

**Title: Investment in a nature-rich future****Date: 09 December 2020**

<b>Purpose:</b>	This paper follows up on <i>Green Finance – SNH Priorities</i> (BOARD/182/11) considered by the Board in December 2019. It updates the Board on the development of Environmental Green Finance in Scotland including NatureScot's role, current activity and future priorities.
<b>How does this link with our corporate priorities of improving biodiversity or delivering nature-based solutions to climate change</b>	<p>New and increased investment is key to our all of our offers presented in <i>NatureScot: Our Future Organisation</i> (BOARD/187/08) to:</p> <ul style="list-style-type: none"> <li>• Advance nature-based solutions to secure a thriving environment for all;</li> <li>• Tackle the climate emergency by leading net zero natural resource management on land and sea;</li> <li>• Redefine economic value by embedding the benefits of natural capital.</li> </ul> <p>NatureScot is in a unique position to lead change because we are Scotland's nature agency. Finance is where our three core offers meet – on nature-based solutions and net zero natural resource management, both of which require finance, and on natural capital, which provides much of the conceptual and evidential basis for investment.</p>
<b>Summary:</b>	Traditional public and philanthropic sources of funding for nature-based solutions and net-zero natural resource management will be insufficient to address the key challenges of the climate and nature emergencies. The paper sets out a vision of the future, defines NatureScot's role in increasing private investment, and identifies the key actions we will take in the next 12 months and beyond.
<b>Recommendations:</b>	The Board are asked to support and endorse the role that NatureScot are playing in this area of our work.
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## Purpose

1. This paper provides the Board with an update on NatureScot's contribution to the development of Environmental Green Finance (EGF) in Scotland. Diversifying the financing of investment in nature, in particular increasing the flow of private finance, is essential for delivery of nature-based solutions and net-zero natural resource management.

## Background

2. This paper follows another considered by the Board in December 2019 (*Green Finance – SNH Priorities* - BOARD/182/11). This topic is central to delivery of NatureScot's vision, strategic priorities and offer as set out in *NatureScot: Our Future Organisation* (BOARD/187/08).
3. The business case for biodiversity and natural capital has been made powerfully in many reports and speeches in recent years. As just one example, the World Economic Forum's New Nature Economy Report, *Nature Risk Rising*, published in January 2020, highlighted that \$44 trillion of economic value generation – over half the world's total GDP – is potentially at risk as a result of the dependence of business on nature and its services.

## The problem

4. **There is a dramatic gap between the finance needed to protect and restore nature and that currently deployed.** As an example, the total cost of restoring all of Scotland's damaged peatlands has been estimated at £3 billion. Most of the money still comes from public or philanthropic sources, despite the growing interest from investors in financing the 2030 Sustainable Development Goals (SDGs). The EGF agenda is concerned with diversifying beyond these traditional sources into investment from businesses and financial markets, and blending public and private finance together.
5. How do we go about bridging the gap in Scotland and drive more private finance into nature and nature-based solutions? **The central problem is not the availability of capital but the lack of the mechanisms to convert the impacts of nature-based solutions into viable revenue streams to service the capital.**
6. To meet this challenge Scotland needs the organisational, technical, regulatory, social and financial capacity that will combine to realise significant new private investment in natural assets, protecting and increasing biodiversity, increasing our stocks of natural capital, and growing the flow of benefits from nature-based solutions to communities and businesses across Scotland. This system of supports and enablers is very immature in Scotland and **systemic change is required** to realise it.
7. There are many actors in EGF. Primarily, of course, investors and suppliers of natural assets such as land managers. Investors themselves come in different shapes and sizes, with varying motivations and appetites for risk and return. Government has a critical role in establishing the framework. In addition there is a requirement for an array of project developers, brokers and other intermediaries. In this complex landscape it is critical that NatureScot identifies and fulfils the most helpful role.

## NatureScot's vision and role

8. NatureScot has established an Environmental Green Finance Programme, the vision of which is to **secure 'a step change in investment, in particular from the private sector, to fund a nature-rich future and unleash nature's ability to mitigate climate change and**

*enable society to adapt to it*. EGF will become ‘business as usual’. It will be aligned with public value as well as the business cases that will drive the natural asset economy. Policy, regulation and blended public/private finance will make sure that this investment delivers both public goods and private benefits. It will enable the reduction of greenhouse gas emissions from Scotland’s land, a task that will become increasingly important as emissions from other sources decline and will be the only show in town from 2045 onward, when maintaining net zero will be all about how we use our natural resources

9. Following the definition of the problem in 5 and the scoping of the solution in 6 it is clear that achieving this vision requires us to collaborate in systemic change. The prize here is not to access a few £million for NatureScot but to enable investment of £100’s of millions, and even £billions of new finance in nature through new marketplaces.
10. NatureScot is in a unique position to lead change because we are Scotland’s nature agency. Finance is where our three core offers meet – on nature-based solutions and net zero natural resource management, both of which require finance, and on natural capital, which provides much of the conceptual and evidential basis for investment.
11. Responding to this challenge, we will adopt three roles. We will provide **strong leadership** through:
  - **Convening stakeholders**
  - Using our expertise in biodiversity, nature-based solutions and natural capital to **develop tools and evidence** and
  - **Influencing national and local government, business, finance and eNGOs** to embrace environmental green finance.
12. We will not seek to be an actor in markets but may acquire and deploy environmental green finance in limited circumstances, for instance to restore peatland, especially where doing so will add significantly to what we can deliver with public funds and/or help to demonstrate new business models.

### **A summary of current work**

13. The following is a brief account of current and planned work.
  - Chair of Economy and Environment Leaders Group Green Finance sub-group
    - ‘Building a portfolio of policy options to drive private investment to protect and enhance Scotland’s natural capital’ for the government’s Global Climate Emergency Programme
    - ‘Facilitating local investment in natural capital’ – We are leading a project<sup>1</sup> aiming to develop and test innovative approaches that could be used by regional partnerships across Scotland to increase investment in natural capital, especially from the private sector. The outputs will include new business models that can be shared and implemented
  - Collaborating on the critical interventions required to establish a natural assets economy, and position Scotland as a lead market for natural assets with the capacity to export the tools and expertise across the world

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<sup>1</sup> Co-funded by NatureScot, Scottish Government, Scottish Forestry and the Scottish Land Commission and partnered regionally with the Tweed Forum.

- Working with government, the private and third sectors and Dark Matter Laboratories (who also work with SNIB and Scottish Exchequer) to develop and test the new approaches, tools and ways of working required to grow the natural assets economy in Scotland
- Peatland restoration
  - Putting the Peatland Code at parity with the Woodland Carbon Code as a tool to support private investment in restoration, generating carbon units to trade in the UK voluntary emissions market
  - In discussion with a range of private investors to identify opportunities for peatland restoration
- £1 Billion Challenge Routemap
  - Supporting the progression of the nine pillars of the £1 billion Challenge Routemap
  - Employing a development officer for the Scottish Marine Environmental Enhancement Fund, which will provide a mechanism for sectors that use the marine environment to contribute to practical conservation and restoration projects to help strengthen the resilience of the marine and coastal environment

### **A summary of stakeholder engagement**

14. As described in 6, the landscape of EGF is complex with many actors. Being an immature field the assortment of stakeholders is also quite dynamic. We are engaging with stakeholders through both planned and opportunistic approaches.
15. Our main links with government and other public sector bodies is through the EELG sub-group on Green Finance. We co-chair this with Scottish Government and it includes representatives from the Directorate of International Trade & Investment (DITI) and the Scottish National Investment Bank, as well as from EELG.
16. We lead Project 7 (Future Funding) of the Scottish Biodiversity Programme. We have been asked by Scottish Development International to join the assessment panel for the Green Investment Portfolio. We are also engaged with DITI to boost the profile of natural capital in SG's next Capital Investment Plan.
17. Natural capital approaches underpin the development of new business models and the Scottish Forum on Natural Capital brings together a large number of diverse stakeholders from the public, private and third sectors. The Forum also played, and continues to play, a prominent role in the Scottish Conservation Finance Initiative and the resulting £1 Billion Challenge Routemap.
18. Our support for the nine pillars of the £1 Billion Challenge includes a leadership group of NatureScot, SEPA and SWT. With them we are cultivating an open online forum for anyone with an interest in EGF in Scotland.
19. More opportunistic engagements include:
  - Kaitiaki – advising a proposed investment fund for woodland creation and landscape scale habitat restoration
  - Landscapes as Carbon Sinks – sharing knowledge with this Edinburgh Centre for Carbon Innovation programme - 'working towards designing a systemic transformation of the land use sectors to make the whole of Scotland a net carbon sink, building on the target of the Government of Scotland of becoming carbon neutral by 2045' - and working with them on 'Flows to the Future'

- Carbon Direct – a global player bringing scientific and financial expertise to act as ‘a strategic advisor to partners with carbon removal commitments and an investor combining human and financial capital to scale carbon removal, reduction, and use’
- Global Ethical Finance Initiative (GEFI) – with SEPA and SWT trying to tap into their network to gain insights and develop new opportunities

### Opportunity and risk

20. Business and finance are going to invest more in natural capital and biodiversity. Awareness and understanding are growing fast. But this is a global trend and the opportunities are also global, especially when it comes to nature-based solutions to climate change. There is a risk that Scotland is left behind in this market but also opportunity because Scotland can offer carbon storage that is high quality in terms of both credibility and ‘charisma’ i.e. investors also get to buy-in to Scotland’s iconic natural and cultural heritage. To avoid being left out of this growing market Scotland must create high quality, credible and accessible opportunities to invest.
21. There is a risk that carbon becomes ‘the only show in town’. Whilst there are many gains for nature to be made on the coat tails of net-zero, it is completely possible to pursue carbon savings at cost to, or at least little gain for, biodiversity. Public policy and blended public/private finance can help to mitigate this risk, along with codes to support verification that encompass biodiversity.
22. There is a risk that greater private investment in nature results in ‘privatisation’ of the benefits and ‘socialisation’ of the costs. This threatens the path of a just transition. The public and eNGOs have mixed perceptions of business and finance. The risk of real, or perceived, greenwash is also significant. Both of these risks require mitigating by careful, transparent and open design of new systems through co-production with all stakeholders.
23. In the aftermath of Covid19 and EU exit and the uncertainty around public finances there is a risk that the funding gap grows even larger. SRDP (AECS and SFGS) and Peatland Action form a very large proportion of all the investment in Scottish biodiversity. It will be important to maintain public funding for nature and make it work harder for nature by placing greater emphasis on public goods for public money. At the same time it will be vital to improve the outcomes for nature from all public expenditure by minimising trade-offs and eliminating perverse subsidies. As an example, the inclusion of natural infrastructure in the Infrastructure Investment Plan offers opportunities to do both. There is also scope to increase the reach and effectiveness of public money by blending it intelligently with private finance, at the same time sharing risks and making it easier for investors to participate in new markets.

### Next Steps

24. Our priorities for the next 12 months are threefold.
- Firstly, to develop the enabling environment to drive more private finance into nature and nature-based solutions.
  - Secondly, to work with willing investors to develop a model for private investment in peatland restoration.
  - Thirdly, applying the findings of ‘Facilitating local investment in natural capital’ both in the Tweed and more widely

25. Together with SEPA and SWT we are proposing to Scottish Government a **‘Scottish Finance for Nature’ accelerator programme** which will support government, eNGOs and the private sector to collaboratively invent, innovate and scale investment. This has arisen from three converging pieces of work – the EELG Green Finance sub-group, the £1 Billion Challenge Routemap and the work that we have done with Dark Matter Laboratories over the summer to identify the critical steps required to scale investment in both peatland restoration and urban nature-based solutions. The establishment of an accelerator programme for nature finance would help scale-up nature-based solutions to climate change by fostering innovation in policy, regulation, reporting and verification, and finance.
26. We are speaking with a number of potential investors in peatland restoration, ranging greatly in size and motivation, and including a global player in carbon markets. We aim to make significant progress towards enabling and concluding at least one substantial deal for Scotland by the time of COP26.
27. In the longer term all of the work that we do on nature-based solutions will have to consider the potential to develop, use and demonstrate innovation in financing. There are three particular areas of activity where we can bring leadership to the adoption and use of EGF: the development and operation of Regional Land Use Frameworks, Regional Economic Partnership plans, and landscape-scale demonstrations of nature restoration.

#### **Resource implications**

28. Whilst NatureScot does not aspire to be an expert in finance or a market player we do need additional skills and capacity to engage credibly and effectively. We require all NatureScot staff working with nature-based solutions and net-zero management of the land and the sea to be open to the new approaches and ways of working this work demands. We need more people with skills in environmental economics and with conceptual and working knowledge of the finance sector. This is a priority area of work and must be built into the active and designed transformation of the organisation set out in *NatureScot: Our Future Organisation* (BOARD/187/08), or our customer offer will falter. We are taking steps to both upskill existing staff and to recruit new and experienced people to new posts, including a new Environmental Green Finance Manager with relevant skills and experience to add capacity and credibility to our offer.

#### **Recommendations**

29. The request to the Board is that it notes and endorses the approach and next steps set out in this paper. Views on the scope and emphasis of NatureScot’s role are also very welcome. The Board may wish to consider its role, collectively and individually in developing the profile and role of Environmental Green Finance in Scotland.