Finance Tools for Coral Reef Conservation: A Training Guide

Debt for Nature Swaps

Developed by the Conservation Finance Alliance and Wildlife Conservation Society for the International Coral Reef Initiative

Content drawn from Finance Tools for Coral Reef Conservation: A Guide (2018)

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Photo: Yen-YiLee, Coral Reef Image Bank

Debt for Nature Swaps - Overview

- Definition: a transaction where a country (the debtor or borrower) has its debt purchased, renegotiated or forgiven by its creditors (fully or partially) with specific conditions, for example, that savings on debt service are invested in conservation activities – commonly through a Conservation Trust Fund.
- Value: Opportunity for countries struggling to pay their debt to receive debt relief and direct the financial savings towards supporting national conservation and other national environmental initiatives.
- Economic Model: distressed debt conversion produces local financial cash flows, risk management through debt reduction
- Other Name: Debt Conversion

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Debt for Nature Swaps - Background

- First used for conservation in the late 1980's and through the1990's
- United States provided for countries in Latin America and Southeast Asia
- "Debt for adaptation" swap is a new form of debt for nature swap intended for climate adaptation (which includes conservation)
- In some cases, a third party (e.g. an environmental NGO) may purchase the debt from the creditor, with a discount awarded to that party by the creditor, or to the debtor by the third party.
- Large program by TNC's NatureVest under the name Debt Conversion

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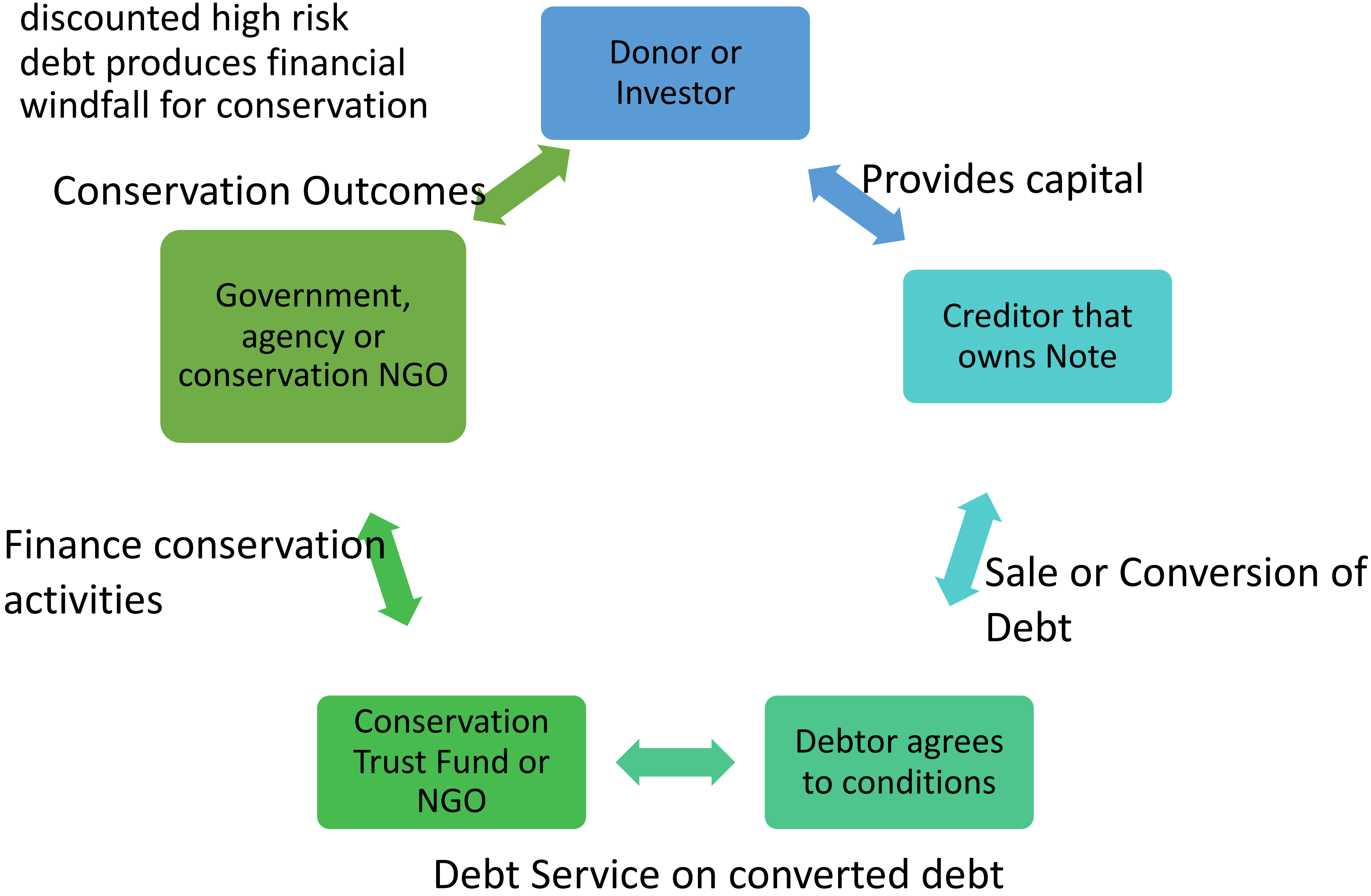
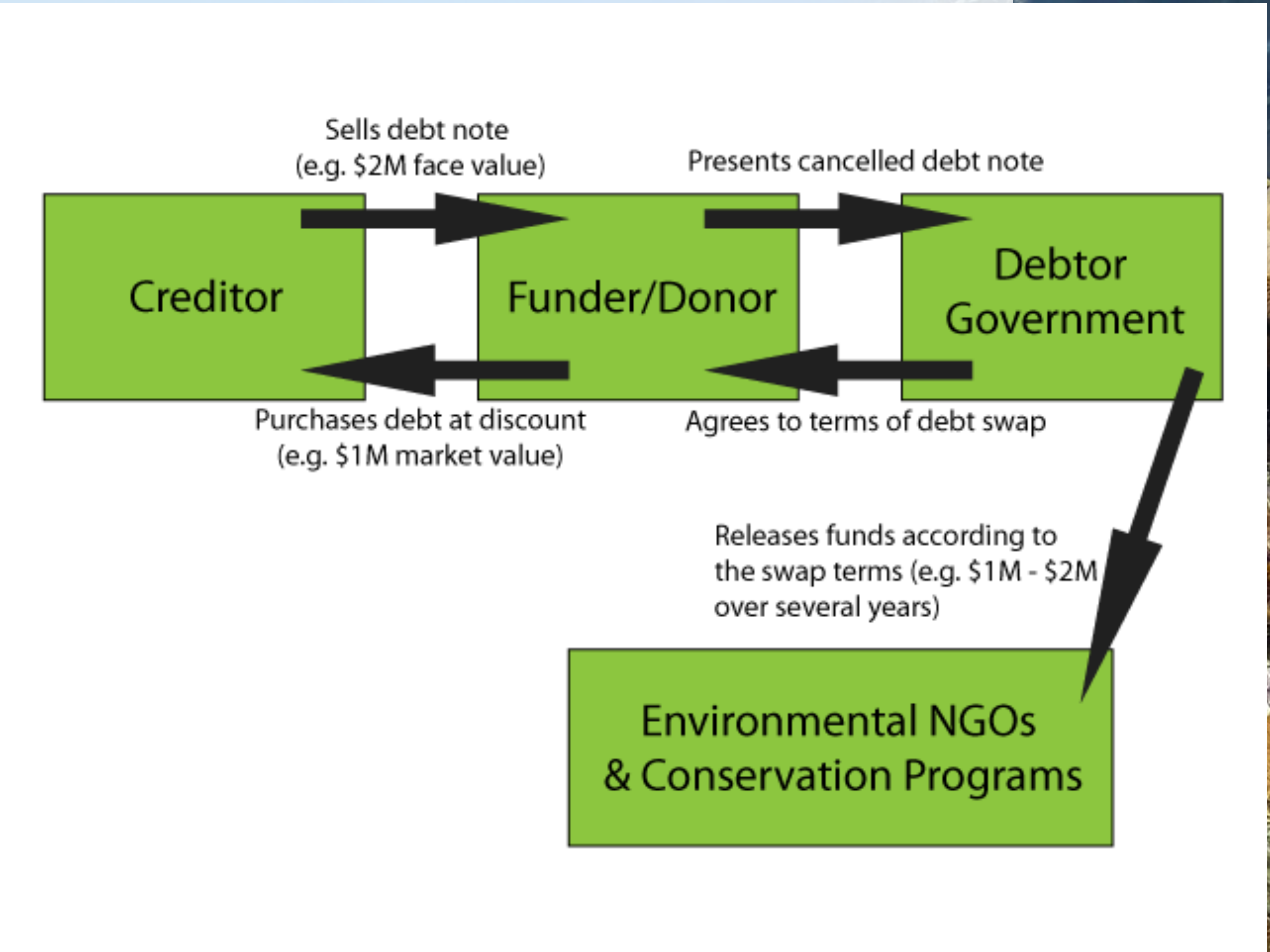
Debt for Nature Swaps

Economic Model:
discounted high risk
debt produces financial
windfall for conservation



Debt for Nature Swaps – How it works



Debt for Nature Swaps – Pros and Cons

Pros

- Can provide large amounts of funds, enough to support national Conservation Trust Funds.
- Strong incentives for developing countries to participate via opportunity to support environmental goals, reduce spending on debt obligations, and increase credit scores.

Cons

- Recently have resulted in only small amounts of debt relief
- Complexity leads to long negotiations and high transaction costs
- Only work in situations where government has distressed debt, a robust conservation policy and is on-board with the process.

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Debt for Nature Swaps - Conservation Activity Relevance

- Funds from Debt for Nature Swaps can support creation, development, and management of MPAs
- Can be used to invest in sustainable fishery infrastructure
- Can fund coral reef restoration and conservation
- Funds can also be used to suppress external pressure factors

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Debt for Nature Swaps - Stakeholders

- Creditor(s) – the country or private organization that loaned the money to the developing country in question
- Donor(s) - The organization funding loan reduction or forgiveness. Could be the creditor or 3rd party.
- Debtor - The (usually developing) country looking to have debt obligations reduced
- Facilitator/intermediary – often an NGO
- Conservation Trust Funds and foundations - Usually a local environmental fund is selected or created to manage and administer proceeds of the debt swap
- Implementing entity/beneficiary – the party receiving the funds from the CTF to support conservation activities, e.g. local conservation organization

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Debt for Nature Swaps – Feasibility Assessment

- Does the country comply with eligibility requirements from the country to which it owes its debt? (e.g. <u>TFCA</u> for USAID)
- Financial, political, economic, and environmental requirements
- Does the government have a robust conservation policy, and have a favorable view of debt for nature swaps and the process of orchestrating them?

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Debt for Nature Swaps – Revenue Potential

- Debt swaps have the potential to produce large quantities of funds, sometimes sufficient to reach conservation goals on a nationwide scale and to support efforts for multiple decades
- The high transaction costs encourage large transaction size

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Debt for Nature Swaps – Case Studies

2018 Seychelles Debt for Nature Swap

- Seychelles (debtor) had $22M in debt held by the Paris Club (creditor)
- The Nature Conservancy (3rd party NGO) loaned the Seychelles $15M (plus $5M grant) to purchase the debt from the Paris Club at a discount
- Funds were held in a newly formed independent trust (SEYCCAT) that performed 3 functions
    - Pay back loan provided by The Nature Conservancy
    - Provide annual funds for conservation activities for 20 years
    - Capitalize an endowment to maintain support after the first 20 years

Debt for Nature Swaps – Case Studies

2018 Seychelles Debt for Nature Swap (continued)

- Among funded activities was expansion of Marine Protected Areas in the Seychelles from 1% -> 30% of the country's EEZ
- Funding for management of the MPA (and other conservation activities) ensured for 20+ years

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