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Can Debt-for-Nature Swaps narrow the global biodiversity finance gap?

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Debt distress is one of the [key obstacles](#) for developing countries to protect their biodiversity. Even though there have been debt restructuring initiatives for least developed countries, it has proven largely [insufficient](#). To simultaneously address the debt and biodiversity crises, Debt-for-Nature Swaps (DNS), perceived as an innovative instrument to exchange sovereign debt for biodiversity commitments, have recently sparked the interest of [private and public actors alike](#). However, acknowledging the fact that DNS have not targeted low income countries so far and have not proven to be a panacea for solving the [debt crisis](#), what is their potential to finance biodiversity in developing countries? Based on the review of the literature and of various proposals for upscaling DNS, IDDRI here outlines key challenges and opportunities for this instrument to support transformative change for biodiversity.

Fostering credibility & transparency via political will

Emerging during the Latin American Debt Crisis of the 1980s, DNS made a comeback in 2016 when Seychelles swapped part of its [Paris Club](#) debt and issued the world's first blue bond¹ with The Nature Conservancy (TNC), an environmental NGO. Since then, TNC has facilitated four other DNS, all in upper-middle or high income countries, amounting to \$2.8 billion of debts restructured,² so that only five countries have used this tool. DNS have therefore had a very limited impact in liberating fiscal space for biodiversity at a global scale. The explanations often put forward are that DNS are complex, time-consuming mechanisms and therefore difficult to scale up.

What is often absent from the debate is the role of political will from official creditors in scaling up DNS. After Seychelles took years to negotiate with Paris Club creditors a debt restructuring that cancelled only \$1.4 million, [TNC saw an opportunity to focus on privately-held debt](#) to achieve more momentum with the DNS that followed. By buying back their commercial debt that was trading at a discounted price in capital markets, Belize, Barbados, Ecuador, and Gabon were able to achieve their DNS without going through the long process of negotiating a debt restructuring agreement with official bilateral creditors. Moreover, [private loans are more burdensome](#) than those issued by public creditors, further supporting the argument for targeting commercial debt. However, the heavy private sector involvement in these DNS has also increased transaction costs and raised concerns about [lack of transparency](#). To avoid speculation in government bonds during the DNS, these transactions have been carried out privately, without involving [civil society](#). Furthermore, the conservation funding agreements of DNS have not been disclosed, and thus fail to comply with the [IFF's Voluntary Principles for Debt Transparency](#). The heavy involvement of corporate intermediaries in DNS has also come with high transaction costs. Just in legal and financial advisory alone, Barbados DNS involved [eight](#) corporations headquartered in rich economies. For Belize, the cost of intermediaries was [\\$2 million more](#) than the amount of money raised for conservation after the swap.

Ultimately, targeting commercial debt has been relevant because the countries that have participated in DNS are all high or upper-middle income countries. To address the biodiversity finance gap in indebted low-income countries, DNS should be scaled up to include countries eligible to the Common Framework (CF countries hereafter)³. Given that most of these countries do not have access to capital markets, most of their external debt is held by public creditors. Therefore, a political dialogue including the main official creditors is necessary for future DNS to respond to the needs of CF countries. Together, the Paris Club, China and multilateral development banks [hold most of the debt](#) of these countries, and thus reaching political consensus at the international level on how to decrease these countries' debt burden whilst increasing their investments in biodiversity could have a transformative impact.

Beyond conservation, addressing the drivers of biodiversity loss

So far, DNS have focused on conservation targets. This has been done by linking the conditions of the new blue loan, issued to buy back the debt, to the country's commitments to establishing and managing new protected areas. While underlining the lack of transparency around the agreements, [Standing \(2023\)](#) stressed that DNS can include provisions for biodiversity-aligned development, however failure to deliver them would not result in a downgrading of loan conditions. All the countries that have done a DNS with TNC have a strong track record of biodiversity conservation and a preexisting relationship with TNC, which is essential to ensure the credibility of biodiversity commitments in countries with often weak governance structures ([Nedopil, Yue and Hughes, 2023](#)). However, by focusing on the conservation of unprotected but still largely intact ecosystems, the question of additionality comes into play. Despite research showing the [cost-effectiveness of prioritising conservation](#) of well-functioning ecosystems over restoration of degraded biodiversity ([Cook-Patton et al., 2021](#)), the scandal around [Verra overestimating the](#)

[additionality of their offsets](#) sheds light on the complexity of assessing how threatened an ecosystem really is.

For DNS to be truly transformative, they must go beyond protected areas and target the root causes of biodiversity loss. For example, the African Development Bank (AfDB) has [explored](#) the possibility of swapping some of the debt that the Democratic Republic of Congo owes AfDB to finance the development of a sustainable alternative to charcoal as a cooking fuel. This would target one of the [leading causes of deforestation](#) in the country whilst also building up a new industry that would create jobs and contribute to a biodiversity-aligned development for the country. Thus, DNS could have the potential to finance sectoral transformations contributing to countries' National Biodiversity Strategies and Action Plans (NBSAPs) and, at the same time, sustainable development targets. Following in the footsteps of AfDB, creditors and public development banks that are called to increase the environmental activities in their portfolios could use DNS for that purpose. Here, [China holds great potential](#) for “greening” its development projects through DNS addressing conservation⁴ and sectoral transformations simultaneously. The [Belt and Road Initiative](#), the large-scale overseas initiative, owns a 1 trillion-dollar debt, and is at risk of stranded assets, and has financed infrastructural and industry projects that have shown [high risks for biodiversity, but also indigenous peoples](#).

The group of climate-vulnerable countries, [V20](#), and the [Debt Relief for Green and Inclusive Recovery](#) (DRGR) Project have both emphasised the importance of moving away from DNS as individual transactions and towards a [streamlined approach](#) to scale up DNS at a global level. They identify the Common Framework as the best place to develop this reform, given that it includes the Paris Club, key bilateral creditors and members of the G20 such as China. Nonetheless, both propose a way of linking debt restructuring to climate commitments and fail to propose how biodiversity could be included in this new global framework. Given that they identify country ownership as a cornerstone of their proposal, countries should be able to choose to link debt restructuring to their NBSAPs to mainstream biodiversity into their development pathways. Ensuring that DNS are part of the emerging discussions on debt restructuring and are not left behind in the name of more transformational debt-for-climate swaps is crucial to align climate and biodiversity strategies and ultimately achieve the Global Biodiversity Framework targets.

Targeting the right countries

Another key element that will need to be considered when developing a global framework for debt swaps is which group of developing countries should be targeted, as this will impact the group of creditors that are most relevant. If the wider group of emerging markets and developing economies are targeted, as seen in the V20 and DRGR proposals, then private bondholders become the biggest creditors and the new framework will have to ensure their widespread participation, notably through a dedicated guarantee facility under the World Bank and/or other multilateral development banks (MDBs). This would be essential to de-risk future swaps, as past DNS have included a high cost for debtor countries in guarantees such as [political risk insurance](#). On the other hand, research that explores the potential of DNS for CF countries highlights the potential for swapping publicly held debt for biodiversity commitments, as private bondholders hold a small percentage of debt owed by CF countries. These countries hold more than 22% of the world's biodiversity, whilst only 17% of this nature is protected ([Nedopil, Yue and Hughes, 2023](#)). Ultimately, the new framework could give special attention to low-income countries that will not be able to benefit from private debt restructuring, not just ensuring a coordinated response amongst creditor countries but also [MDBs](#) holding debt of low-income countries without access to capital markets.

A global framework for linking debt restructuring to both climate and biodiversity commitments would directly address the transparency issues seen with market-based DSN. States should allow for prior consultation and open access to key documents, most notably the biodiversity/climate commitments made by the debtor country and the conditions of the new bond in the cases when one is issued. Avoiding the corporate intermediaries of the third-party transactions

seen in recent years would also **lower transaction costs**. To ensure this, the V20 calls for an ‘independent and impartial mediator’ in the cases swaps are facilitated by a third party preferably governed by a multi-state structure, such as the United Nations Multi-Partner Trust Fund, the Green Climate Fund, or the Global Environmental Facility.

1 A blue bond is a financial instrument which aims to raise capital for marine conservation projects.

2 Belize: a \$553 million debt restructured,\$364 million in blue bonds (2021); Barbados: a \$150 million deal (2022); Ecuador: conversion of a \$1.6 billion debt into \$12 million per year for the conservation of the Galapagos Islands (2023); Seychelles: a \$21.6 million deal (2016); Gabon: a \$500 million deal (2023)

3 The Common Framework for Debt Treatments beyond the DSSI is a G20 and Paris Club countries agreement to coordinate and cooperate on debt treatments for up to 73 low-income countries that are eligible for the Debt Service Suspension Initiative (DSSI):

<https://www.imf.org/en/About/FAQ/sovereign-debt#Section%205>

4 For instance, a 2022 research paper has drawn several options for a DNS between Ecuador and China:

<https://portalreerca.uab.cat/en/publications/propuesta-para-un-canje-de-deuda-por-naturaleza-con-china-2>

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