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FINANCING THE BLUE ECONOMY IN SMALL STATES

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Key Points

- The blue economy approach offers small developing states — countries with populations of 1.5 million or less — the opportunity to diversify from a narrow production base; invest in and develop growth and employment opportunities in a wide range of both existing and new sectors and industries; and shift away from predominantly land-based industries toward those that integrate and sustainably develop a broader range of land-based, coastal and ocean-based sectors.
- Small states have had limited success, and are at the very earliest stages of mobilizing and securing finance and investment for the blue economy, with most resources typically confined to established areas rather than new blue growth sectors.
- A small but growing number of international public financing and other innovative instruments are emerging to finance investments in nascent and new sectors, but many challenges remain in scaling up finance and attracting investments in a wider range of blue growth sectors. A strengthened enabling environment to attract investment, improved information sharing among small states, support from international development partners and new partnerships to leverage blue investments are needed to overcome these challenges.

Introduction

The blue economy approach seeks to balance growth with sustainability objectives. It offers small island and coastal developing states, and the regions in which they are located — primarily the Caribbean, Pacific and Indian Oceans — a unique and untapped opportunity to break their dependence on a narrow range of goods and services, predominantly tourism, fisheries and agriculture, and to expand into new blue growth sectors, including marine biotechnology, deep seabed mining (DSM) and ocean renewable energy.

Pursuing the blue economy requires access to affordable long-term financing at scale, yet small states have thus far experienced limited success in catalyzing public and private investments in the blue economy at scale. Immediate financial constraints, common to most small states, include a lack of fiscal space, and stagnant or declining flows of both official development assistance and foreign direct investment. Among Caribbean and Pacific small states, many also suffer from large, unsustainable levels of external debt. Other challenges include: developing the enabling conditions for the blue economy, including the institutional, regulatory, governance, legislative and human resources needed to achieve both intersectoral and transboundary coordination; the high upfront research, development and capital costs; and insufficiently developed ocean industry technologies. Not unique to small states, these challenges have proved daunting for much better resourced developing countries, many of which still lack institutional support and capacity to achieve integrated coastal and ocean management (Economist Intelligence Unit 2015).

Current Sources of Blue Financing

Three trends are evident in financing the blue economy in small states: there is significant financing and investment in several coastal and sea- and ocean-related blue economy sectors, through an array of blue financing sources and instruments; there is nascent but very limited success in developing new and innovative financing mechanisms; and small states are failing to attract financing for several blue growth sectors, each with largely untouched potential for growth and economic transformation. Collectively, current financing is — and will remain — insufficient for the blue economy to represent a serious transformative pathway for small states. Finding ways to break the short circuit between abundant opportunities to diversify and limited access to finance is — and will continue to be — one of the most important development challenges facing these countries.

Success in Some Sectors

Small states have had encouraging success in attracting blue financing to support sectoral and intersectoral planning and for policy coordination, and have also attracted blue investments in sustainable fisheries development and protection, aquaculture, water and waste treatment, and for addressing marine ecosystem degradation. Most financing to date has been provided by international public finance sources, including through grants and loans from global and regional development banks, other development finance institutions and both bilateral and multilateral donors. Significant sources include the Global Environment Facility (GEF), United Nations Development Programme (UNDP), the World Bank Group, the United Nations Environment Programme (UNEP) and the United Nations Food and Agriculture Organization (FAO). Globally the GEF and the UNDP have financed catalytic interventions to address marine ecosystem degradation and the loss of livelihoods, with more than $1.1 billion[1] of GEF investment leveraging $4.7 billion in co-finance for water, environment and community security projects in over 170 countries, including the majority of small states.[2] The World Bank Group has provided approximately $6.4 billion in blue financing in developing countries, including approximately $1 billion in sustainable fisheries, aquaculture and for the conservation of coastal and ocean habitats, and $5.4 billion for coastal infrastructure, including waste treatment, watershed management and other activities that help reduce coastal pollution.[3] The FAO has established the Blue Growth Initiative, catalyzing policy development, investment and innovation, and supporting several blue economy sectors, including aquaculture, capture fisheries, seafood systems and the promotion of ecosystem services.

Small states are benefiting both through direct country support and through multilateral programs supporting regional institutions of which they are members. For example, in financing fisheries development and the protection of the marine environment in the Southwest Indian Ocean, the World Bank Group has developed a regional program in collaboration with the Southwest Indian Ocean Fisheries Commission, which focuses on managing shared resources and ecosystems among small states in the region. The World Bank Group has also established a similar $33 million regional program to support select Pacific countries and institutions, including the Federated States of Micronesia, the Marshall Islands, the Solomon Islands, Tuvalu, and the Pacific Islands Forum Fisheries Agency. The FAO has accorded a dedicated focus to small island developing states (SIDS) members, crowding in blue financing and technical support for SIDS in the Caribbean, Pacific and Indian Oceans (see FAO 2016).

Emerging Financial Innovation for the Blue Economy

Recent financial innovation is also helping to attract new private investors, including impact investors, private philanthropic sources, foundations, family offices and non-profit organizations, and is simultaneously encouraging the governments of small states to allocate an increasing share of domestic public revenues in blue investments. Two among these — marine conservation financing and the emerging use of innovative financing instruments — offer particular promise for scaling up blue financing.

Marine conservation: A number of small Caribbean and Pacific states already generate resources from visitor entry fees from tourists to safeguard marine protected areas (MPAs). For example, Belize collects tourism entry fees in excess of $2 million to fund conservation projects, and Palau utilizes such fees — estimated to be in excess of $27 million — to improve wastewater management, thereby protecting coral reefs. These states are also beginning to use a variety of more innovative financing mechanisms and, in so doing, are contributing to developing markets for the payment of ecosystem services, such as marine and coastal protection, in which small states are particularly well placed to provide services. The Caribbean Challenge Initiative, a collective endeavour by 10 countries, has committed to conserving at least 20 percent of near-shore marine and coastal environments in MPAs by 2020 and to creating National Conservation Trust Funds, with new financing mechanisms

1 All figures are in US dollars.

2 See www.thegef.org/gef/International_Waters

3 See www.worldbank.org/en/topic/environment/brief/oceans.

to provide for the management and protection of these areas. Over 50 new marine/coastal protected areas have been declared and the Caribbean Biodiversity Fund, a $42 million regional endowment, financed by the German government, the GEF/World Bank and The Nature Conservancy, provides annual disbursements to the national conservation funds (The Nature Conservancy 2016).

Similar initiatives — such as the Blue Halo partnership in the Caribbean, a private sector collaboration with Barbuda, Montserrat and Curacao, financed jointly by private investors and domestic tourism revenues — are also helping to finance the development and implementation of sustainable ocean policies, with private investors providing stakeholder surveys, ecological assessments and other services, while governments commit to developing sustainable ocean policies and create dedicated funds to finance implementation.[4]

Moreover, the scope to expand finance for marine protection is vast and largely untapped. The World Wildlife Fund identifies over 30 potential sources, including through grants, donations, revenues from the fishing industry, energy, mining and biodiversity prospecting (Spergel and Moye 2004). A recent survey notes that development finance institutions such as the World Bank's International Finance Corporation and the European Investment Bank — both potential sources of blue financing in small states — already committed $21.5 billion in conservation impact investments during the period 2009–2013, and are likely to increase this by a further 50 percent in the next five years (NatureVest and EKO Asset Management Partners 2014).

Innovative financing instruments: Two other financial instruments have also recently emerged. The first is debt swaps for conservation, which mobilize private impact investor resources to swap out high-interest-bearing sovereign debt in exchange for governmental commitments to conservation and climate adaptation and mitigation. The Seychelles is proceeding with a $30 million debt for conservation swap, in exchange for the government's commitment to enhance marine conservation and climate adaptation, including protecting important tuna feeding grounds. The initiative will also establish a permanent endowment generating sustainable financing for Seychelles' marine conservation and climate adaptation activities. The second is blue bonds — an adaptation of land-based green bond instruments to finance the ocean economy. The Seychelles plans to issue blue bonds in 2016, the first trial of this instrument among small states. Bond sales, facilitated by multilateral institutions including the World Bank and the African Development Bank, will fund the implementation of a fisheries management plan to develop the Seychelles' semi-industrial and artisanal fisheries sector. If successfully trialled, both debt swaps and blue bonds offer significant new blue financing potential for small states.

4 See http://waittinstitute.org/bluehaloinitiative/.

Limited Additional Blue Financing

For all the promise offered by the blue economy, there has to date been minimal actual investment in small states in several sectors with growth and economic transformation potential, in particular marine renewable energy, marine biotechnology and DSM. In marine biotechnology, progress in attracting financing and investment has been almost negligible, despite marine biology featuring as a prospective transformative investment opportunity for SIDS in the Mauritius Declaration, a globally agreed strategy for the sustainable development of SIDS, as early as 2005.[5] Notwithstanding a recent report estimating that the global market from products derived from marine biology could exceed $4 billion, no small developing states appear to have established national marine biotechnology research centres and only a handful, including Mauritius, have begun to develop marine biotechnology products.

The marine renewable energy sector is characterized by high upfront research and development costs and as yet unproven technologies in some sub-sectors, limiting private investors' interest. Even among developed countries, project setbacks, fatigue among venture capital investors and the harshness of the marine environment have all limited the development of tidal and wave energy, suggesting that significant investments may be unlikely in the medium term (Bloomberg New Energy Finance 2014). Nevertheless, an indicative $2.5 billion project pipeline of potential public-private projects in SIDS has recently been developed, together with a specific initiative, the Blue Guardian Initiative, focusing on new opportunities to develop ocean energy resources in order to build climate-resilient island economies.

Separately, although DSM offers small states, in particular those in the Pacific, enormous potential for growth and economic transformation;[6] it also poses many technological, economic and environmental risks, including the danger of substantial damage to marine ecosystems, deep-sea carbon sinks and economically important fisheries. In the Cook Islands, despite identified mineral resources, a five-month open tender process failed to register a single bid for DSM, due to the depressed state of global mineral markets and the high-risk, high-cost nature of DSM. Despite challenges, a number of countries, including

5 See Mauritius Declaration and Mauritius Strategy for the Further Implementation of the Programme of Action for the Sustainable Development of Small Island Developing States, United Nations, www.un.org/ga/search/view_doc.asp?symbol=A/CONF.207/11&Lang=E.

6 See Pacific Community (2016).

Papua New Guinea (PNG), Tonga, Kiribati and Nauru, have initiated DSM exploration. PNG is expected to commence commercial DSM operations in 2018, and Nauru has begun developing the legislative and policy environments to exploit seabed minerals in international waters, establishing a National Seabed Minerals Authority and passing an International Seabed Minerals Act in 2015 (Pacific Community 2015).

Key Policy Actions

While small states are making modest progress in attracting finance and investment for the blue economy, capitalizing on the transformative potential of the blue economy will need financing and investment at scale, across a much wider range of countries and regions and in many of the emerging and new blue economy industries that offer the potential to transform small states' long-term growth prospects. Several key policy actions can help develop this approach.

First, national and regional initiatives to develop an enabling framework for the blue economy should be strengthened. Greater, more reliable flows of long-term financing can only emerge in the presence of an enabling framework for the blue economy. Small states need to redouble their efforts to mainstream the blue economy in national and regional development plans; and to establish an effective enabling framework for the blue economy, including governance, institutional and policy frameworks that reflect the transboundary and the integrated land, coastal and ocean characteristics of the blue economy. Practical initial steps include strengthened coordination and cooperation across sectors and ministries, developing new national and regional capacities in activities and skills supportive of the blue economy, for example, in marine spatial planning, oceanographic mapping, ocean conservation and marine protection, and in integrated cross-sectoral planning. Small states, supported by development partners, can develop new information-sharing portals and intra- and inter-regional databases on blue investment project financing.

Second, domestic resource mobilization for the blue economy should be strengthened. Sustaining the transformation to a blue economy will necessitate much stronger reliance on domestic financing, requiring small states to progressively convert public expenditure from land-based to integrated land-based, coastal and ocean-based investments. While this process has commenced, in particular through the development of MPAs, more substantive initiatives are needed to develop new revenue streams that can be reinvested in further blue economy investments.

Third, sharing knowledge and absorbing regional and other tools and lessons of good practice are key. Sharing knowledge on the blue economy, through lessons learned and evidence of success, assists countries and regions to make the short-term investments needed to transition to a blue economy in the longer term (UNEP 2015). Among many examples that can be of use to small states are the ISLANDS program of the Indian Ocean Commission, which links spatial development planning with integrated policy frameworks for the blue economy to help policy makers understand policy choices and trade-offs in developing strategies for the national and regional blue economy, and the United Nations Economic Commission for Africa, which has developed a practical seven-step guide for African countries to mainstream the blue economy into national policies, laws, regulations and practices.

Fourth, a new approach, led by small states and supported by international development partners, is needed to capture and share information on the sources, instruments and uses of blue financing in and for small states. Initiatives to capture information on financing the green economy — for example, the Climate Bonds Initiative — can be emulated and developed for the blue economy, and initiatives such as SIDS Dock, which shares information on renewable energy initiatives in SIDS, can be broadened, to include a wider range of sectors, including blue financing for aquaculture, marine biotechnology and DSM, providing information on sources, terms and recipients of blue finance.

Fifth, partnerships between small states should be expanded and new sources of blue finance should be explored. Deepening existing partnerships and exploring new initiatives may be pivotal to future resource mobilization. Partnerships to date have been effective in honing small states' policy positions, mobilizing international acknowledgement of small states' unique vulnerabilities and fashioning global goals relevant to and achievable by small states. Some have also attracted some blue finance, but not at the scale needed. Small states can more actively forge new institutional partnerships — for example, with the Group of Twenty, the New Development Bank, the Asian Infrastructure Investment Bank and other emerging international financing institutions — to promote blue infrastructure in small states.

Conclusion

Despite the odds, small states are making steady progress in securing blue financing and investment; however, this progress is piecemeal, and too slow and insufficient to convert the transformative potential of the blue economy into reality. Increased policy effort by small states and strengthened support from international development partners can help accelerate blue finance. In some new ocean industries, technological and other constraints are likely to limit the ability to attract financing at scale for the foreseeable future.

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About the Author

Cyrus Rustomjee is a CIGI senior fellow with the Global Economy Program.

At CIGI, Cyrus is looking for solutions to small states' debt challenges and exploring the benefits of the blue economy. His research looks into how small countries in the Pacific, the Caribbean and elsewhere can benefit from greater reliance on the use and reuse of locally available resources, including those from maritime environments.

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In addition to the blue economy and domestic resource mobilization, his research has previously focused on diaspora finance and innovative financing for development as well as on migration issues.

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CIGI Policy Brief No. 75
Cyrus Rustomjee

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Jason Thistlethwaite and Melissa Menzies

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Céline Bak

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Growth, Innovation and Trade in Environmental Goods

CIGI Policy Brief No. 67
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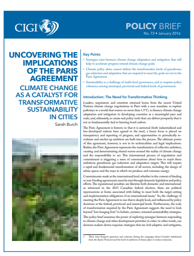

Uncovering the Implications of the Paris Agreement: Climate Change as a Catalyst for Transformative Sustainability in Cities

CIGI Policy Brief No. 72
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Global Treaty or Subnational Innovation? Canada's Path Forward on Climate Policy

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Sarah Burch

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CIGI's current research programs focus on three themes: the global economy; global security & politics; and international law.

CIGI was founded in 2001 by Jim Balsillie, then co-CEO of Research In Motion (BlackBerry), and collaborates with and gratefully acknowledges support from a number of strategic partners, in particular the Government of Canada and the Government of Ontario.

Le CIGI a été fondé en 2001 par Jim Balsillie, qui était alors co-chef de la direction de Research In Motion (BlackBerry). Il collabore avec de nombreux partenaires stratégiques et exprime sa reconnaissance du soutien reçu de ceux-ci, notamment de l'appui reçu du gouvernement du Canada et de celui du gouvernement de l'Ontario.

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