Photo by Joshua Nasielski

Global Landscapes Forum | *Paris*

Launching the new climate and development agenda

5-6 December 2015

Background Brief

Finance and trade

This background brief was prepared for participants of the 2015 Global Landscapes Forum.

Why are finance and trade important for achieving climate and development goals?

Finance is the lifeblood of the global economy. Today, the global capital market is worth about US$225 trillion (Lund et al. 2013) and is a fundamental driver of decisions affecting land use worldwide. However, the finance sector remains largely disengaged from discussions on sustainable development, despite some leveraging of private capital and noteworthy corporate initiatives (Shames et al. 2014; IISD and UNEP 2014).

A much larger proportion of finance sector profits must be channeled toward sustainable land uses if key Sustainable Development Goals (SDGs) on land, health, biodiversity, climate and food security are to be met. Estimates of the private funds needed until 2030 to meet SDGs in developing countries alone are in the range of US$805–1379 billion (Schmidt-Traub and Sachs 2015). Mobilizing capital for sustainable development on this scale will be possible only if the goals are mainstreamed into the decision making of large-scale financiers, including those in emerging economies and developing countries. The pursuit of SDGs, especially those related to landscape restoration and climate change mitigation and adaptation, will require buy-in from the private sector – as service providers or investors or both. Nevertheless, there are many constraints on private finance for the SDGs, including the short-term opportunity costs of more sustainable practices, and the business case for sustainable land use remains underexplored.

Like finance, international trade is a major driver of economic growth, and trade decisions (including trade agreements and finance) often have profound implications for the environment and for sustainable development. The volume and importance of international trade have risen rapidly in recent decades: since 1980, world trade has grown six-fold and the global economy has about tripled in size. In 2011, exports were worth more than US$22 trillion and by 2013 formed nearly a third of global GDP (IISD and UNEP 2014).

Trade liberalization can expose countries to greater scrutiny and may encourage best-practice natural resource governance. However, it can also trigger intensified pressure on ecosystems and natural resources, promote growth in carbon emissions, and make it harder for governments to pass or enforce environmental regulations. As long as economic growth is coupled to activities associated with carbon emissions and environmental degradation, it will be very hard to achieve key SDGs – without substantial trade reform. Some progress has been made toward integrating sustainability objectives into trade negotiations, but, for the most part, these are still seen as separate and secondary to economic goals.

Some institutional investors are responding to mounting customer and shareholder concerns about unsustainable practices by, for example, committing to zero deforestation and sustainable standards for commodities (e.g. BEI 2015). Large banks and others have begun to incorporate social and environmental standards into their policies, to make bold commitments, to develop new financial instruments, and to enter into partnerships with governments and civil society. Sustainable supply chain initiatives, such as the Roundtable on Sustainable Palm Oil, have been established to reward more sustainable practices, but questions about implementation remain (see Case Study).

Among key reforms needed to align finance, trade and the SDGs are carbon pricing (achievable in various ways) and a phase-out of perverse subsidies. Public subsidies of natural resource exploitation and energy consumption amounted to US$1.1 trillion in 2011 (McFarland et al. 2015). Although the implications for forestry and agriculture are unlikely to mirror those for other industries, "pricing in" climate change and other environmental costs of trade and finance will level the playing field, increase the demand for and supply of investment opportunities for sustainable land use, and give investors greater long-term certainty. Beyond broad reforms, strategies are needed to enable stakeholders, including smallholder farmers, to put investments to best use for integrated landscape management.

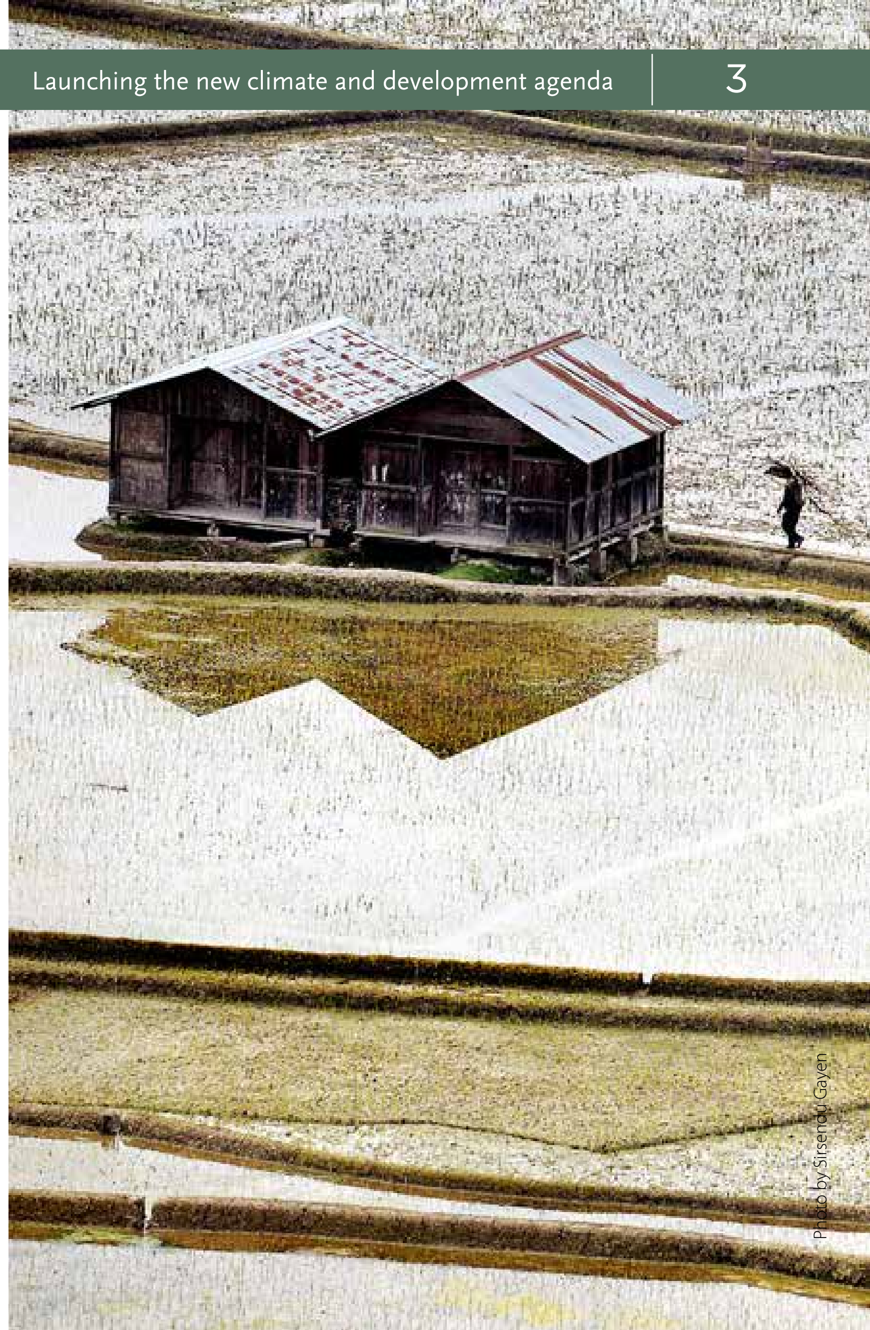

Photo by Sirsendu Gayen

What are some of the key issues?

REDD+ and other sustainable landscape investments are not always readily available.

There is a chronic shortage of quality land-use projects. Despite hopes to the contrary, there is no evidence that public sector funding is catalyzing demand. In addition, it will be a long time before market institutions are mature. There is still much work to be done to demonstrate viable conservation-business ventures, with many existing REDD+ and similar programs established without planning for private finance.

Schemes for payments for ecosystem services are seldom well established.

Payments for ecosystem services (PES) and other performance-based schemes are not straightforward. They typically involve a variety of stakeholders and decision makers, operate at multiple levels (from global to local) and take time to establish. In some cases, PES is not the only or even the central driver of behavioral change, so a good understanding of the local social, cultural, political and economic context is crucial.

Private finance is not yet readily available for sustainable landscapes.

Although private finance exists in vast pools, some of which might be directed into sustainable land use, this is not necessarily the best way to frame the issue. Instead, the issue is really one of the political will to deploy a multilevel institutional and policy framework that minimizes risk to private financiers' return on investment. This is easier said than done. At present, opportunities for investment are few. Unlike, say, the renewable energy sector, the definitions and metrics involved in sustainable land-use projects are unclear or missing from the point of view of a financier. Definitions of "forest", "restoration" and "degraded land", for example, are still hazy. Hence, potential projects are often fraught with uncertainty that makes assessing investment risk very difficult. Often, the opportunity costs associated with forest protection and/or restoration are simply too high relative to business-as-usual.

The private sector and civil society do not yet speak the same language.

Great progress has been made in establishing multi-stakeholder forums, corporate–NGO partnerships, and dialogue for change, yet there are still substantial problems in communicating between the world of finance and the world of sustainable development. The word "equity", for example, means very different things to representatives of financial institutions and development agencies. Many environmental professionals do not speak the language of the corporate CEO, and many corporate boards do not understand environmental and development basics. Even economic evaluations of environmental issues, such as those for ecosystem services, do not necessarily make much impact on the behavior of boards and shareholders. The answer is not always more information, but better communication.

Environmental input and safeguards in trade agreements need not hamper trade.

With guaranteed better environmental and social safeguards, trade agreements would be more likely to receive broad support. Moreover, such safeguards can often serve as drivers of industrial innovation and efficiency.

Transforming supply chains in the land-use arena is not simple.

In contrast to the fossil fuels sector, the supply chains of the mainstream agriculture and forest industries are often very complex and messy, with high variability depending on the commodity, although this is offset somewhat by consolidation and vertical integration. Keeping track of supply chains is crucial for taking action for change and investment decisions. But investment disclosure is problematic and progress very hard to measure, making divestment strategies less straightforward than for the fossil fuels sector.

Ongoing globalization is not a given.

Globalization has been ongoing for hundreds of years and has certainly driven much environmental change and the reach of resource industries. However, the future of globalization is not a given and may, in fact, have peaked in 2007 with a 60 percent decline in cross-border capital flows since (Lund et al. 2013). Moreover, US$1.9 trillion of foreign investment in the global South in 2012 was from other emerging/developing economies (Lund et al. 2013). This may have profound, and as yet unexplored, implications for the environment and sustainable development.

What can participants learn about finance and trade at the 2015 Global Landscapes Forum?

Participants will gain a better understanding of the complexities of the world of finance and trade, and the links between finance and landscapes in developing countries. The sessions will look at every level of finance and the value chain, from the local to the global. Discussions will cover ways to reduce investment risks and, at the other end of the chain, how small enterprises can access funds. They will explore how finance can be coordinated at a landscape scale, what happens if the rules of the financial game are changed, and what difference policy interventions can really make. Participants will learn what happens to agriculture and the potential of REDD+ if wasteful subsidies are cut, how commodity prices affect deforestation, and how reputation risk influences company behavior. The role of insurance in sustainable landscapes will also be covered.

Photo by Bruno Locatelli/CIFOR

Who are the key audiences for the discussion?

Because trade and finance involve an array of decision makers, this theme is of relevance for several groups.

Policy makers (national and international) need to understand how state interventions can make trade and finance more or less sustainable, and the difference that particular instruments can make. They should understand that change is possible, but that relying on self-regulation and voluntarism will have little effect. In particular, ministries of planning, economics, trade, and finance should find the discussion useful.

Civil society has a strong say in corporate behavior and policymaking, and needs to understand the complexities of the trade and finance arena. It also needs to understand the issues that preoccupy corporate decision makers, in order to establish better dialogue and to become better watchdogs.

For *institutional investors and other private firms*, the discussion is important not only for specialist corporate sustainability professionals, but also for those assessing credit risk, procurement officers and, of course, CEOs.
All audiences should understand that, in spite of the compelling high-level case for change and presence of some pathways forward, translating goals into action at the country or corporate level is not easy.

Interested in **finance and trade?**

These sessions take a closer look...

Action on zero deforestation pledges: The challenge of aligning public and private sustainability goals. A case study of palm oil in Indonesia

Center for International Forestry Research (CIFOR), Tropical Forest Alliance 2020 (TFA 2020)

Saturday, 5 Dec: 12.15 - 13.45; Room: 252B

Industrial agriculture, ape conservation and climate change: More than a business case for reducing deforestation

United Nations Environment Programme (UNEP), UNEP Finance Initiative (UNEP-FI), Arcus Foundation

Saturday, 5 Dec: 17.15-18.45;
Room: Amphithéatre Bleu

Mobilizing finance for integrated landscape initiatives: Three scalable financial instruments

European Investment Bank, Credit Suisse, Althelia Ecosphere, eco.business Fund, Global Canopy Programme, The United Nations Convention to Combat Desertification (UNCCD)

Sunday, 6 Dec: 16.30-18.00; Room: 252B

Investing in integrated landscapes to achieve the SDGs

Landscapes for People, Food and Nature Initiative (LPFN), EcoAgriculture Partners, United Nations Environment Programme (UNEP), Food and Agriculture Organization of the United Nations (FAO), UNCCD Global Mechanism

Saturday, 5 Dec: 15.30-17.00; Room: 252A

Changing agricultural fiscal policies to stimulate sustainable economic growth, food production, and reduced deforestation

United Nations Environment Programme (UNEP)

Sunday, 6 Dec: 11.30-13.00; Room: 241

Engaging the private sector in long-term solutions to end Indonesia's forest fires and haze

Indonesia Palm Oil Pledge (IPOP), Golden Agri-Resources (GAR), Musim Mas, Wilmar, Asian Agri, Cargill, Indonesia Chamber of Commerce and Industry (KADIN)

Sunday, 6 Dec: 16.30-18.00; Room: 241

Shaping sustainable supply chains of the future: How to create links between smallholder farmers, companies sourcing raw materials, and the environment

Livelihoods Fund, Danone, Mars Inc.

Saturday, 5 Dec: 15.30-17.00; Room: 252B

Green Growth Compacts: How three states are pursuing a different industrial development

The Nature Conservancy (TNC), Governors' Climate & Forests Task Force (GCF)

Sunday, 6 Dec: 16.30-18.00; Room: 252A

Case study

The struggle for sustainable palm oil

Relatively inexpensive and easy to produce, palm oil is consumed by about 3 billion people in numerous products, such as cosmetics, chocolate, ice cream, toothpaste, potato chips and cooking oil.

In 2012, the combined value of palm oil produced by the world's largest producers – Indonesia and Malaysia – was around US$40 billion derived from about 13 million hectares, and growing. Estimates vary, but demand is expected to continue to rise at least until mid-century, most of it in India and China.

But economic benefits frequently come at environmental and health costs, with millions of hectares of primary tropical forest cleared and fragmented, large and growing volumes of carbon emissions, and serious health impacts from "megafires" associated in part with oil palm cultivation.

In response to mounting public concern, the Roundtable on Sustainable Palm Oil (RSPO) was established in 2004 to transform markets and mainstream more sustainable production. The RSPO now boasts over 40 percent industry coverage. Its members include companies, governments and non-governmental organizations, which have agreed to environmental and social benchmarks and approve third-party auditors. Around 2.7 million hectares of oil palm plantations are RSPO certified, including over 450,000 hectares of smallholdings.

Despite these achievements, the RSPO has been criticized for low standards and weak enforcement. In 2015, several companies – including PepsiCo, Kellogg, Mars, Starbucks, Wal-Mart and Colgate-Palmolive – proclaimed that RSPO certification does too little to protect high-carbon forests and peatlands, and must shore up transparency, auditing and enforcement. More recently, NGOs have questioned the credibility and impartiality of RSPO-approved auditors. And the industry still has trouble linking verifiable claims to measurable outcomes, with, as yet, no shared definition of "sustainable palm oil."

Even where companies commit to change, they encounter multiple dilemmas, including how to satisfy mainly Western demand for social and environmental responsibility while expanding in lucrative, less-demanding markets elsewhere, such as India and China.

Private sector initiatives may also come up against governments. In New York in 2015, several companies controlling 80 percent of global refining capacity signed the Indonesia Palm Oil Pledge (IPOP), including a commitment to zero deforestation. But the move has met with resistance from the Indonesian government, which is concerned about economic impacts, including on smallholders, and requires companies to use all of the land allocated to them for plantation development.

In 2014, the Banking Environment Initiative (BEI) was launched, with 10 international banks agreeing to finance only sustainable land use by 2020. Furthermore, Unilever has said it will make sure 100 percent of its agricultural raw materials are sourced sustainably by the same year. Both initiatives highlight palm oil.

Palm oil supply chains, however, are typically disjointed, complicated, opaque and notoriously difficult to trace; many buyers do not know the provenance of 100 percent of their supplies. In countries such as Indonesia, the political economy and governance institutions hamper enforcement of laws and corporate standards. Hence, while there are clear signs of progress, high-level company commitments can prove tricky to translate into guaranteed practices on the ground.

Where are the key knowledge gaps?

- What are the real opportunities and risks in the land-use sector? Where projects do exist, how can they be translated into financial terms, enabling investors to understand risks and opportunities?
- How can better cross-sectoral communication be achieved? Who are the actors and decision makers in land-use finance and how can they be motivated to change their behavior?
- What role can insurance play in promoting sustainable landscapes?
- How can governments effectively create long, clear price and demand signals for carbon? And how can the finance sector best contribute and be prepared?
- How do we keep track of long, complex, messy supply chains in agriculture and forestry? How can global supply chains be transformed so they are sympathetic to achieving the Sustainable Development Goals?
- How can funds best be coordinated once they reach landscapes? How can we make land-based investments match integrated landscape management and transparency goals? What do local stakeholders do with the finance once they get it?
- Are companies that maintain unsustainable practices really at material risk? What kinds of economic valuations of environmental issues will have the most impact on decision makers in finance and government?
- How can climate change mitigation and adaptation be meshed into trade decisions – meaningfully and enforceably? What are the implications for achieving the Sustainable Development Goals under various globalization and regionalization scenarios?
- How do we establish a body of research on investment in sustainable landscapes that is transferable and applicable broadly?

Literature

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About this Background Brief

This Background Brief was produced by the organizers of the 2015 Global Landscapes Forum based on input from session hosts and members of the Science Committee. It is not intended to provide an exhaustive analysis of the theme, but to establish key issues, as perceived by those who provided input. Any opinions expressed do not necessarily reflect the views of the organizers of the 2015 Global Landscapes Forum or partner organizations.

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