MCS / Theo Vickers

Building a blue finance ecosystem

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Building a blue finance ecosystem

There is a growing interest in investing in the blue economy, underscored with many large financial institutions now turning their attentions to the blue economy (see Citi, Deutsche Bank, Standard Chartered, BNP Paribas). Currently, however, they are very few funds in the blue economy and not enough projects of sufficient size to attract the investment needed to improve ocean health. At our blue finance event with Simmons & Simmons in June 2023, we brought together experts from across the private sector to talk about how we can turn this appetite into substantial investment that holds sustainability at its core.

Speaking the right language

An important first step outlined by our panellists is to start speaking a language that financial institutions and investors understand. Instead of "people, planet or purpose" the financial world deals in risk, regulation, return, and investment infrastructure. There is also a need to talk about systemic risk. The triple threats of climate change, biodiversity loss and pollution are all threats to the global economy and it should be within the interests of institutions to integrate natural ecosystems into their risk models. This means understanding how financial value depends on the environment and the need to protect that value by safeguarding ecosystems. By framing nature and climate change as a systemic risk, it brings investors into the conversation that are not only philanthropic or impact focused.

Define roles

Once we have adopted the same language, everyone can begin to understand the role they have to play within the ecosystem. For example, asset managers need to choose and value blue projects, while consultants can advise on allocating capital to nature-based solutions. Regulators have a role to play in making sure we can monetise the benefits that these projects can deliver. Governments will need to be involved in accelerating the blue economy by setting the operating, regulatory and policy environments that can remove barriers to investors. Despite the best of intentions and appetite to invest, companies and investors alone cannot create the regulatory and policy frameworks to enable large-scale investments. Once everyone knows their role and the ecosystem is developed, money could start to flow into the blue economy at much greater scale.

Redistribute risk

The ecosystem should bring together institutions to manage and redistribute risk – so that investors are not left to take on all of the risk themselves. International Finance Institutions and public-private partnerships can help in creating a mix of blended and commercial investments. Developing mechanisms that front-load financing (as demonstrated by the World Bank's Rhino Bond) can help to get projects off the ground.

> International Finance Institutions provide finance to enhance development globally, regionally or in specific developing countries. These can be set up by multiple nations (multilateral) or between two nations (bilateral), and they can provide large-scale financing on competitive terms to support development. Well-known examples include the World Bank, International Monetary Fund, the European Investment Bank and the Asian Development Bank.

This could also help to create investment grade opportunities where there is sufficient liquidity and enough counterparties to deal with. There will always be a level of risk - any nature restoration project is susceptible to unexpected loss - but there are some risks that can be insured against so that the investment remains focused on the gains to be found, such as within in carbon and biodiversity markets. This does not necessarily require the creation of new insurance products, but rather incorporating business interruption insurance into blue projects. This may be enough to tip the balance for the more risk averse investors, and once we begin to see more success stories, we could start to see a blue rush of investment.

Scale of investments

Another issue the ecosystem can address is that of scale and having funding available for a range of different projects and investment sizes. Large scale investors and sovereigns typically look at large scale investments. For example, fixed income funds are in the order of millions and billions of pounds and will look at projects that are worth hundreds of millions of pounds (referred to as benchmark sized). However, considering the scale of investment needed to transform the blue economy, the fixed income asset class can play a big role.

> Fixed income refers to assets that pay out a fixed amount, in the form of interest or dividends for a period of time. These can be bonds or debt instruments – the most common types of fixed income products are government or corporate bonds. Equities are shares of ownership in an asset, where the value of the shares (or stock) is linked to the performance – investors benefit where the share value rises and may also receive dividend payments.

There have already been exciting developments within fixed income, such as the emergence of the labelled bond market (green, blue, sustainable bonds, sustainability-linked bonds) where the funding generated is ringfenced for particular activities or outcomes. This provides visibility of where the funding is going and allows investors to signal where they want companies to do more.

At the other end of the spectrum, small-scale projects may require the use of grant or philanthropic funding unless they can be pooled into larger investments. There remains a gap in funding for small-medium enterprises (projects worth $5 – 10 million) that fall between these two extremes and will require impact investors to be brought in for funding.

Investing in ocean health

Finally, the development of the blue finance ecosystem, and the common language used, should not lose sight of the primary need to protect our ocean. The ocean regulates the entire system of the planet and provides fundamental life-support for all life on earth. It remains our best tool for mitigating climate change, and it regulates the climate more effectively than any other technology. This makes it the leading cause to invest in when it comes to tackling the greatest threats faced by society and nature. Whatever the cost of protecting our ocean, it will be a bargain compared to the cost of allowing them to fail. It just so happens that it can also be financially beneficial.