Oxfordshire Nature Catalyst Investment Facility (ONCIF) – A proposal

I. RATIONALE

a) Background

Biodiversity is in decline globally, nationally and locally. The negative impact of this decline on the wider economy, and on human health and wellbeing is increasingly well understood.

Oxfordshire is one of the most nature depleted counties in the UK, which in turn is one of the most nature depleted countries in Europe, the most nature depleted continent globally.

With the advent of the Environment Act 2021, the UK Government is promoting new ways to monetise ‘ecosystem services’ (such as through flood mitigation payments, nutrient neutrality, biodiversity net gain and carbon credits). The new Environmental Land Management system of payments to the farming sector is also providing greater incentive for landowners to manage habitats for nature.

Meanwhile, recognising the financing gap to fund nature recovery, the UK Government has laid out plans to increase funding for nature including an aspiration to mobilise £1bn of private sector funding by 2030.

These developments – alongside the advent of Oxfordshire’s Local Nature Recovery Strategy - all provide opportunities to deliver a step change in the restoration of Oxfordshire’s lost natural habitats. But whether we successfully seize this opportunity will depend to a great extent on the availability of ready financing.

The Oxfordshire Nature Catalyst Investment Fun (ONCIF) will aim to catalyse new sources of financing to support nature recovery, bringing in new private, corporate and social investors interested in supporting nature projects capable of creating self-sustaining revenues.

b) Why an investment facility?

In order to mobilise investment in new nature markets, participants must have clarity and confidence in the market frameworks. This applies on both the ‘supply’ and ‘demand’ side of these markets, as well as to any potential investors.

In the case of habitat banks for mandatory Biodiversity Net Gain, for example, we can identify a number of potential barriers to uptake on the ‘supply’ side (i.e. landowners):

- Regulatory uncertainty: BNG is based on new and largely un-tested legislation. Like any legislation, it subject to public and political support. While there is a degree of imposed uniformity, individual planning authorities have a degree of discretion over implementation, affecting both the ‘demand’ side (implementation of planning policy, balance between on-and off-site) and ‘supply’ side (regulations – and hence costs - for the creation of habitat banks).
- Market uncertainty: While ‘mandatory’ BNG units have now begun to come on to the market, the supply is very limited and the price is high. While it relatively easy to predict

the short term outlook, it is almost impossible to predict what will happen to the price of units in the next 5 years.

- Cost of entry / operating risks: With the introduction of a formal regulatory framework for off-site BNG, landowners now face a considerable cost of entry as well as potentially greater risk. While the return on investment is potentially very high (revenues of £2-3 million on a 30-hectare site are not unheard of), it now costs £30-50,000 simply to register a site (incl. surveys, management plans, legal costs, as well as formal registration), before even any habitat creation or management works are undertaken. These up-front capital costs are usually borne entirely by the landowner.

From a potential investor's point of view, the lack of data for any likely return on investment in nature markets acts as a block on the in-flow of financing. Landowners are typically left only with the option of investing their own capital, effectively excluding smaller and less well-capitalised participants from the market.

The role of the proposed ONCIF would thus be to plug some of these investment gaps, reduce risks for potential participants, and to help ensure high quality delivery for the nascent market.

II. OBJECTIVES

The primary driver for change is the biodiversity crisis and its associated impacts on human health, and social and economic wellbeing.

Our underlying assumption is that a step change in nature restoration cannot solely depend on public or philanthropic financing, but must rely in large part on private sources of financing.

a) Purpose

To stimulate financially self-sustaining, revenue-generating projects which deliver measurable benefits in biodiversity and which are aligned to the Local Nature Recovery Strategy.

The facility will work to attract significant new and additional private, philanthropic and public investment into nature-based projects in the county. It will aim to build local capacity in green investment, collect and collect data on successful business models, and inspire more landowners, buyers and investors to participate in nature markets in Oxfordshire.

The facility will work to 'innovate, replicate, demonstrate and advocate'. In other words, it will seek to support innovative projects with the potential for both biodiversity enhancement and commercial return, replicating successful models and using the data from these initiatives to build participant confidence in emerging markets, demonstrating potential returns in different sectors of natural capital markets, and advocating to investors to put forward new capital.

b) Co-benefits:

1. Climate change: mitigation and adaptation.
2. Job opportunities generated by green businesses / nature-friendly farms, especially in rural areas of the county where there are fewer opportunities.

3. Sustainable economic development

III. MANANGEMENT ARRANGEMENTS

a) Delivery in Partnership

The Oxfordshire Nature Catalyst Investment Facility will be delivered in partnership, initially between the Trust for Oxfordshire's Environment (TOE) and the Oxfordshire Local Nature Partnership (OLNP).

As the legally responsible entity, ultimate responsibility for and management of monies held by the facility will be the responsibility of TOE Trustees in accordance with charitable law.

The boards of both the LNP and TOE will feed into the strategic direction of the facility, including the business plan and criteria etc.

Fund investment decisions will be made, in line with agreed criteria, by an Investment Group consisting of the major investors plus an agreed number of independent experts with ecological or related expertise.

As it is expected that proposals will come from nature organisations, landowners, and/or farmers, measures will be put in place avoid conflicts of interest in funding decisions.

Once initial proof of concept has been delivered, the project partners envisage bringing in either outsourced fund management expertise or a third-party partner to act as fund manager.

The day-to-day management of the facility will initially be overseen by a project team consisting of staff allocated from TOE and the Local Nature Partnership.

b) Planned function of the Facility

i. Overview

The aim will be for the facility to be cost-neutral to its initial investors, though there will be risk to the investment (particularly in the facility's early stages). Ultimately, the facility will aim to deliver a return in such a way as to attract commercial or semi-commercial investment.

The project will initially draw in an investment of £200,000 from the Trust for Oxfordshire's Environment. The facility will then seek to match this initial investment with contributions from philanthropic donors and public bodies within the first 12 months. Thereafter, it will use the funding it has secured and the track record it has built to attract private investment.

The aim of the facility will be, from the beginning, to maintain the principal investment, rather than spend it down as with 'traditional' public sector grant funding. Hence contributions from public and philanthropic bodies will be repayable after 5 years, if required. Alternatively, these initial investments may be recycled into the facility for a further 5 years, allowing them to continue to deliver environmental and economic impact through financing natural capital projects.

Furthermore, the aim will be to use the pilot investments to leverage at least a further £X million in additional private investment into the facility in the first 5 years. This may initially be from philanthropic/semi-philanthropic social impact investment, but again the aim will be to draw in more commercial (for-return) investment, as the development of the natural capital markets allow.

iii. Scope and Selection Criteria

Once fully implemented, it is envisaged that the facility will operate across a wide range of investable natural capital markets in Oxfordshire.

Recognising the need to support both innovation and the emergency of new markets, the facility will have at its core only three core criteria. Projects will be sought that:

- Are capable of delivering measurable benefits for biodiversity;
- Are capable of delivering a return on investment.
- Are not able to self-finance, and/or are unsuitable for / unable to access mainstream commercial finance.

Full guidelines for applicants will be developed in the initial inception year of the project (‘year 0’), with input from investors and other stakeholders.

iv. How the facility will mobilise investment

In addition to the initial seed investment of £200,000 from TOE, the facility will seek further seed capital in its first 3 years from public bodies and philanthropic donors, either in the form of grants or ‘soft’ (non-commercial) loans. The intention is to raise a minimum of a further £1million over the first 5 years of operation.

This initial phase of the facility will, by definition, operate at higher risk. Markets will be evolving and emerging and data on performance will be scarce. Nevertheless, the aim will be to recover the initial funders’ Principal Investment within 5 years and repay interest on any loan component.

Beyond this initial investment phase, the intent behind the facility is to leverage in private investment, so we will aim to achieve this as soon as practically possible. Initially, this may be in the form of ‘social investment’, Environmental Social and Governance (ESG) payments, or tax-efficient semi-commercial investment bonds. Later, investment may be brought in on a more commercial basis.

It is envisaged that the facility may explore some or all of the following as means of leveraging inward investment into the facility:

Social Investment Tax Relief Loan / Equity	Individual investors into charities and social enterprises can claim 30% of the cost of their investment in income tax relief (provided certain conditions are met). Investors can't have their loan repaid or sell their shares for 3 years, although they can receive interest on loans.
Community Shares	A withdrawable, non-transferrable equity investment in a project or company. A form of equity because the investors get a share of the organisation, but which is not tradable.
Crowd Funding	An investment raised via an online platform and not secured against an asset. Individual investors put (mostly) small amounts towards a loan which is repaid on an agreed basis, usually with interest.
Philanthropic Bond	A tradable loan from a group of social investors over a fixed period of time with a fixed rate of interest. For example, if you issued a £2million bond over 5 years at 2% interest in 2017, you would pay the social investors £40,000 interest each year and repay the £2million in 2022.

v. How the facility will invest in Natural Capital projects

As with its strategy for raising funds, the facility will seek an adaptive approach to the outward investment models it employs, maintaining a flexible, responsive and evidence-based strategy to supporting natural capital projects.

While the precise modality will be developed during inception, an indicative initial operating model could be as follows:

- Initial focus on unsecured loans
- Low interest to attract those with less capital / social enterprises – envisaged at 5% with a small admin fee of, say, 2%.
- Initial 5-year minimum term (9-year maximum)
- Loans between £10,000 and £150,000
- Can cover both capital and revenue costs
- Some investment expected from the enterprise owner (e.g. 10% of total upfront costs)

Early investments may be semi-grant/'soft' finance – i.e. if the enterprise fails through no fault of the enterprise owner, then the loan may be either fully or partially written off. Again, a key driving factor for this facility is to encourage landowners to adopt new income generating strategies from their land, and this is partly about de-risking these new markets for those who are otherwise motivated to engage.

Social impact grants

Successful applicants could also have the opportunity to access to a Social Impact Grant set as a percentage of the loan amount. These grants would cover non-commercial or social impact elements of an enterprise, e.g. a regenerative farm offering educational opportunities for local school children.

Support and advice

The fund will aim to work alongside applicants / recipients to ensure both investment readiness and maximise impact. The facility will work with a range of LNP partners and the wider Oxfordshire business community to ensure that advice is tailored to individual needs.

Outline Timings

Assuming July 2024 approval in principle,

1. By end October 2024 agree initial arrangements for bids appraisal. Issue interim applicant guidelines advertise for expressions of interest. Agree initial governance and management arrangements.
2. By end December 2024 constitute investment committee
3. By end of June 2025, have deployed at least three initial investments to projects, to include timelines for the payments of money from the Fund.

IV. RISKS AND MITIGATION

a) Competition with other mechanisms

It is our understanding that this facility would be new and additional to the existing natural capital financing ecosystem, which is very limited at the present time.

Nevertheless, there are two related public or philanthropic initiatives which should be noted:

- **UK Nature Accelerator:** Implemented by Finance Earth on behalf of DEFRA, this is a national scheme aimed as brokering in new private sector financing to support the development of natural capital markets. While its aims broadly align with ONCIF, it is our understanding that the UK Nature Accelerator is looking for much larger-scale projects than those on the individual farm or small enterprise level. ONCIF will also eventually cover a broader scope of enterprise activities than the UK NA, and will have the advantage that it is aligned specifically to the Oxfordshire LNRS.
- **Loans for Enlightened Agriculture Programme (LEAP):** Implemented by the Real Farming Trust, this scheme offers social impact loans to farmers who are looking to make the transition to regenerative agriculture, as well as community-based food and farming enterprises which support more sustainable farming and food production. While there is some overlap in the potential scope of projects funded, LEAP does not have a particular focus on biodiversity. Moreover, the scheme is international (although most loans are given to UK businesses) and again would not be aligned to specific Oxfordshire LNRS or other interests.

The facility would look to coordinate activity with both these schemes as well as any other potential sources of funding and finance for natural capital projects in the county.

In addition, there are a small number of commercial lenders which are beginning to explore natural capital as a market for loan finance and other investment. Again, this scheme is not intended to compete with commercial sources of financing, a key criteria of the fund being that no other suitable source of financing is available. Rather, this scheme will seek to add value to the existing financing ecosystem, by supporting early-stage projects/markets.

Other risks / mitigation

1. Lack of initial public / philanthropic investment [Mitigation – broker initial discussions with local authorities, plus arms length bodies and Defra prior to inception]
2. Lack of private sector investment [Mitigation – public and philanthropic matching funding may be used to the risk element and encourage new sources of 'patient capital'. Can seek lower returns on investment or more favourable terms on demonstrator projects]
3. Double counting of public investment if landowners receiving other payments for public goods such as from ELMs (Mitigation – due diligence checks on projects)
4. Time lag between investment and nature benefits (Mitigation – long term management requirements built into funding agreements and regular reporting on project milestones)
5. Lack of landowner interest due to competing economic returns [Mitigation – TOE as a project partner having expertise in delivering nat cap projects. Does not necessarily require the use of most productive land to uplift nature benefits; this is what the facility is seeking to test]

A full risk register will be developed in Yr0 of the project.

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