How do financiers value the environment? Or, why a pile of stones is not a house

And its link to displacement, dispossession and alienation of the non-human world....

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Where are we going with PSD?

Objectives

- To understand how financial networks in Africa (and tax havens) link natural assets to international private equity funds, and donor development finance
- To give a brief overview of how self defining 'impact investing' or 'developmental' private equity funds build in concern for the 'environment' into their investment decision-making

Argument

- 'high net worth individuals' (HNWIs), 'permanent tourists' (PTs), and 'politically exposed persons' (PEPs) are investors in a privatised international 'virtual' space , sometimes as a consequence of displacement or dispossession of others
- Private equity currently employs a thin, partial, and pseudo mathematical method of assessing environmental impact and worth
- Environmental and developmental impact 'science' is a performative *political technology* which adds legitimacy to their authority.
- Private equity has lead the financialisation of the non-human world

1 Financialisation

Most presenters have evidenced the financialisation of the non-human world in new products

For example:

- “for capitalism to make an accumulation opportunity of environmental crisis it needs to create new products, new commodities, that can be invested in, traded and speculated on” (Sullivan, 2010: 4)
- Capital making new natures that is ‘can see’ (Robertson, MM, 2006) such that “the earth-in-crisis is rethought and reworded such that it is brought further into alignment, conceptually, semiotically, and materially with capital” (Sullivan, 2010: 4)

Financialisation in this talk is conceptualised within the ‘normal mainstream’ capital market (cf Adam Harmes), not in new carbon markets or new commodities representing an aspect of environmental damage (biodiversity derivatives, species banking, environmental

1.1 Financialisation cont:

- The two ways of conceptualising financilisation (new and additional; old and mainstream) are related since
  - ‘new’ products have precedents (cf debt-for environment swaps; loans for ‘non-development’/conservation)
  - Many new products are linked to offsetting the consequences of accumulation elsewhere, in the mainstream economy, where environmental impact must thus be measured, evaluated and priced.
  - Some ‘new products’ are rebranded or reclassified prior existing ‘old’ companies and funds. (cf impact investing, eco-funds, natural capital, green bonds) in green-wash processes

1.2 Many definitions of financialisation

- Widely used at an *abstract theoretical level*, akin to the Marxian notion of the ever greater commodification of life and resources under capitalism.
- Alternatively it is applied to *discrete and limited financial instruments*, such as carbon trading.
- Together financialisation [from this literature review] could refer to
  - the depth and spread of financial markets
  - combined with new innovative complex financial instruments, including a spectacular range of short term and abstracted derivatives and futures products
  - accompanied by a growth in all types of debt finance and the consequent dominance of financial over productive capital and consumption.

1.3 Conceptual map

But, the weakness of current theorisation is that it exists on several levels whose interconnections are not well built:

- the abstract theoretical where it is closely entwined with neoliberalisam;
- the micro, where it is discussed in specific financial instruments and policy.

The interconnection between definitional levels occurs in identifying the structure and agency of the relationships that 'carry' financialisation into human lives and non-human worlds, through the *actual mechanisms and institutions* which codify financial practices as power

Then, we need theorisation of the wider structural consequences of

1.4 Mechanisms and institutions

- Financialisation does not ‘just happen’, but has agents which employ money as a *technology of power* (aka Foucault), using the money form to quantify human and physical contexts, privilege financial parameters and pecuniary factors in decision-making, and thus return decisions in favour of money-holders.
- Financialisation works particularly through private equity funds investing in natural resources, mostly using secrecy jurisdiction domicile, which cre-order (Nitzan and Bichler) a particular pattern of ownership and

1.4.1 An example, Mineral Deposits Ltd, Senegal

Australian gold mining company, funded by the CDC through a private equity fund in Mauritius (Private Eye, 16th April 2010).

The Mauritius companies facilitated a movement of wealth out of Senegal (where the company nominally never makes a profit, and which has a 30% tax rate) to the order of

- USD 12.4 million in tax-deductible "technical assistance" fees
- USD 11.1 million in 2009 for the leasing of mining fleet equipment
- USD 42 million in tax-deductible interest payments on loans to the offshore parents.

In short, Mineral Deposits Ltd paid just USD 45,000 in tax in Senegal, while benefiting from tax exemption of USD 14.6 million (Private Eye, 2010).

Supporters of the view that development is achieved in this way say that without this company structure

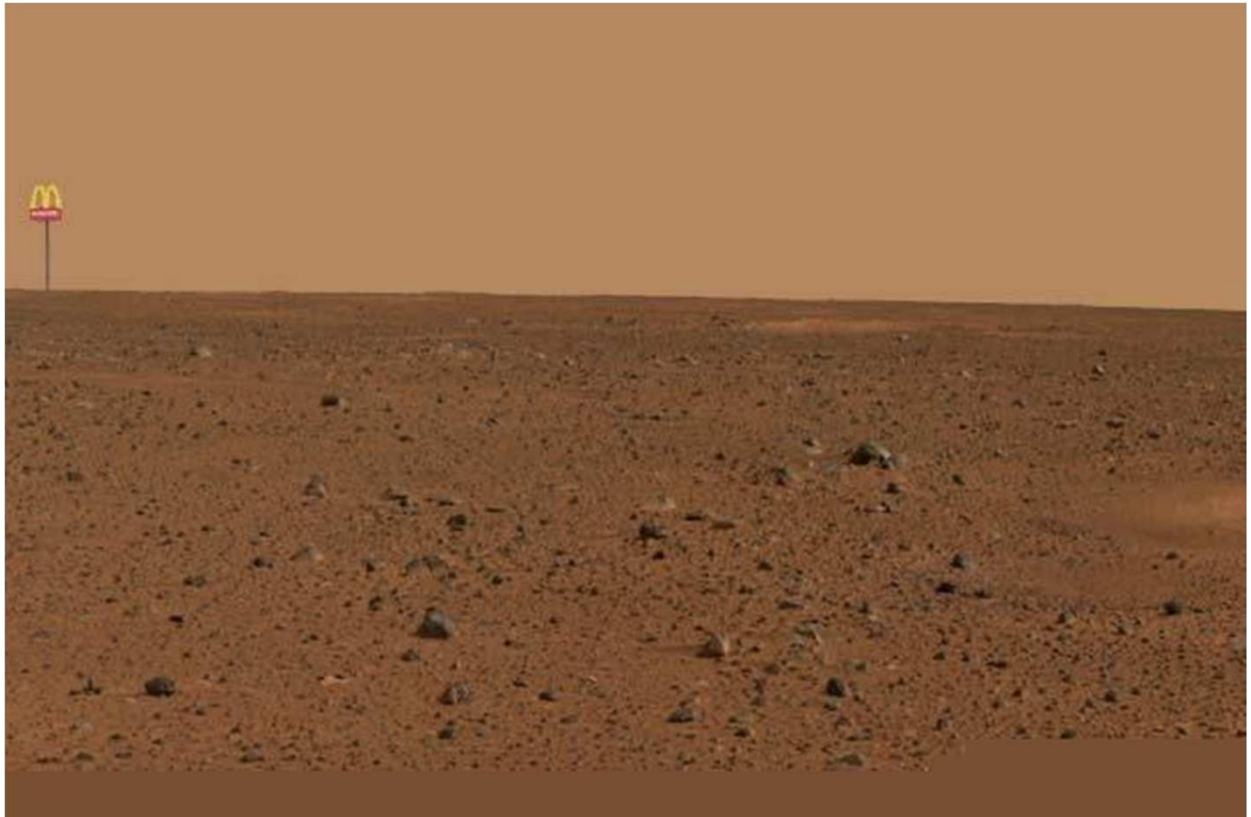
- the foreign direct investment would not arrive at all

1.5 Wider consequences

- Financialisation also serves to dissemble sovereignty and national economic space through the making of spaces of exception from law and regulation (tax havens), creating challenges for the future of democratic management of environmental resources.

- Cf. Nitzan and Bichler, *Capital as Power* thesis:
  - "capital is not a narrow economic entity, but a symbolic quantification of power…[capital] represents the organized power of dominant capital groups to reshape – or *creorder* – their society" (2009, auth emph) .... and economy

Life in 2030?



2 finance, DFIs and environment

- What does this new financialised structure of the global economy, and the predominance of private equity, mean to the environment?
- This question critically depends on financiers' investment decisions, and how environmental impact is managed in risk instruments – since risk and return are the parameters of the way market makers set price

- And of course the 'postscript' paperwork, EIAs

2.1 DFIs and PE Funds

- Researching DFIs gives a window into world of private equity proper (cf Bracking et al, 2010, funded by Norad)
- DFIs, as pseudo public institutions are supposed to be market leading in reform and 'good ideas'
- Claim to lead on green energy (at least Norfund does)
- And mirror behaviour of private sector in order

2.2 DFIs frame this as PSD

- Private Sector Development (PSD) interventions of four types:
  - **Market architecture**, improvements to soft infrastructure, efficiency of banking, tax, import export, information (state agency)
  - **Regulatory Concessions**, treaty largesse, ethical trade, supply chains (state agency)
  - **Harnessing private sector** Catalysing change in pre-existing corporates, promoting CSR, impact investing
  - **Project or firm based**, equity or loans, DFIs and

2.3 DFIs operational principles

principle of cial contribution	To supplement, complement but not displace market operators [IFC 'non-displacement provision'] Providing capital which would not otherwise be available or suitable	Modifying the risk-reward relationship Design, experience, expertise To validate that private sector not willing to participate without IFIs
business principal	funds are transferred under market disciplines to ensure profitability	Engineer acceptable rates of return Be as efficient as a market operator [including through tax avoidance and minimization]

2.4 DFI Working principles

objective or principle	Explanation	Instrument
nenting capital flows	Public funds can provide critical weight to other investors' efforts	Improving capital market efficiency Leveraging in the private sector 'Piercing the [credit] ceiling'
onstration effect	A successful project encourages imitation by other firms.	Set up a unique commercial venture Providing equity, loans and management (E,L and M) 'infant industry' investment
erating investment risk	Expertise and standing in relation to domestic government and the capital markets provides insurance against investment and political risk	Providing a 'Seal of Approval' Providing an 'umbrella of deterrence' against default Negotiating with government and partners Innovative sharing of risk
ytic principle	Proving minority stake to catalyse others' crowding in	Leveraging equity by providing core stake Securing political 'go-ahead'

3 DFI governance

- Various aspects of work in DFIs compartmentalised.
- Environmental impact assessment has a separate Department and relationship with others is complex
- Role of EIAs in Board-level investment decision-making opaque
    - Have to be ‘seen to be written, but not written to be seen’ (Brassed Off)
- Cf history of resignations from World Bank, in particular around Chad-Cameroon Pipeline and Extractive Industries Review (which advocated

3.1 World Bank Environmental Assessment

Category A: A Category A project is likely to have **significant adverse environmental impacts that are sensitive, diverse, or unprecedented.** These impacts may affect an area broader than the sites or facilities subject to physical works. The EA for a Category A project examines the project's potential negative and positive environmental impacts, compares them with those of feasible alternatives (including the "without project" scenario), and recommends any measures needed to prevent, minimize, mitigate, or compensate for adverse impacts and improve environmental performance. For a Category A project, **the borrower is responsible for preparing a report,** normally an Environmental Impact Assessment (or a suitably comprehensive regional or sectoral EA).

- **Category B**: A Category B project has **potential adverse environmental impacts on human populations or environmentally important areas** - including wetlands, forests, grasslands, and other natural habitats - which are less adverse than those of Category A projects. These impacts are site-specific; few if any of them are irreversible; and in most cases mitigatory measures can be designed more readily than for Category A projects. The scope of EA for a Category B project may vary from project to project, but it is narrower than that of Category A assessment. Like Category A, a Category B environmental assessment examines the project's potential negative and positive environmental impacts and **recommends any measures needed to prevent, minimize, mitigate, or compensate for adverse impacts** and improve environmental

3.2 IFC's new proposal 6

- 'Working towards' actual ceilings and targets in pollution
- But compare with established means to 'price in' environment as
  - risk of disruption [by environmental movements]
  - or litigation [by concerned literate classes]

3.3 IFC does care...[but just] through bottom line?

- Thus, the IFC's *Planning and Financial Valuation Model for Sustainable Investments* is designed to show that investing sustainably guarantees financial return, to encourage mangers to make developmental investments (IFC, 2010).
- In this, 'environmental risk' is defined through disturbance to financial returns
- attributes to environmental movements a powerful ability to disrupt, as issues of disruption, appropriations and lawsuits figure heavily in 'sustainability related risks' and are 'priced in'.
- Fund Managers are urged to take heed and 'do the right thing' *a priori.*
- Also, arguable that recent cases have expanded concern with reputational risk, particularly if exposure in media or Owner

IESTER
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f Manchester

4 European DFIs

- Development impact measurement in European development finance institutions (DFIs) includes environmental aspects
- Recently reviewed this (Bracking and Ganho, 2011) (funded by Norwegian Church Alliance)
- Using three research questions:
  - In what ways, and using what tools and systems, do development finance institutions measure the developmental impact of their work?
  - How effective are the measurement tools in use?

4.1 The challenge [assumptions]

- How do, or could, DFIs invest in a way which
  - Improves the income and livelihoods of the poor?
  - Contributes to social justice and wellbeing?
  - [development in a holistic sense]
- Important because if ‘smart’ policy guides investments this can cause substantial improvements in well-being
- Impact evaluation, in so far as it influences investment decision-making, can embed policy direction

4.2 Results overall

- An increasing amount of data is being generated. For example, CDC and Norfund now have extensive systems of social and environmental reporting.
- However, problems remain in terms of what the data tells us about development impact, and what they do with it once it is generated
- Some DFIs have improved their development impact evaluation systems and [claim they] are giving them a higher operational priority
- However, science of this is of poor quality, which has to put operational use in doubt

4.3 Current environmental impact assessment in DFIs

Science is built up of facts, as a house is built of stones; but an accumulation of facts is no more a science than a heap of stones is a house.

enri Poincaré, *Science and Hypothesis*, 1905).

roblems:

- how much 'change' can be attributed to the contribution of the development finance institutions. [They claim too much]
- what meaning should be assigned to the numbers generated [given poor directionality of indicators, and quality of proxies]
- the influence the results have on actual investment decision-making [not proved]
- And there are important commissions, omissions, exceptions and

4.4 Some examples

- CDC has recently (!) mandated Fund Managers to produce ESG data on portfolio companies, but compliance with the Investment Code is self-regulated by same fund managers, who rarely visit actual sites
- Many frameworks have voluntary sections and indicators (see Indicator Library]
- No framework enjoys majority support by DFIs, so no single system means little comparative data and low public trust
- But do not have to be published anyway – only ‘cases’ on websites
- FMO ‘scorecard’ has no ex ante environmental assessment of projects, and does not require Fund managers, direct investment company managers, or underlying investee companies to have any specific system for development impact assessment.

4.5 examples continued

- FMO assessment has somewhat arbitrary and low weighting for social and environmental factors [only approx 20% of 'points' in whole impact framework]
- Norfund is only DFI to have policy setting a preference against secrecy jurisdictions, but ESG reporting quality from underlying companies can be of poor quality
- Swedfund ex ante assessment does not include ESG, only risk and financials, with overreliance on 'honour code'. [Reporting of investee companies low and not mandated]
- Huge use of tax havens by DFIs sector: 81% Norfund portfolio, 164 CDC funds (Bracking et al, 2010)

4.6 Systemic problems

- ‘Positive influence effect ‘ on better environmental outcomes of ‘public’ DFIs is little proved, as unclear effect of board membership
  - Also low staffing, few visits, overreliance on FM assurances
- In DFIs, although portfolio companies, direct investments and funds all legally obliged to produce statistics, these are aggregated when reported to the public
  - Cannot check for the bad project in a good setting (low income country) effect
- DFIs carry significant reputational and political risks because of poor oversight standards and process indicators

4.7 Corporate Policy Project Rating (CPR)

- DEG sponsored impact tool now also used by Proparco (France), SIFEM (Switzerland), Bio (Belgium), COFIDES (Spain) and OeEB (Austria)
- But weightings in CPR favour financial criteria, and in aggregation poor ESG can be offset
- CPR assessment is only in relation to other portfolio companies.
- Company Boards have subsequent opaque powers to override DIAs. That is even when the ‘worst’ score is recorded a project can go ahead by ‘special exception’
- Not clear how ESG used subsequently to change firm behaviour or for decision-making

4.8 IFC uses DOTs

- Some Development Outcome Tracking (DOTs) IFC indicators of poor quality in terms of their relationship to the effect desired
- Also less expected in some contexts [don’t expect much in some countries].
- Scores only in relation to initial targets and low initial expectations
- Builds in pathologised and racialised views of FMs and excuses exceptionally high profits

4.9 Specific environment indicators

- DFIs only measure whether an environmental management system is in place and whether 'things are improving' against internally set targets. [cf IFC's social performance standards which similarly mandate procedures but not specific outcomes].
- No view is assigned to actual pollution levels
- The extra-territoriality of European environmental law is *not applied* (inc through EIB)
- FMO scorecard and DEG's influential CPR offset bad environmental performance against good scores in other areas
- At present the frameworks are too thin on benchmarking against international standards, particularly when this involves a mandatory obligation

4.10 Overall,

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P-EU Cotonou Partnership Agreement
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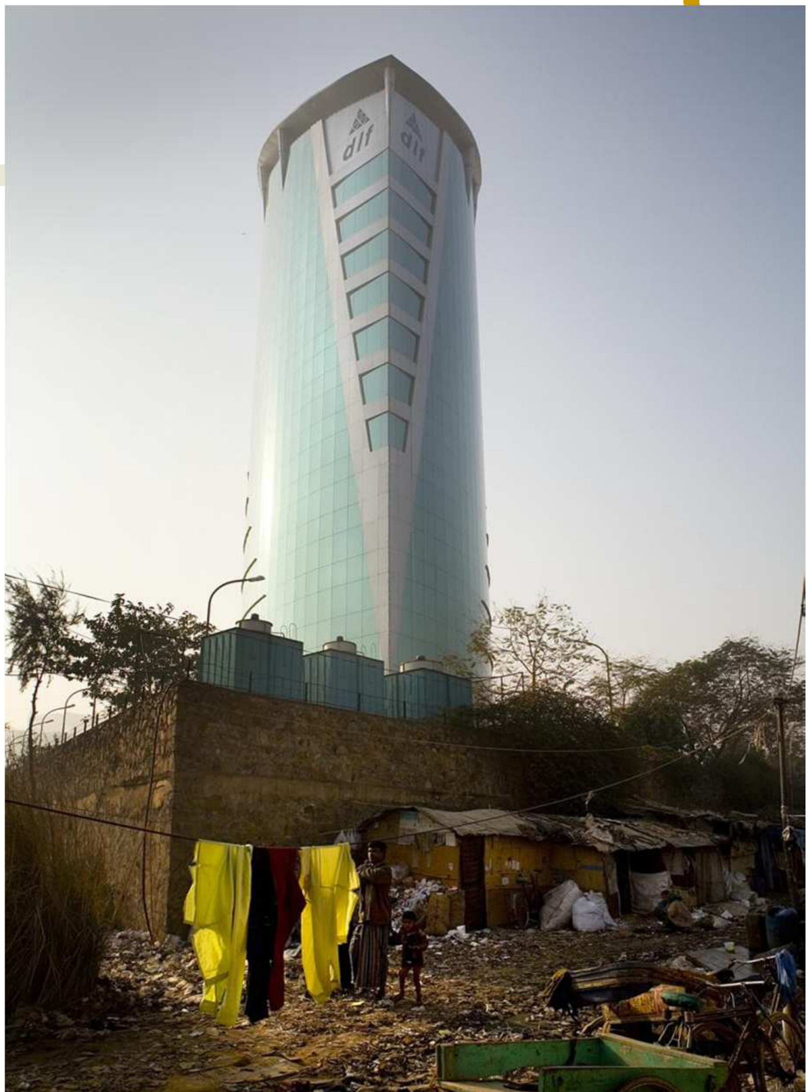


5 New indicators for DFIs required!

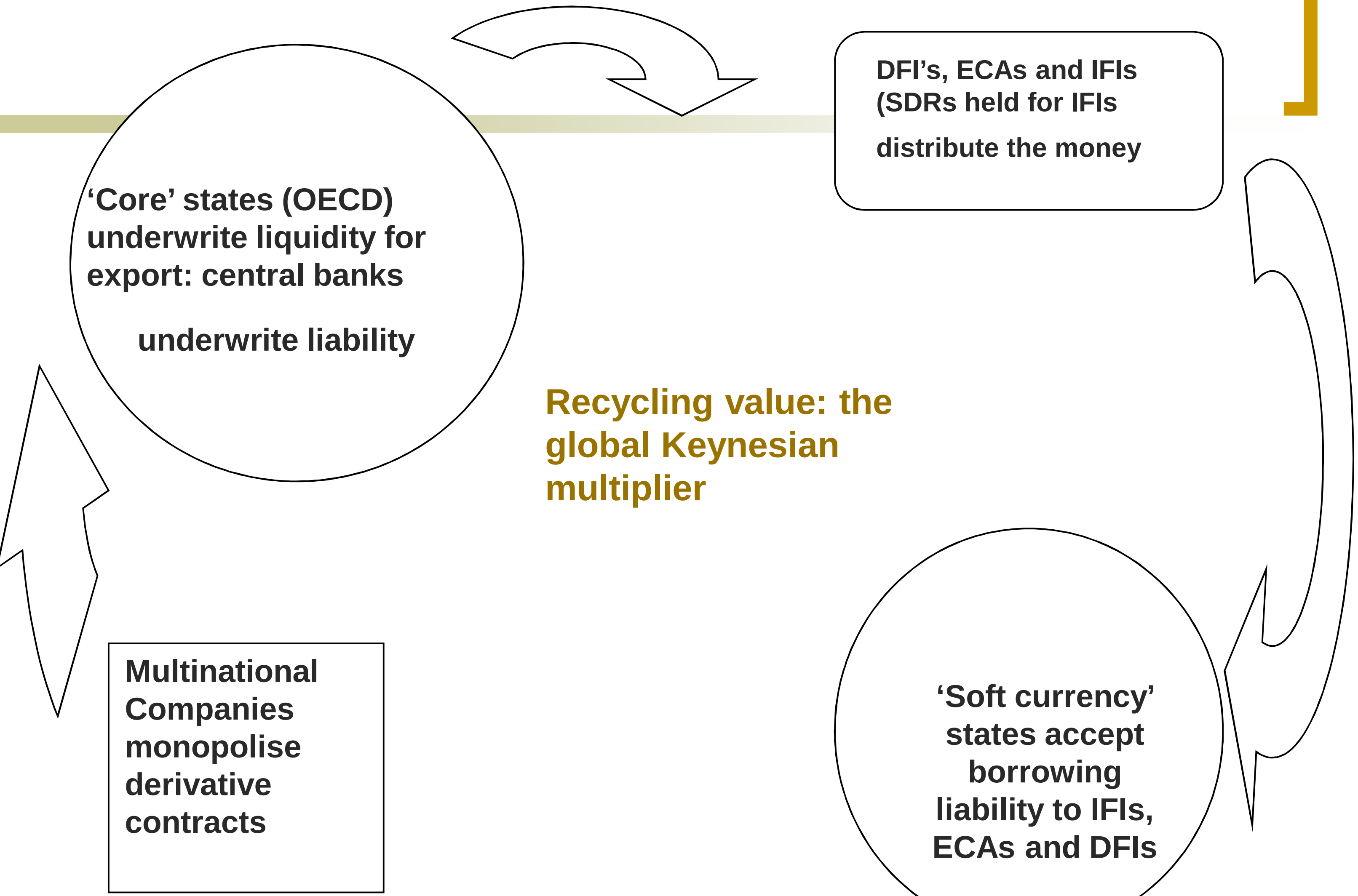
- *investment domicile*, incorporating a preference for onshore domicile
- *investment vehicle* (broadly funds, firms, SMEs, MFIs), including a ceiling on management fees and end-user interest rates
- *influence measure*, to mandate change by using conditionality on disbursements or government policy particularly in intermediated investments
- *corporate governance* indicators to benchmark them with relevant international standards
- *target sector* indicator, with a preference for supply-constrained sectors with proven developmental impact
- *employment process indicator*, to ensure trade union recognition and workers' rights.

5.1 And a change in the politics of private sector development

- There is no mandatory planning process! And thus no democratic accountability
- This would require (at least) an ex ante planning and consultation process
- This should be mandatory for large, risky or contentious investments.

Old Naledi PRA, Cobasys, 2011

5.2 Or system change?



6 Conclusion

- Environmental impact assessments begin when decisions on who, how and where investments will be made, are already determined.
- The DFIs, private equity funds and commercial bank intermediaries are largely ‘black boxes’ into which the public cannot see, and decisions made within the capital supply institutions are not clearly influenced by the data provided by development or environmental impact evaluation systems.
- The financialisation of the political economy in Africa has already lead to investment decisions being the sole preserve of financiers in the mainstream private economy.
- The current financialisation of the non-human world aligns itself to this wider pre-existing context
- Despite the faults in new offsetting mechanisms and product

PSD – state-sponsored export of capital?