Online Annex 5. Debt-for-Nature Swaps in Latin America and the Caribbean[1]

Debt-for-nature swaps have gained prominence due to the elevated public debt levels following the pandemic and the need to advance on the commitments to the United Nations' Global Biodiversity Framework, which aims to protect 30 percent of the world's land, ocean, and inland waters by 2030. Over the last two years, Barbados, Belize, and Ecuador completed large debt-for-nature swaps, using the proceeds from the issuance of blue bonds supported by credit enhancements to buy back existing public external debt at a discount or replace expensive debt with cheaper debt. These swaps provided debt relief and funding for marine conservation, while countries also committed to the implementation of other key measures to protect the marine environment.

Common financial features

Initial steps. The country's government and international partners—such as The Nature Conservancy (TNC), the Interamerican Development Bank (IDB), and the U.S. International Development Finance Corporation (DFC)—identified potential debt and debt service savings based on the country's existing debt profile, including debt that could be bought at a discount or with high service costs. They also identified marine protection initiatives that could accompany the debt relief operations.

Blue bond issuance. A Special Purpose Vehicle (SPV) was created to issue blue bonds, which are securities that commit the borrower to use a large part of the proceeds for marine conservation projects. The funds were then lent to the government in the form of a blue loan with the same terms as the blue bond in order to (i) buy back part (Barbados, Ecuador) or all (Belize) existing external bonds on the secondary market at below par market prices or existing domestic loans with high coupon rates (Barbados); (ii) establish an endowment fund to finance marine conservation projects in the long run (Barbados, Belize, Ecuador); and (iii) pay various closing costs and fees.

Credit enhancement. International partners provided credit enhancements to secure favorable terms for the blue loan. The DFC provided political risk insurance of non-payment of arbitral award and denial of justice for Belize and Ecuador, the IDB provided credit guarantees for Barbados and Ecuador, and TNC for Barbados. These credit enhancements allowed the blue bonds to have credit ratings several notches above that of the sovereign, lowering the interest rate on the blue bond, and allowing for a longer grace period and maturity. Blue loans for Barbados and Belize also included parametric insurance against hurricanes.

Debt relief and funding for marine conservation. The operations reduced countries' debt stocks while allocating significant resources to marine conservation (Online Annex Table 5.1). The latter included both annual government contributions to fund marine conservation projects during the duration of the blue loan and an endowment fund created with the blue loan, which will be reinvested during the duration of the blue loan and will be used to fund marine protection projects after the government's annual contributions stop.

Online Annex Table 5.1. Recent Debt for Nature Swaps: Key Indicators

	Blue Loan	Debt Retired	Immediate Debt Reduction		Average Repurchase Price	Funds for Marine Conservation
	(US$ millions)	(US$ millions)	(US$ millions)	(Percent of GDP)	(Cents per dollar)	(US$ millions)
Barbados	146	150	4	0.1	96.2	50
Belize	364	580	216	8.7	55.0	178
Ecuador	656	1,628	972	0.8	41.0	450

Source: IMF staff calculations.

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Main conservation commitments

Creation of a conservation fund. All swap deals included the creation of a conservation fund with a mandate to fund marine conservation projects. The fund's board is composed of international partners and local players, including the government, private sector, and CSOs. This institution enforces the payment of annual contributions by the government, selects the marine conservation projects to finance (other marine conservation commitments were agreed ex-ante), manages the reinvestment of the endowment fund for future marine conservation, assists the government advance on its other conservation commitments, and collect penalties in the form of higher conservation payments when key conservation milestones are missed. These penalties are not distributed to blue bond holders but are held by the conservation fund and are refundable once the government restores compliance with the commitments.

Barbados. The swap will provide $50 million for marine conservation, $23 million to the conservation fund (an average cashflow of $1.5 million per year for 15 years) to finance marine conservation projects between 2023 and 2037, and $17 million towards a long-term endowment fund, which will be reinvested for 15 years and is expected to generate additional $10 million in earnings. This fund will be used to finance marine conservation projects after 2037. Barbados also committed to develop a Marine Spatial Plan and to protect 30 percent of its ocean by 2030. TNC is supporting these activities with technical assistance.

Belize. The swap provided $178 million for marine conservation, including government contributions of $4.2 million per year for 20 years to finance marine conservation projects between 2022 and 2041, and an endowment fund projected to reach $94 million after 20 years of reinvestment, which will be used to finance marine conservation projects after 2041. Belize also committed to develop a marine spatial plan, expand the area of ocean it protects to 30 percent by 2026, and improve the regulatory framework for sustainable development. These commitments are bound by deadlines and progress is marked by milestones. Penalties apply if milestones are missed.

Ecuador. The swap provided $450 million for marine conservation, including government contributions of $12 million per year for 18.5 years for conservation activities between 2023 and 2041 and an endowment fund projected to reach $227 million by 2041, which will be used to finance marine conservation projects after 2041. The Galapagos Life Fund (GLF) was created to administer the endowment fund and marine conservation activities. The focus of the GLF is to develop and implement a management plan for the newly created Hermandad Marine Reserve, which covers 60,000 square kilometers between Galapagos and the Costa Rican border. The GLF also collects penalty payments if conservation commitments are missed.

Final considerations

Debt-for-nature swaps have helped reduce public debt and protect the marine environment in some countries in Latin America and the Caribbean (LAC) in recent years. However, these operations have been small and did not provide a universal solution for countries struggling with debt sustainability and nature loss. Scaling up the number and size of the debt-for-nature swaps can help countries in LAC strengthen fiscal and environmental sustainability at a time when financing is scarce.