UNEP FI & HypoVereinsbank Event
The New Frontier – Towards a Collaborative Effort by Financial Institutions to Integrate Biodiversity and Ecosystem Services into Business

An increasing number of financial institutions (FIs) are realising the growing materiality of environmental risks and opportunities. Increasingly, members of the finance community are also responding to this increased recognition for natural capital, and the pressing need to understand systemic risk in a far more holistic way. Around 35 institutions - including banks, investors, rating agencies and NGOs - came together at Hypovereinsbank to discuss the current recognition and understanding of natural capital in the finance sector, as well as the rationale behind developing a statement to further embed biodiversity and ecosystem services in the finance sector. This summary outlines key elements of the discussion and the proposed agenda for moving the debate on natural capital forward, potentially through the support of a statement on embedding Biodiversity and Ecosystem Services (BES) into the finance sector.

1. Natural capital & finance: the background

What do we mean by natural capital?

An important objective of the workshop was to discuss how to advance the understanding and integration of biodiversity and ecosystem services (BES) criteria and risk management, lending and investment products. When we refer to natural capital we are referring to both biodiversity and ecosystem services. In the UNEP FI CEO Briefing 'Demystifying Materiality', biodiversity is termed as the 'variability among living organisms, which includes the diversity at ecosystem, species and genetic levels' (Art. 2, Convention on Biological Diversity). Ecosystem services are the goods and services that biodiversity provides. We will use the terms natural capital and BES interchangeably in this document.

How does natural capital impact finance?

A number of recent reports, including TEEB and the CEO Briefing, have outlined that BES is becoming increasingly material for banks and lenders, particularly in addition to the growing public awareness around the issue of environmental degradation. Financial institutions should be thinking about both impacts and dependence on BES and framing risk as more than just reputational but also physical, regulatory, market, legal, operational and capital. One of the main drivers for the integration of BES into lending are the benchmark standards from the World Bank Group, including the IFC Performance Standard (i.e. PS6) which impact the Equator Principle (EP) Banks. The mitigation hierarchy advises banks to 1) avoid 2) minimise 3) relocate 4) repair/renaturate 5) offset as much of their ecological footprint as possible.

Other tools available to EP Banks include the Integrated Biodiversity Assessment Tool (IBAT), Environmental Impact Assessments (EIA), roundtables and standards, biodiversity offsets, NGO partnerships, investor questionnaires such as SAM, CDP and Alcom, as well as the Natural Value Initiative (NVI). Despite the proliferation of methods, a proxy KPI for BES is still missing, in the way that carbon serves climate

change. This is part of the reason that the topic of BES still plays almost no role in investment decisions. Improvements could be made through standards and regulatory tools, triggering analysts to look at these issues and make natural resources more expensive. Additionally, BES could be better factored into rations, but it seems unlikely that rating agencies would be ready for such complex calculations for so many companies.

2. Where is the upside?

There are some areas of innovation, where investors can play a forward-thinking role in treating natural capital issues as drivers of shareholder value. While regulatory drivers can act as a stick to the finance industry, carrots can be found in market drivers and consumer choices (FSC, MSC), encouraging more positive behaviour. FIs should be looking at where those eco-conscious consumer trends are heading, and how they are placed to support developments in market behaviour. Responsible investment should be moving in the direction of 'impact investment'. In particular investors with large diversified portfolios (such as pension funds) should be thinking beyond only financial risk and return, to recognising both short-term and long-term impacts that can impinge on a portfolio, as well focussing more on the long-term generation of financial value.

3. Where are the major challenges?

Participants noted that one of the major challenges remaining was to define natural capital and its relevance to different groups in a meaningful way within the sector as well as across other sectors. Moving beyond a traditional comprehension of direct and indirect risks is still very challenging, primarily in terms of the difficulty to quantify environmental disasters with credit failure, as so many factors may also lead to this. Finally, participants highlighted that the time consuming nature of engagement not only with the company, but equally along the entire supply chain is also an impediment to fully embedding BES issues.

4. Further embedding BES risks: statements & principles?

The afternoon session focussed on familiarising participants with the Biodiversity Principles, developed by the VfU-Forum Biodiversity Working Group in 2010, and the Natural Capital Statement. While the Biodiversity Principles have gone quite a way towards elaborating how FIs should take BES into account, FIs are not yet ready to sign such principles because of concern about accounting for their actions to meet them . Questions remain as to whether this is the right way to go? Should further work be done to develop the indicators more? A general invitation to support the working group was extended.

So far a series of workshops in Nagoya, Hong Kong and London have discussed the rationale and scope for a Natural Capital Statement to further embed BES into the finance sector. Participants finished the day by moving on the discussion of the rationale for such a statement, and if there was one, how the Biodiversity Principles should relate to it.

Generally, it was felt that the statement was useful as a mission statement, while the principles offered more operational guidance. However, one issue is that when more detail is added to the statement, the overlap with guidelines such as IFC PF6 increases and it becomes harder to convince both leaders and laggards in the field to sign up (leaders because they already have their commitments and laggards because it becomes too ambitious for them). Through the afternoon break-out session, a number of key points for discussion were posed. From these and the discussion the following key points for clarification and development can be summarised:

- For whom should the statement be?
    - What is the intended audience?
        - Should it aim at leaders or laggards?
- What would be the aim?
    - Should it be pitched as an important market signal?
    - Should it point the way forward for those who are further behind but also be relevant to leaders?
- How should it relate to other initiatives/statements/performance standards/internal policies?
    - Do we need something more cohesive to bring all these other efforts together?
- What could its USP be?

5. <u>The way forward</u>

A number of participants expressed their interest at moving the potential statement forward. In order to advance the discussion and momentum for a potential statement, UNEP FI will now be consolidating input from all four working sessions on the statement to clarify answers to the points listed above. We will then be following up with meeting participants and interested parties to engage with committed parties and establish a clear way forward.

With many thanks to the participants and to Irina Detlefson of HypoVereinsbank for hosting the meeting, as well as those who presented.

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