**RECOURSE: SUBMISSION TO THE FMO CONSULTATION ON ITS**

Position Statement on Phasing Out Fossil Fuels in Direct Investments

9 November 2020

**Preamble**

[Recourse](https://www.re-course.org/#about) works for a world where people and planet are at the heart of development: we campaign to redirect international financial flows away from dirty, harmful investments, towards greener and more inclusive development, working with partners around the world to hold financial institutions accountable. The social and environmental standards, including climate policies, adopted by publicly-backed development finance institutions form a crucial part of this accountability and help to ensure projects do no harm and promote development benefits.

Recourse welcomes this opportunity to make a submission to the FMO’s position statement. We are also a co-signatory to the Both Ends submission which covers wider climate issues; but in this submission, we wish to focus solely on the issue of financial intermediary (FI) investing.

**Climate action and the FMO portfolio**

Climate is a priority for FMO: one of the three ‘headline’ Sustainable Development Goals (SDGs) FMO focuses on in its work is SGD13 on Climate Action. In practice, “this means pursuing a portfolio that delivers positive outcomes on climate mitigation and adaptation;” and includes striving “to align our portfolio with a 1.5°C pathway.”[[1]](#footnote-1) This is a laudable ambition.

It is therefore surprising and deeply disappointing to find that FMO’s new climate policy does not apply to its entire portfolio, but only to FMO’s direct investments There is no rationale given for the omission of indirect lending to FIs in the draft Position Statement.[[2]](#footnote-2)

The rationale *for* including indirect as well as direct investments in the Position Statement is clear, for two important reasons. First, FI lending forms an important and growing part of FMO’s portfolio. FMO’s annual financial intermediaries portfolio in debt and equity more than doubled from EUR 600 million in 2016 to EUR 1.3 billion in 2019.[[3]](#footnote-3) Current financial intermediary investments total 338 - a significant proportion of overall business, at over a third of the total number of investments (919).[[4]](#footnote-4)

Second, FI investing is higher risk than direct investing, by its hands-off nature, leaving FMO potentially exposed to projects that do not meet its environmental and social goals. Recourse has advocated around the issue of FI investing for many years, including at the International Finance Corporation (IFC). Our work with partners[[5]](#footnote-5) helped to expose how IFC inadvertently supported over 40 coal plants through its FI portfolio and led to IFC introducing far-reaching reforms: developing a new approach to greening equity and taking action to ring-fence debt investments, in order to limit fossil fuel exposure.[[6]](#footnote-6)

The exclusion from the Position Statement of over a third of FMO’s business simply does not make sense and leaves a loophole which could end up undermining commitments and achievements in FMO’s direct lending portfolio. Such an exclusion risks policy incoherence and should be addressed as a matter of urgency.

An important step in achieving a low carbon economy, which is FMO’s stated goal, should be to support FI clients in shifting investments out of fossil fuels and into cleaner and more sustainable choices. FMO could play a critical role in achieving this – something that will not be achieved by merely ignoring this substantial portion of FMO’s portfolio.

We understand that it is more difficult to address indirect investments, but this difficulty should not stand in the way of action. There is existing good practice that FMO could emulate and adopt. IFC has demonstrated[[7]](#footnote-7) how fossil fuel exposure for both debt and equity clients can be addressed in FI lending and we urge FMO to adopt these lessons learned. Ring-fencing debt investments to exclude fossil fuels and working with equity clients to reduce fossil fuel exposure in line with a 1.5°C pathway are necessary steps to address FMO’s fossil fuel footprint in FI investments. We would be happy to work with FMO to develop the detail necessary for it to take these steps. To start with, here are the detailed recommendations that we provided to IFC when it was developing its Approach to Greening Equity: <https://www.re-course.org/wp-content/uploads/2019/05/Submission-to-public-consultation-on-the-Green-Equity-Approach-May-2019-final.pdf>

It is also essential that FMO be transparent about which of its FI investments are exposed to fossil fuel projects. This is particularly important given the findings of the recent internal review of the FMO’s FI business[[8]](#footnote-8), published on 4 November 2020, which assessed its contribution to SDG13 on climate action as follows:

**“SDG13 (Climate Action):**FMO also increased its contribution to SDG13 through its financial institutions investments in the past five years, although the growth of its green portfolio slowed down in 2019 (due to increased competition). By design, FMO’s green investments create a positive impact on SDG13. However, *the precise contribution could not be established at portfolio level*.” [emphasis added]

It is clear from the review that the current FI portfolio cannot be assessed in terms of its contribution to SDG13. To address this, enhanced transparency – including the name, sector and location of high-risk projects – is required. Additionally, if the Position Statement applied to FI as well as direct investments, FMO would be able to measure more accurately its contribution to SGD13, since mitigation efforts would be more effectively assured.

**In conclusion, we urge FMO to:**

* **Extend its Position Statement to include its entire portfolio, including direct and indirect investments;**
* **Improve transparency in FI lending to ensure robust monitoring and reporting.**

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1. https://www.fmo.nl/news-detail/04e58852-2d73-44a9-8b93-79b6d33262ee/fmo-opens-consultation-on-next-step-in-climate-action-commitment [↑](#footnote-ref-1)
2. https://www.fmo.nl/l/en/library/download/urn:uuid:a33fb062-2f52-44e0-9e1e-c0992fe6cd45/201006+final+draft+fossil+fuel+position+statement\_for+consultation.pdf [↑](#footnote-ref-2)
3. https://www.fmo.nl/evaluation-financial-institutions [↑](#footnote-ref-3)
4. https://www.fmo.nl/worldmap?search=&region=&year=&projects=allProjects [↑](#footnote-ref-4)
5. See, for example: <https://www.re-course.org/wp-content/uploads/2019/04/Digging-Deeper.pdf>; <https://www.inclusivedevelopment.net/wp-content/uploads/2018/04/Philippines-Coal-Report.pdf>; https://www.inclusivedevelopment.net/wp-content/uploads/2016/09/Outsourcing-Development-Climate.pdf [↑](#footnote-ref-5)
6. https://www.devex.com/news/opinion-a-new-ifc-vision-for-greening-banks-in-emerging-markets-93599 [↑](#footnote-ref-6)
7. https://www.ifc.org/wps/wcm/connect/05541643-0001-467d-883c-5d7a127ffd57/IFC+Greening+Report+Sept+2020.pdf?MOD=AJPERES&CVID=nisvaOC&ContentCache=NONE&CACHE=NONE [↑](#footnote-ref-7)
8. https://reporting.fmo.nl/FbContent.ashx/pub\_1000/downloads/v201103155523/200701%20Final%20report%20FI%20Evaluation\_ext.pdf [↑](#footnote-ref-8)