Briefing

How to increase private investment in nature

November 2024

Summary

Although nature underpins the successful functioning of businesses and our economy, this vital source of wealth is declining at ever increasing rates. The UK is one of the most nature depleted countries in the world.[1] Protecting and restoring the UK's natural wealth is estimated to require at least £44 billion of investment over the next ten years.[2] We will need both public and private finance to meet this goal.

Private finance flows into UK nature restoration are currently only contributing a tiny proportion of what is needed, with just £95 million per year invested, mainly by the water sector.[3]

UK nature finance policy, so far, has focused on creating nature market architecture, including setting standards and a promised consultation on market governance.[4] This is welcome and provides important foundations for new markets, but policy in this area has ignored the elephant in the room, that there are still not enough businesses willing to invest in the nature they rely on.

Without policy to drive demand, there is a risk that these markets will fail, investors will lose interest and farmers and land managers will be left without an important source of funding to enable their projects to succeed.

Some businesses already invest in nature through voluntary markets, such as the one that exists for carbon, but this is not happening at a level sufficient to drive nature restoration at the scale required across the country. Markets need more than voluntary commitments to drive greater private finance into nature restoration.

This briefing sets out options the UK government should explore to drive more private finance into nature, including creating new compliance markets like biodiversity net gain (BNG), charging a levy on businesses and pooling the funds to invest in nature, and changing incentives for companies, including expanding fiduciary duties to include nature.

We are calling on the government to set out a roadmap for how it will develop nature markets and scale up private finance for nature restoration,

focusing on driving demand. This roadmap should contain three key elements:

1. **Economy-wide actions that support all businesses to invest in nature,** such as a timeline for making the recommendations of the Taskforce for Nature related Financial Disclosures (TNFD) mandatory.
2. **Sector specific plans for creating new nature markets** through regulation, focusing on the water and food sectors initially.
3. **Immediate action on unresolved questions to bolster investor confidence**, such as the consultation on governance of carbon and nature markets.

Without a plan for development, there is a risk nature markets will not materialise at scale. Underinvestment from the private sector will either leave public funding to fill the gap or nature will continue to decline in breach of UK targets to restore it.

Introduction

Nature underpins our economy.[5] Almost every material used in our daily lives has been either mined or grown from the earth. Nature provides food, fuel and materials to build homes and products, as well as cleaning the air we breathe and the water we drink. There is strong evidence that our mental health depends on thriving nature, and even that exposure to nature changes how our brains develop as children.[6] But biodiversity is declining at the fastest rate in human history, with extinction rates 100 to 1,000 times higher than the baseline, and still increasing.[7] Recent research from the Green Finance Institute has shown that nature loss could lead to a 12 per cent loss to UK GDP by the 2030s, which is larger than the impact of the Covid-19 pandemic.[8]

Nature is therefore key to the economy, but there is a lack of investment in its protection and restoration. The Dasgupta Review, commissioned by the UK Treasury, outlines how the creation of productive economic capital has been at the expense of natural capital.

Between 1992 and 2014, productive capital per person globally doubled, while natural capital per person declined by 40 per cent.[9]

Research suggests the UK needs to invest at least £44 billion to restore and protect its natural wealth over the next ten years.[10] This will need to be delivered through a combination of public and private finance.

The private sector should be motivated to invest in nature to reduce its risks and costs and improve the long term viability of its operations. For example, increasing soil quality will improve long term crop production, maintaining farm income and goods supplied to supermarkets. Other benefits from nature that reduce business risks include reduced flood risk, reduced drought risk and higher water quality.[11] Companies which rely heavily on the natural world, such as the food sector, also benefit from habitat creation and protection beyond the farms they source from, to provide pollinators, richer fungal diversity in the soils and protection from extreme weather events. As the value of those natural assets is not incorporated into their economic decision making, private companies are able to use these resources for free. This is essentially a gift of public wealth to enrich private interests.

This is not necessarily a problem if the private sector puts the money it gains from this enrichment back into nature. However, the private sector is failing to invest to maintain the nature it uses. There are some mechanisms to facilitate private investment in nature in the UK, but they are too small and piecemeal to deliver the scale of nature restoration needed.

Private investment in nature is estimated to be just £95 million a year, mostly driven by regulation of the water sector, with an expected boost of £200 million a year from new regulation in construction.[12] The polluter pays principle, enshrined in UK law, tells us that businesses should pay for the damage they do to nature, even if it does not directly impact their current bottom line.[13] The private sector should not be able to destroy the nation's natural wealth, and then pass the costs onto the public sector to restore it.

There is a need for new policy mechanisms to drive business investment in nature at greater scale in the UK. In our previous briefing, we set out the policies needed to boost supply in nature markets.[14] But markets depend on both supply and demand: buyers and sellers. Here, we set out why demand is a major barrier to the growth of nature markets in the UK, the potential mechanisms for driving greater private finance into nature, the pros and cons of different approaches and what action the UK government needs to take.

Current state of play: nature markets policy

The previous government's policy in this area focused on creating nature market architecture, including developing standards for markets and promising to consult on governance models for the voluntary carbon and nature markets.[15] This is important, as it helps to build business confidence, but it has been insufficient for market development. The market will fail without policy that also drives demand and attracts buyers.

This is a major issue for nature markets, as too few businesses are investing. Only the water and construction sectors are currently required by regulation to invest in nature restoration through water sector regulation and biodiversity net gain (BNG). All other sectors only invest on a voluntary basis, largely through voluntary markets for carbon that include woodland creation and peatland restoration. Farmers and land managers are creating projects and preparing for private investment through government schemes like the Natural Environment Investment Readiness Fund, but too few businesses are interested in buying them.[16,17]

Investors have told us they would be willing to provide finance, like loans, to nature projects if financial returns could be guaranteed. However, without companies interested in buying nature credits there is nothing for them to provide finance for and therefore no returns are on offer.

The international context

This briefing focuses on how private finance can support nature restoration in the UK, while seeking to guard against increasing impacts on nature overseas. In some policy areas, it is important to align the approach the UK takes internationally, to help restore and protect nature globally, and to ensure international businesses do not face conflicting regulations. For example, aligning standards that define what 'good' nature credits look like with internationally agreed definitions from the International Sustainability Standards Board (ISSB).

However, the UK can take a lead on developing governance models and on creating new markets. The UK has already done this through biodiversity net gain (BNG) in the construction sector. This avoids questions of overseas impacts by focusing on the land affected by construction, rather than the full supply chains impacts of companies. It is critical that when creating new markets to protect nature in the UK, we do not offshore impacts overseas, for example by increasing imports that have an impact on nature in other countries.

Mechanisms for getting private money flowing into nature

When designing policy for nature restoration it is vital to take the 'mitigation hierarchy' into account. The priority should always be to avoid harm to nature, and only if this is not possible should policy look instead to minimise damage and compensate for losses.[18]

We have identified five mechanisms for driving private finance into nature: supporting the development of more effective voluntary markets, creating new compliance markets where companies are required to buy credits, charging a levy on businesses to account for their impact on nature and investing the returns in nature, charging fees for the provision of natural infrastructure and changing company incentives.

The first three change the external incentives for companies, and mostly focus on the lower end of the mitigation hierarchy, ie compensating for damage done. The last option focuses on changing the internal incentives for company action. This targets attention at the top of the mitigation hierarchy, avoiding impacts in the first place. These are not either/or choices, mechanisms could be combined to create the most impact. These approaches are explored in our accompanying discussion paper, which outlines the pros and cons in more detail, summarised overleaf.

Mechanism	How it works	What policy is needed
Develop voluntary markets for nature	Businesses invest in nature restoration out of choice, either to enhance their reputation with customers or because they recognise the material risks to their business of not doing so. Businesses do this by buying nature 'credits', sold by farmers or land managers who make improvements to the nature and biodiversity on their land.	– Make Taskforce for Nature related Financial Disclosures (TNFD) reporting mandatory. – Create strong standards and governance. – Define what 'good' nature positive action looks like for businesses.
Create compliance markets	Government policy requires businesses in certain sectors to invest in nature restoration. A market is then created enabling businesses to purchase nature 'credits' to meet their regulatory obligations.	– Existing compliance markets in construction could be expanded to cover wider environmental gain or other ecosystems, eg marine net gain. – New markets could be created for new sectors, eg the food industry, by introducing new regulation.
Charge a levy	Businesses are charged a levy based on their impact on nature. This funding is then spent on nature restoration in the UK, such as Landscape Recovery projects. The levy could be collected and spent by central government or devolved to regional business-run funds which direct the money to local projects.	– Introduction of a levy. – Design management of the fund created by the levy, who runs it, and how the money is spent.
Change company incentives	Expand the legal responsibilities of company directors (fiduciary duties) to include the protection of nature. This would require businesses to consider nature as a stakeholder impacted by	– Reform to the Companies Act (2006) to expand the definition of fiduciary duties – Reforms to ensure measures are accurately

	company activities, as an incentive to invest in its protection.	reported to boards and shareholders and justified to regulators.
Fund natural infrastructure through a Regulated Asset Base (RAB) model	Landowners charge businesses who benefit from the way they manage their land a fee to cover maintenance and upkeep. For example, insurance companies benefit from lower flood risk to the properties they insure. This could be organised as a RAB model, with an economic regulator setting the fee to be paid.[19]	– Legislation to create the framework for the RAB model – Assigning an economic regulator to set fees, and the possible creation of regional natural capital utilities companies to manage the natural infrastructure services created.

Voluntary markets are not sufficient

There are two type of nature market: voluntary and compliance markets. In voluntary markets, businesses can choose whether to engage or not. In compliance markets, regulation requires businesses to engage and purchase nature credits to meet certain requirements.

Voluntary markets, created through societal pressure and supported by frameworks like the Taskforce for Nature related Financial Disclosures (TNFD) are growing, but they will not drive enough demand on their own to restore and protect UK nature.[20]

In addition, there is a risk that they will generate very low prices for nature credits. This is the current problem with the voluntary carbon market, where prices are too low for a strong investment case. This is partly due to fluctuations in supply and demand of carbon credits and poor quality of the credits leading to accusations of greenwashing. Strong standards and governance are needed.

There are proposals to raise the price of nature-based carbon credits by allowing them into the Emissions Trading Scheme, a compliance market for carbon which, analysis suggests, could raise the price of woodland carbon credits by 67 per cent.[21] This supports the case that sensible, investable pricing is supported by compliance markets, like BNG, rather than voluntary markets.

Current compliance markets, like BNG and nutrient neutrality, have the potential to deliver significant benefits for nature but are not big enough on their own to reverse nature's decline. BNG in England only applies to land used for development plus a potential ten per cent additional land area if units are created offsite. The Climate Change Committee suggests an additional two per cent of land area will be needed for housing in 2050.[22] If all this land, plus ten per cent, was protected for nature under BNG, the land area set aside for nature in England would still only increase 0.44 per cent by 2030.[23] This is a tiny contribution, representing just over one per cent of the government's target of protecting 30 per cent of land for nature by 2030.

New compliance markets, created by regulation, are needed beyond the housing sector to ensure that all sectors of the economy are playing their part in protecting and restoring nature.

The history of biodiversity net gain (BNG)

BNG was introduced under the 2021 Environment Act, becoming mandatory for housebuilders from February 2024. The regulation requires developers to produce a net gain in biodiversity of at least ten per cent, ideally onsite, but if this is not possible then offsite, or through buying biodiversity credits from a government repository. It will be expanded to cover Nationally Significant Infrastructure Projects (NSIPs) from 2025, and the Department for Environment, Food and Rural Affairs (Defra) is working on an equivalent policy for the marine environment called Marine Net Gain.[24]

Creating this compliance market in law took a long time, with over a decade of lobbying from environmental groups, pilot studies and consultations. Six biodiversity offsetting pilots were set up by Defra between 2012 and 2014, which demonstrated that a voluntary approach was not sufficient to deliver genuine net gains or a level playing field for developers.

Four years later, in 2018, Defra published a consultation on mandatory BNG and provisions were made for it in the 2021 Environment Act.[25] Further detailed consultation was published in 2022 on biodiversity metrics and implementation.[26] The regulation was finally made mandatory in 2024.[27]

Nature cannot wait another decade for the next compliance markets to be created. The UK has legally binding targets to halt species decline by 2030 under the 2021 Environment Act and a commitment to the international target to protect 30 per cent of land for nature by 2030.

New compliance markets should learn lessons from the creation of BNG and build on the evidence already compiled on biodiversity metrics, for example by the TNFD.

Beyond biodiversity net gain: which other sectors should have compliance markets?

All sectors should contribute to maintaining the natural assets upon which the economy depends. However, creating new compliance markets, like the one that exists for BNG, requires a sector specific approach that considers current regulation and market dynamics.

The logical place to start with compliance markets for nature are the sectors with the biggest impact. Building housing and infrastructure has a direct impact on nature on land and in water, so mitigating those impacts is an obvious place to start. However, the sector with the largest impact is food, with over 60 per cent of land in England used for agriculture.[28]

Agriculture is the largest contributor to biodiversity loss, water use and nutrient pollution globally.[29] In the UK, it is the major driver of water pollution, causing more damage than the water industry.[30] However, the industry is also hugely reliant on natural assets and vulnerable to degrading soil quality, drought and flood risk, and biodiversity loss. Reconciling these vulnerabilities and the industry's position as a key driver of nature loss requires an understanding of market dynamics within the food sector. Placing additional requirements or costs onto farmers, many of whom are already struggling with profitability, would be unfair. The supermarkets, food manufacturers and multinational food companies are the businesses profiting from the current system.[31] Carefully designed policies should target those with the power to create change within their supply chains.

The water sector also has clear impacts on nature, through water treatment and sewage works, but it too depends on natural assets to provide clean water and reduce its responsibility for flooding and drought risks. Regulation of this sector is ripe for reform, with many objectives currently not met.[32] Current regulation is ineffective and inefficient, with many requirements enforced in ways that prevent use of nature-based solutions. Setting objectives at catchment scale on biodiversity, water quality, flooding and drought risk, and value to consumers, could enable more investment in the nature-based solutions to infrastructure challenges the water industry faces.[33] Close monitoring and enforcement of water company activity is necessary to ensure objectives are delivered.

Next steps for nature markets

There is no simple fix. Nature is complex and so are supply chains. The government needs to give certainty to investors and suppliers, who are currently interested but nervous. They can do this by setting out a roadmap for how policy will drive demand in new nature markets, and what contribution is expected from private sector investment to meet UK nature restoration targets, such as target to have 30 per cent of land and sea protected for nature by 2030.

The previous government aimed to deliver £1 billion of private investment into nature by 2030 but did not make clear how it expected markets to scale up to meet that, or what contribution would be expected from each economic sector. The government should now catalyse the growth of the market by providing a plan for its development.

The roadmap should include an overarching statement of ambition on private finance for nature and a timeline of key decisions and relevant milestones. It should cover three key categories of action:

– **Economy-wide actions that support all businesses to invest in nature.** This should include a timeline for when reporting under TNFD will become mandatory in the UK and how the government plans to agree the definition of what 'nature positive' means for business.[34] It should also include a review of fiduciary duties regulation and how they can be reformed to include nature.

- **Sector specific plans for creating new nature markets through regulation**. This should focus on the food and water sectors initially.
  - For the water sector, the announcement of an independent commission to review regulation is welcome.[35] This should ensure reforms actively encourage investment in nature-based solutions, rather than preventing it. On flooding, the Regulated Asset Base (RAB) model should be investigated as a potential approach to managing flood risk across water catchments, with contributions from insurance companies.
  - For the food sector, a joint Treasury, Department for Business and Trade and Defra commission is needed to investigate new incentives for supermarkets and food producing companies to invest in nature through their supply chains. The commission should include food industry, academic and civil society representatives. It should also consider creating new compliance markets and charging levies on businesses.
- **Immediate action to bolster investor confidence.** This should include publishing the consultation on the governance of carbon and nature markets and including nature-based credits in the UK Emissions Trading Scheme.

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Endnotes

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