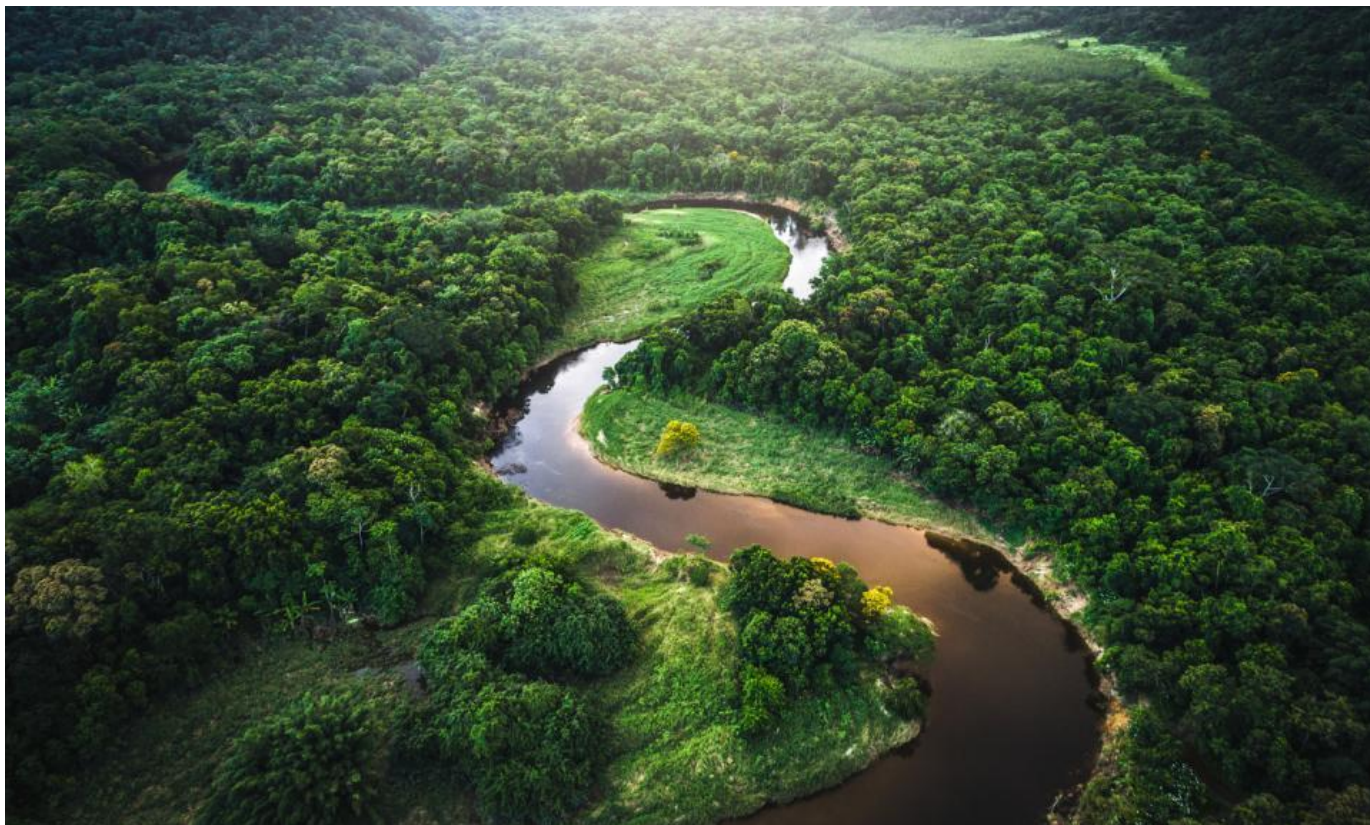


Brazil's (and the world's) climate conundrum



Written by

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Can Brazil attract essential foreign investment for climate initiatives without sacrificing its natural resources?

As Latin America's largest market, and [one of the world's ten largest economies](#), Brazil holds a vital global position as a bridge between developed and developing countries. In areas such as capital markets, democratic systems, and technological prowess, Brazil has the potential for a unique model of economic progress.

Environmental risk now threatens that potential. Through the haze of the fires burning in the Amazon, one thing has become clear: Brazil must find a new recipe for more sustainable economic growth.

The [Paris Agreement](#), of which Brazil is a signatory, set the target of keeping global temperature increases this century to below 2°C. In order to achieve its [individual contribution](#) to this goal, projections from Integrated Assessment Models indicate that Brazil will need, on average, around \$30 billion of investment per year by 2030 - rising to over \$60 billion per year by 2050 - in the energy sector alone. Given the Brazilian government's current drive to [slash public spending](#), this target cannot be met by the state.

Furthermore, Brazil's policies on land use - in particular, the conservation of tropical forests - will go a long way in dictating whether net zero emissions can be accomplished this decade. As made clear by the recent Intergovernmental Panel on Climate Change (IPCC) [Special Report on Land Use](#), transforming the ecological impact of agriculture will be a key element of both reducing greenhouse gas emissions and adapting to a warmer planet. The Amazon rainforest is a critical asset in the drive to stabilise the earth's climate due to its massive capacity to store carbon dioxide and its rich biodiversity.

With its huge potential for cost-effective emissions reductions, Brazil will be an important testing ground for global investment appetite in large-scale financial flows that don't throw open the flood gates to ecological destruction.

The scale of investments needed in food systems and forestry are beyond the capacity of Brazil's public balance sheet. While more robust than in neighbouring countries, domestic capital markets are not up to the enormity of the task.

Whatever the current political rhetoric, Brazil simply cannot afford to lose existing foreign aid and channels of direct investment. After the recent wave of [deforestation and fire](#), the big question is whether global investors will demand better environmental stewardship, or reduce their overall exposure to Brazil due to ecological risks. In response to Jair Bolsonaro's anti-environmental rhetoric, [Germany and Norway suspended their contributions to Brazil's Amazon Fund](#). That may have caught headlines, but the [suspension of Brazilian sovereign bond purchases](#) by some institutional investors poses a much bigger problem.

Barriers to progress

Private sector investment through capital markets is essential for Brazil's economic and ecological transition. "The public sector alone cannot finance the trillions of dollars needed for green infrastructure", [wrote](#) Akinchan Jain, a specialist at the World Bank, earlier this year. "We need to mobilise significantly more private sector flows to have any realistic chance of achieving climate goals." The obvious solution is to increase capital flows from the private sector. And while that seems straightforward in abstract, the practicalities will be challenging.

Climate-friendly investment involves low-carbon technologies that remain novel to investors. Furthermore, the volume of capital required will swamp the capacity of domestic investors. Foreign direct investment (FDI) can help plug the gap, but it's prone to flight during times of high political risk and environmental tension. So how can a government get in the "good" kinds of investment, while keeping out the "bad"?

The key question now is whether being "open for business" can be beneficial not just for short-term gain but for investments in sustainable technologies and infrastructure.

Of course, Brazil is not alone in this challenge. Dealing with climate change will require considerable financial flows to countries with immature capital markets and higher equity risk premiums. With its huge potential for cost-effective emissions reductions, Brazil will be an important testing ground for global investment appetite in large-scale financial flows that don't throw open the flood gates to ecological destruction.

Investing in the future

President Bolsonaro has declared Brazil open for business, promising tax cuts and regulatory environment changes designed to appeal to inbound finance flows. These changes will most likely include measures to address the country's perceived economic instability, complex fiscal system and issues with corruption – all areas with the potential to influence the attraction and retention of foreign capital. In any normal investment consideration, these moves would be viewed as unequivocally positive.

Taken in the context of stabilizing the earth's atmosphere, the [President's call to increase the rate of exploitation for non-renewable resources](#) makes Brazil a real flashpoint in the climate crisis. Brazil has some of the richest mineral deposits and largest rainforests in the world. It is endowed with a vastly disproportionate share of the planet's river water. Envious resources that most countries would be jealous to have. On the other hand, financial flows to poorly regulated mining and rampant deforestation have stripped Brazil of some of its most attractive long-term assets.

The key question now is whether being “open for business” can be beneficial not just for short-term gain but for investments in sustainable technologies and infrastructure. Finding a balance between conditions supportive to foreign investment and constraints that ensure all Brazilians share in the country's natural wealth has been tricky, to say the least. Even more so now, in Latin America's fluctuating political landscape.

Ultimately, Brazil's key challenge over the coming decade will be whether it can resume economic growth without sacrificing its natural resources and prioritise long-term reliability over short-term boosts. With environmental, social and environmental (ESG) issues rocketing up the agenda, can investors influence the shape of things to come?

Our ongoing research is searching for the ingredients in that all-important recipe – enablers that will allow Brazil to attract the investment it urgently needs in strategic, low-carbon infrastructure without opening the floodgates. Brazil's opportunity to be a world leader in driving sustainable, responsible development is too important to waste. Given recent events, there's no time to lose.

This article draws on work in progress for a research paper entitled 'The Flow of Capital for Climate Action in Brazil – The Role for Foreign Direct Investment', by

Janaina Stewart-Richardson, Alexandre Koberle and Dr Charles Donovan, due to be published in Q4 2019. The work has involved collaboration between researchers at the Centre for Climate Finance and Investment, the Grantham Institute – Climate Change and Environment (both Imperial College London) and Fundação Getulio Vargas (FGV), the top think tank in Latin America.

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Dr Charlie Donovan is former Executive Director of the Centre for Climate Finance & Investment at Imperial College Business School. He is currently Senior Economic Advisor at Impax Asset Management and Visiting Professor of Sustainable Finance at the University of Washington in Seattle.

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He is a lead author on the UN Environment Programme's Sixth Global Environment Outlook, a contributing author on its Gap Report, and a lead author for the Intergovernmental Panel on Climate Change's Sixth Assessment Report.