

BLOG POST

FINANCING THE BIOECONOMY IN THE AMAZON

HPL

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December 3rd, 2023

The Amazon is home to the greatest source of biodiversity in the world, responsible for sheltering 10% of all plant and animal species on the planet. The Amazon biome, which occupies 6.7 million km² and is distributed throughout nine different countries (with Brazil home to the largest portion), is responsible for capturing carbon dioxide (CO₂) emissions and maintaining regular rainfalls throughout South America. These ecosystem services play an important role in both the global and regional economies, such as the agribusiness sector in countries such as Brazil, Bolivia, and Paraguay[1].

Rapid deforestation has heavily impacted the Amazon, with deforestation rates reaching 83 million hectares just in Brazil. Professor Carlos Nobre, a renowned climate specialists with a lifelong study of the Amazon forest, says the region is at risk of reaching a tipping point[2], meaning that the forest would lose its biodiversity and become a savannah, provoking new CO₂ emissions and altering rainfall pattern in the South American continent, consequently affecting agriculture, energy, and water sectors[3].

Stimulating the bioeconomy is one way to conserve the rainforest and promote rural livelihoods in the Amazon. Bioeconomy is a developing concept with multiple debated definitions. Initially, organizations like the OECD and EU defined it to describe the shift from fossil fuel-based economies to models relying on agricultural biological inputs, without a specific focus on biodiversity. Recently, the concept has been redefined as a productive and reproductive paradigm, meaning that bioeconomies should be evaluated by their production process rather than by the product itself, with a focus on respecting parameters of society and biodiversity. The bioeconomy in tropical forests, such as the Amazon, must integrate both the economic system and socio-ecological landscape, while at the same time preserving the biome.[4]

Stimulating the bioeconomy will help unlock natural capital services while conserving the forest and promoting sustainable livelihoods for those living in these locations.[5] This is especially relevant in the Brazilian Amazon, a five million km² region with 28 million inhabitants, which has numerous economic and social challenges but with the potential to seek sustainable economic development while keeping the forest standing.[6]

HOW CAN SUSTAINABLE FINANCE MAKE A DIFFERENCE?

There is a growing interest in preserving and promoting the Amazon: a good example is the recent Amazon Summit, which united the eight Amazonian countries and other multilateral organizations (IDB, NDB and CELAC[7,8] participated) to discuss challenges and opportunities faced by the region. In addition, the UN decided to host the UNFCCC COP30 in Belém, Brazil. Another example is the "Amazonia Forever" program announced by IDB this year, which looks to increase financing and strengthen planning and execution of projects to improve coordination and collaboration within the Amazon.[9] Furthermore, BNDES, the largest development bank in Brazil, has been active with its Amazon Fund[10], which receives international donations from several countries.

Investing for financial returns and a positive impact is not only beneficial for the environment but also for the communities that live in the Amazon. Various financial instruments could be applied to promote investment in the bioeconomy in the Amazon.

Sustainability Linked Bonds (SLB) and Sustainability-Linked Loans (SLL): SLBs and SLLs are fixed-income instruments that offer financial or structural incentives to issuers who meet certain sustainability objectives. These instruments require issuers to commit to specific targets within a set timeframe, influencing the economic terms of the bond. The objectives are measured through pre-defined Key Performance Indicators (KPIs) and assessed against predefined Sustainability Performance Targets (SPTs).[11] SLBs and SLLs could be applied by governments, financial institutions, or other actors to promote conservation in the Amazon.

Uruguay, for example, issued its inaugural SLB in October 2022 in the amount of USD 1.5 bn, which was successfully retapped in November 2023 for USD700 M, with two KPIs: reduction of greenhouse gas emissions and the preservation of native forests.[12] The transaction is innovative because it includes a two-way pricing structure, featuring a step-down coupon for outperformance and a step-up for underperformance. In the case of the conservation KPI, the step down would be activated if Uruguay increases native forest area (over 103% coverage), while the step up would be activated if Uruguay does not maintain 100% native forest coverage. This instrument could be replicated in Brazil, for example, by national or local governments to promote the conservation of the Amazon.

Green, Social and Sustainability (GSS) Bonds or Loans: GSS bonds and loans are fixed income instruments that apply use of proceeds raised to finance or refinance green and/or social projects, assets or business activities.

These instruments can be applied to direct financial flows towards projects related to promoting the bioeconomy, local communities in the Amazon, conservation, amongst others.

The Brazilian Government issued its first Sovereign Sustainability Bond in November 2023, in the amount of USD 2 billion, with the proceeds being utilized for actions that promote sustainability and contribute to the mitigation of climate change, the conservation of natural resources and social development.[13] The Federal Government has included various eligible projects/use of proceeds to help further promote the protection, conservation, recovery, restoration, and sustainable management of the biodiversity of terrestrial and marine ecosystems.[14]

Green CRAs: are fixed-income, low cost and agile securities supported by the expected payments from transactions between rural producers or their cooperatives and third parties. To receive payment, rural producers need to follow certain criteria such as low-carbon agriculture, the recuperation of degraded soils, forest regeneration and crop livestock-forest integration. [15] Today Green CRAs can be issued in international markets, which could potentially increase the investments needed in the Amazon region, but they are still very incipient, with the first green CRA being issued in 2022 (US\$11 million) towards the harvesting of soy in regions without deforestation.[16]

Blended Finance Instruments: Private markets could also enter the Amazon region using blended finance instruments. Common structures consist of public or philanthropic (e.g. governments, international organizations) investors that provide funds on below-market terms within the capital structure to lower the overall cost of capital or to provide an additional layer of protection to private investors. Other examples include providing credit enhancement through guarantees or insurance on below-market terms.[17] However, there are still challenges facing this path, such as fiscal restrictions on local/state governments and limited capital markets operational capacity regarding socio environmental impact in Brazil, especially in the Amazon region.[18] Regional and Multilateral Development Banks are avid propagators of these instruments. Within the region, the IDB is promoting blended finance instruments through its "Amazonia Forever" program.[19]

Investing in ways to achieve zero deforestation, growth of the bioeconomy sector, and land restoration are important steps that could help avoid the Amazon from reaching its tipping point. It is of the utmost importance that we do this in order to secure a more sustainable future for us and the planet.

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