] For corporates, these requirements may be introduced via UK-adapted versions of the ISSB standards. The ISSB standards currently capture nature-related issues in IFRS S1 General Requirements for Disclosure of Sustainability-related Financial Information. The ISSB is also seeking views on a proposed research project related to nature to lay the groundwork for potential future standard setting and targeted enhancements to IFRS S2 Climate-related Disclosures for climate-adjacent risks and opportunities.[80] As part of this project, the ISSB is expected to draw on the work of the TNFD and the Science Based Targets Network.

Acknowledging the risks facing the UK economy as a result of nature loss, the Government should consider encouraging businesses to voluntarily align their reporting with the TNFD Framework while the ISSB is advancing its proposed project on nature. This would build momentum and capabilities on nature-related disclosures ahead of the ISSB finalising its project and UK reporting requirements being introduced via UK SDR. While the final regulatory requirements may not align exactly with the TNFD Framework, early adoption by organisations would help businesses lay the groundwork for nature-related reporting and ensure that they are prepared for eventual regulatory requirements.

5.1a. Informing investors and consumers

Transition Plan Disclosures

UK SDR is expected to include transition planning-related disclosure requirements based on the outputs of the UK Transition Plan Taskforce (TPT). The TPT is currently exploring how nature should be integrated into its draft Disclosure Framework and Implementation Guidance,[81] which it intends to finalise in October 2023.

The Government and the Financial Conduct Authority (FCA) have committed[82] to considering the outputs of the TPT when strengthening transition planning disclosure requirements for asset managers, regulated asset owners and listed companies as part of UK SDR. For private companies, the Government has committed[83] to consulting on transition plan disclosure requirements that match existing FCA requirements for listed companies, which are based on TCFD Guidance.

The Government and the FCA should consider incorporating the anticipated TPT Framework, including any guidance on nature, into any proposed transition planning disclosure requirements as part of UK SDR. Doing this would avoid disparity between the requirements for listed and private companies, and would ensure that investors have information on how companies across the economy are considering nature as part of their transition planning. It would also ensure that financial services firms have the data they need from real economy companies to guide their own transition efforts.

UK Green Taxonomy

The UK is developing a UK Green Taxonomy that will provide a common framework to define economic activities that can be defined as environmentally sustainable. Organisations could be required to report on how Taxonomy-aligned their economic activities are against specific Key Performance Indicators (KPIs), such as firms' revenue and capital expenditure, as part of UK SDR. This would help investors substantiate organisations' environmental claims and assess alignment with the Government's definitions of "green" economic activities. The UK Green Taxonomy is expected to cover six environmental objectives, several of which relate to nature, including sustainable use and protection of water and marine resources; transition to a circular economy; pollution prevention and control; and protection and restoration of biodiversity and ecosystems. All of the environmental objectives will have some link to nature, due to the "Do No Significant Harm" (DNSH) aspect of Taxonomy alignment, which will see nature considered even for activities that may not have an obvious link to nature.

In its updated Green Finance Strategy, the Government announced its intention to make reporting against the UK Green Taxonomy voluntary for the first two years and committed to an initial consultation on its proposals for a UK Green Taxonomy in the autumn of 2023. In that consultation, it would be beneficial for the Government to provide clarity on timings for developing Technical Screening Criteria for the nature-related elements of the UK Green Taxonomy and on its approach to the principle of DNSH.

RECOMMENDATIONS:

1. Encourage businesses to voluntarily align their reporting with the TNFD Framework in anticipation of future regulation.
2. When designing transition plan disclosure requirements as part of UK SDR, incorporate the TPT outputs, including the TPT's anticipated guidance on nature.
3. In its autumn consultation on the UK Green Taxonomy, it would be beneficial for the UK Government to provide clarity on timings for developing Technical Screening Criteria for the nature-related objectives and its approach to the principle of DNSH.

81. TPT (2022) The Transition Plan Taskforce Disclosure Framework
82. HM Treasury (2021) Fact Sheet: Net Zero-aligned Financial Centre
83. HM Government (2023) Mobilising Green Investment: 2023 Green Finance Strategy

5.1b. Acting on the information

The UK Government is creating expectations and requirements to mainstream nature-related information into business and financial decisions.

To become a global leader in nature finance, the UK financial system will need to shift beyond transparency and high-quality reporting towards ensuring that nature-related issues are central to business and investment decision making. The UK has taken some important steps towards moving beyond disclosure and mainstreaming nature into business and financial decision making by ensuring that sustainable and nature-positive investment products are clearly signposted to investors and that UK regulators consider biodiversity and other nature-related issues when discharging their functions. These globally-leading initiatives will facilitate the shift of financial flows towards nature-positive projects and activities.

Proposed sustainable investment labels

Sustainable Focus:
Products investing in assets that a “reasonable” investor would consider sustainable.

Sustainable Improvers:
Products investing to improve the sustainability of assets.

Sustainable Impact:
Products investing in solutions to environmental and social problems.

Sustainable investment labels

In October 2022, the FCA published a consultation seeking views on a package of new measures, including a new sustainable investment labelling regime for investment products and associated rules restricting the use of certain sustainability-related terms for products that do not use a label. These measures, which are the first of their kind internationally, will help drive investor action and ensure that nature, along with other sustainability factors, is mainstreamed into investment decision making.

The proposed labels will help consumers navigate an increasingly complex sustainable investment landscape, supporting them to identify nature-positive and other sustainable investments, and enabling them more easily to factor environmental and social considerations - including those related to nature - into their investment decision making. The FCA is due to publish a Policy Statement containing the finalised rules in Q4 2023.

5.1b. Acting on the information

FCA proposed anti-greenwashing rule

In its Consultation Paper CP22/20, the FCA proposed a general "anti-greenwashing" rule for all FCA-regulated firms. This rule, which would apply more broadly than the naming and marketing rules and would not be linked to the sustainable labelling regime, would ensure that the naming and marketing of financial products and services is consistent with their sustainability profile.

By applying this rule to all FCA-regulated firms, the FCA will help cultivate investor confidence and trust in firms' sustainability claims, including those relating to nature, facilitating investor action to align their investments with nature and broader sustainability objectives. The FCA has proposed that this rule take effect as soon as it publishes the Policy Statement containing its finalised rules in Q4 2023.

Regulatory principles

The Financial Services and Markets Act 2023[84] expanded the FCA and Prudential Regulatory Authority (PRA) regulatory principles to require them to have regard to the need to contribute towards the UK's environmental targets when exercising their functions. Equivalent requirements will also apply to the Bank of England (in respect of its financial market infrastructure functions) and to the Payment Systems Regulator.

The newly expanded regulatory principles are significant because they introduce explicit mandates for regulators to consider biodiversity and other nature-related issues when discharging their functions. This will embed the Government's commitment to nature-positive growth in regulators' functions, including both the creation of new rules and supervision of relevant sectors.

Pursuant to the new regulatory principles, UK regulators can be expected to increase their focus on nature and to allocate more resources towards nature-related supervision and regulation. Businesses should expect increased supervisory scrutiny on nature-related issues, for example whether they are "greenwashing" by overstating their credentials on nature, and regulatory intervention relating to nature.

The UK Financial Reporting Council's world-leading UK Stewardship Code

The UK Financial Reporting Council's (FRC) Stewardship Code[85] sets standards on the responsible allocation, management and oversight of capital and requirements for investors to evidence their commitment to effective stewardship through reporting. In October 2021, the UK Government set out expectations on stewardship in its Roadmap to Sustainable Investing[86], including that organisations become signatories of the UK Stewardship Code, take into account the information generated by UK SDR when allocating capital, and actively monitor, encourage, and challenge companies by using their rights and influence to promote sustainable value generation.

In Q4 2023, the FRC, working with the Government, the FCA and the Pensions Regulator, will review the regulatory framework for effective stewardship and will assess whether there is a need for further regulation in this area. Strengthening UK regulation on stewardship could help ensure that economically significant asset owners, asset managers, and the service providers that support them actively contribute to a more nature-positive economy.

84. Financial Services and Markets Act (2023)
85. FRC (2020) UK Stewardship Code
86. HM Government (2021) Greening Finance: A Roadmap to Sustainable Investing

5.1c. Shifting financial flows

The UK Government and regulators have begun work on ensuring that financial flows across the economy shift to align with the UK's environmental goals, including on nature.

A global centre for nature finance should require alignment of financial flows with environmental targets. To do this, financial flows must shift across the economy, which will require transformation within businesses' governance, strategy and risk management processes. The UK Government and regulators have started to explore how regulation could require businesses to transform their practices, integrating nature considerations throughout their organisation. A clear example of this is explored in Box 10, which provides an overview of the UK's current work to prevent the use of certain commodities linked to deforestation.

FCA discussion paper on sustainability-related governance, incentives and competence in regulated firms

In February 2023, the FCA published a discussion paper on *Finance for positive sustainable change: governance, incentives and competence in regulated firms*.[87] The discussion paper seeks views on how regulated firms are approaching sustainability governance and culture, based on which the FCA will consider whether further regulatory intervention is necessary.

In the discussion paper, the FCA asks a range of questions across several key themes, including:

- Whether firms should be expected to embed sustainability-related considerations into their business objectives and strategies.
- What sustainability-related factors firms should consider when designing their remuneration and incentive plans.

The issues raised in the paper represent a possible shift towards requiring firms to make changes to their business objectives, strategies, governance, and remuneration and incentive arrangements to align with the UK's sustainability goals, including the UK's GBF commitments. The Discussion Paper closed on 10 May 2023 and the FCA will consider the feedback received before publishing a response and determining next steps.

RECOMMENDATIONS

1. To ensure coordination across the economy, the UK Government could consider exploring how private and other real-economy companies are approaching sustainability (including nature-related) governance and culture. This could help drive transformation within the real economy as well as in the financial services sector.

BOX 10 - UK DEFORESTATION-FREE COMMODITIES LEGISLATION

Schedule 17 of the UK Environment Act 2021 prevents the use of certain commodities linked to deforestation in UK commercial activities by large businesses unless relevant local laws are observed. Businesses that use the specified commodities, or their derivatives, must perform due diligence on them and take steps to mitigate any identified deforestation risks. Businesses must also publish information about the commodities in their annual reports.

The UK Government is developing secondary legislation that will specify the commodities, the precise scope of companies, and the detailed due diligence and reporting requirements. Defra has consulted on these key areas and committed to legislating at the earliest opportunity.[88] In designing its legislation, the UK Government could aim to at least match the ambition of the European Union Deforestation-free Regulation which requires companies to determine the precise geolocation, date and time range in which specified commodities were produced, carry out risk assessments related to each of their products and outline risk mitigation actions.

The UK requirements will not capture all businesses that contribute to deforestation. For example, they do not include measures targeting the financing of commodities linked to deforestation.[89] Additionally, small and medium-sized businesses will not be captured despite potentially contributing significantly to deforestation.

The Financial Services and Markets Act 2023 introduced an obligation for HM Treasury to review the effectiveness of UK regulation in eliminating the financing of commodities linked to deforestation. If HM Treasury were to propose regulation targeting the financing of deforestation by the financial services sector as a result of its review, and if the Government were to develop scoping requirements based on the amount of restricted commodity used by a company rather than company size as part of its secondary legislation, the UK's position as a nature finance hub would be strengthened.[90]

87. FCA (2023) Finance for Positive Sustainable Change
88. Defra (2022) Consultation on implementing due diligence on forest risk commodities
89. HM Government (2023) Financial Services and Markets Act 2023
90. HM Government (2021) Fact Sheet: Net Zero-aligned Financial Centre

5.2. Advance Central Bank oversight

The Bank of England and Prudential Regulation Authority should consider the supervisory steps needed to ensure that the safety and soundness of regulated firms are not impacted by nature-related financial risks, while also securing an appropriate degree of protection for insurance policyholders from those risks.

As a critical node for maintaining financial stability, the UK cannot be considered a global centre for nature finance if its central bank is not appropriately considering and acting on nature-related risks.

Central banks have begun to consider the impact of nature-related financial risks on their respective economies, publishing the results of their findings. In 2020, the Der Nederlandsche Bank (DNB) produced a report titled "Indebted to Nature"[91] which considered the relationship between biodiversity risks and the Dutch economy. The report highlighted that Dutch financial institutions worldwide have £457 billion in exposure to companies with high or very high dependency on one or more ecosystem services, which comprised 36% of the portfolio examined by the DNB. A report[92] published by the Banque de France in 2021 identified a similar finding: 42% of the market value of securities held by French financial institutions was derived from companies that are highly or very highly dependent on at least one ecosystem service.

In line with this trend, it was announced in April 2023 that with the backing of Defra and the Bank of England, the Green Finance Institute would lead new analysis in collaboration with the UN Environment Programme World Conservation Monitoring Centre and the Universities of Oxford and Reading to quantify UK financial and economic risks from exposure to nature degradation.[93]

Given the relatively consistent findings of the DNB and Banque de France reports, the UK study is likely to arrive at a similar set of results which would indicate a level of material risk to exposed UK banks and insurers. If the UK is to position itself as a global centre for nature finance then the next steps following completion of the study are to develop a more proactive supervisory and regulatory approach for nature-related risks.

The UK was the first nation to publish specific supervisory guidance for the management of climate-related financial risks. It should consider doing the same for nature-related financial risks with the PRA consulting on and subsequently publishing a supervisory statement for nature-related financial risks. The Supervisory Statement (SS) should seek to adopt a similar set of requirements as those utilised in SS3/19 - *Enhancing banks' and insurers' approaches to managing the financial risks from climate change*[94] - (governance, risk management, scenario analysis and disclosure) and could employ the same principles of approach (proportionate, holistic, ambitious, strategic).

Further impetus for this approach has been provided by the recent introduction of the Financial Services and Markets Act 2023[95] which expanded the PRA's regulatory principles, explicitly requiring the PRA to have regard to the need to contribute towards the UK's environmental targets when exercising its functions. If the PRA is to meet the spirit and detail of this new obligation then it will require more than a simple "have regard" when assessing the response by banks and insurers to nature-related financial risks. A coherent supervisory approach to nature-related financial risks would enable the PRA to demonstrate tangible progress against the nature-related element of its regulatory principles.

The foundations for this supervisory approach could be drawn from the Network for Greening the Financial System's (NGFS) recently published technical note *Nature-related Financial Risks: a Conceptual Framework to guide Action by Central Banks and Supervisors*. Climate and nature-related financial risks should not be considered in isolation and the NGFS guide provides an important first step towards developing an integrated assessment of climate and broader nature-related risks.[96]

In addition to managing micro-prudential risks through the PRA, the objective of the Bank of England is to protect and enhance the UK's financial system. The DNB and Banque de France reports indicate that nature-related financial risks, when aggregated at a sector or economy-wide level, present a risk to financial stability given the significant dependency on nature for economic or financial outputs. This risk presents an opportunity for the Bank of England to explore how it might deliver a nature-focused stress test for banks and insurers. Such a stress test would consider and seek to understand the current and future impacts on the UK economy generated by the depletion of natural capital at both a firm and sectoral level.

RECOMMENDATIONS

1. The PRA should consider publishing specific supervisory guidance for the management of nature-related financial risks.
2. The Bank of England should seek to understand nature-related risks across the financial system in anticipation of the possibility of a future nature-focused stress test for banks and insurers.

91. DNB (2020) Indebted to nature
92. Banque De France (2021) A "Silent Spring" for the Financial System? Exploring Biodiversity-Related Financial Risks in France
93. GFI (2023) UK economy's nature-related risk to be assessed for the first time
94. Bank of England Prudential Regulation Authority (2019) Supervisory Statement | SS3/19. Enhancing banks' and insurers' approaches to managing the financial risks from climate change
95. Financial Services and Markets Act (2023)
96. Network for Greening the Financial System (2023) Nature-related Financial Risks: a Conceptual Framework to guide Action by Central Banks and Supervisors

Conclusion

Conclusion

Financing nature

The UK has a strong foundation for financing nature, partially due to the infrastructure, services and expertise that have been built up to support climate finance, a field in which the UK has consistently been world-leading.

With global policy and market signals boosting the profile of nature and biodiversity recovery, now is the time for the UK to build upon these strong credentials and create a supportive enabling environment for the development of socially responsible and high integrity nature markets. The vast stores of comparatively patient capital concentrated in the insurance and long-term savings institutions that dominate our finance sector are ideal for financing nature projects. Therefore, UK institutions in this sector - as well others such as banks and asset managers - should be bold in their investment strategies, building their nature-related portfolios and utilising innovative new financing mechanisms and products to boost wider participation in nature markets.

This must be facilitated by UK-based services in legal, regulatory and advisory sectors, who should seize this market opportunity to develop their expertise in supporting nature-related investments, with a view to exporting this knowledge globally. The growth of nature markets in the UK can be further accelerated by public finance institutions working to develop and provide mechanisms to de-risk early investment opportunities in nature.

Integrating nature into the financial system

The UK is playing a leading role in sustainability regulation, and is paving the way for other countries to support the growth of nature finance within their own economies. The UK's ambitious three-phase plan to green the financial system will be key to maintaining its position as a global leader in this space. In advancing its regulatory framework, the UK should continue to prioritise international interoperability to facilitate consistency and comparability globally.

The UK can consolidate and advance its position as a global leader on sustainability regulation by ensuring that businesses and financial institutions understand and are addressing their nature-related risks. To ensure consistency within the UK economy and provide certainty to businesses, the Government could publish a roadmap for moving beyond disclosure and advancing phases two and three of its plan in a coordinated and sequenced way across the economy.

Glossary

Biodiversity: Biodiversity is the variability among living organisms from all sources including terrestrial, marine and other aquatic ecosystems and the ecological complexes of which they are a part.[97]

Concessional capital: Below market rate finance provided by financial institutions such as development banks and multilateral funds in the interest of accelerating a development objective,[98] such as the preservation and restoration of nature.

Global Biodiversity Framework: The Kunming-Montreal Global Biodiversity Framework was a non-binding agreement signed by 196 nations at CBD COP15, seeking to halt and reverse biodiversity loss to achieve a nature-positive world by 2050.[99]

Global centre for nature finance: A geographical location with a high concentration of financial services institutions which allocate capital (and related professional services and technical expertise) domestically and internationally into the preservation and restoration of nature and biodiversity. This term also encompasses the enabling environment provided by governments, regulators, advisory and intermediary services that incentivise or de-risk investment.

Monitoring, reporting and verification (MRV): MRV refers to the processes whereby factual information is provided, examined and assessed to see whether parties meet their obligations.[100]

Nature: Nature is 'the natural world', with an emphasis on the diversity of living organisms (including people) and their interactions among themselves and with their environment (land, ocean, freshwater and atmosphere).[101]

Nature-based solutions: Nature-based solutions are actions to protect, sustainably manage, and restore natural and modified ecosystems that address societal challenges effectively and adaptively, simultaneously benefiting people and nature.[102]

Natural capital: Natural capital is the stock of renewable and non-renewable natural resources (e.g. plants, animals, air, water, soils, minerals) that combine to yield a flow of benefits to people.[103]

Natural credit market: Nature markets are mechanisms "for private investment in nature through the sale of units of ecosystem services, which are delivered by nature restoration projects or improvements to land or coastal management", encompassing voluntary credits and compliance credits purchased in order to meet regulatory requirements.[104]

Nature-related impacts, dependencies, risks, and opportunities:

- **Nature-related impacts** are changes in the state of nature, which may result in changes to the capacity of nature to provide social and economic functions. Their impacts can be positive or negative, as a result of an organisation's or another party's actions and can be direct, indirect or cumulative.
- **Nature-related dependencies** are aspects of ecosystem services that an organisation or other actor relies on to function. Dependencies include ecosystems' ability to regulate water flow, water quality, and hazards like fires and floods; provide a suitable habitat for pollinators (who in turn provide a service directly to economies), and sequester carbon (in terrestrial, freshwater and marine realms.
- **Nature-related risks** are potential threats posed to an organisation linked to their and wider society's dependencies on nature and nature impacts that can derive from physical, transition and systemic risks.
- **Nature-related opportunities** are generated through impacts and dependencies on nature, and can occur:
  - When organisations avoid, reduce, mitigate or manage nature-related risks
  - Through the transformation of business models, products, services, markets and investments that work to reverse the loss of nature.[105]

Nature-positive: While the term itself does not have a universally agreed definition, the IUCN has proposed the following working definition: "A nature-positive future means that we, as a global society, halt and reverse the loss of nature measured from its current status, reducing future negative impacts alongside restoring and renewing nature, to put both living and non-living nature measurably on the path to recovery."[106]

Nature-positive transition: The transition to a nature-positive state will involve both incremental and transformative changes at a project, organisational or societal level. The nature positive transition describes the journey from a state of nature loss, through no net loss of nature, and on to a state of nature recovery.

97. IPBES (2023) Glossary: Biodiversity
98. World Bank (2021) What You Need to Know About Concessional Finance for Climate Action
99. Convention on Biological Diversity (2023) Kunming-Montreal Global Biodiversity Framework
100. ISSD (2012) Measurement, Reporting and Verification: A note on the concept with an annotated bibliography
101. IPBES (2015) The IPBES Conceptual Framework - connecting nature and people
102. IUCN (2023) Nature-based Solutions
103. Natural Capital Coalition (2016) Natural Capital Protocol: a primer for business
104. HM Government (2023) Nature markets: A framework for scaling up private investment in nature recovery and sustainable farming
105. TNFD (2023) Concepts and Definitions
106. IUCN (2022) Towards an IUCN nature-positive approach: a working paper

Acknowledgments

We would like to thank all of the individuals and organisations that contributed to the engagement process that supported the development of this report. In particular, we would like to thank Helen Avery, Ryan Jude, Felicity Hall, Ashleigh Lee, Kerstin Mathias, Will Evison, James King, Theo Bromfield, Rona Nairn, Lewis Brusby, Nikul Pandya, Galia Wells, Lucas Penfold, James Rowe and Jon Williams for their contributions to the report.

About the City of London Corporation

The City of London Corporation is the governing body of the Square Mile dedicated to a vibrant and thriving City, supporting a diverse and sustainable London within a globally successful UK.

We aim to:

- Contribute to a flourishing society
- Support a thriving economy
- Shape outstanding environments

By strengthening the connections, capacity and character of the City, London and the UK for the benefit of people who live, work and visit here.

About the Global City campaign

The Global City campaign is the City of London Corporation's overarching initiative to promote the UK as a world-leading international financial centre. It showcases the UK as a great place for financial and professional services firms to invest, locate and grow.

theglobalcity.uk

About PwC

At PwC, we combine human ingenuity with technology and data to help our clients create commercial and societal value and turn their Environmental, Social and Governance ambitions into action.

Centre for Nature Positive Business

PwC's global Centre for Nature Positive Business unites more than 500 nature specialists from across our network. Bringing together knowledge in biodiversity, water, forestry, regenerative agriculture and geospatial analysis, the Centre is accelerating the global transition to a nature positive and netzero future.

https://www.pwc.com/nature

About The Green Finance Institute

The Green Finance Institute is an independent, commercially focused organisation, supported by HM Treasury, the Department for Environment, Food and Rural Affairs, the City of London Corporation, and other philanthropic funders. As the UK's principal forum for public and private sector collaboration in green finance, it is uniquely placed to mobilise capital to accelerate the domestic and international transition to a sustainable, net-zero carbon economy that is also climate resilient. The Green Finance Institute convenes and leads mission-led coalitions to identify and unlock barriers to deploy capital at pace and scale towards impactful, real-economy outcomes.

The GFI Hive's mission is to increase investment in nature restoration, nature-based solutions and nature-positive outcomes in and for the UK. We work with the finance sector, government, academia, environmental NGOs and land managers to identify and unlock barriers to this mission, and act as a knowledge hub on private investment in nature to increase shared learning, best practices and investment appetite.

www.greenfinanceinstitute.co.uk/gfihive

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