Balancing profit and planet

Summary
- The introduction of the Taskforce on Nature-related Financial Disclosures (TNFD) has increased focus on nature-related considerations in pension schemes, but a gap remains between awareness and action.
- Confusion persists around distinguishing between climate and nature risks, which complicates decision-making for asset owners.
- Despite regulatory developments challenges persist, such as a lack of governance structures for biodiversity and concerns over market returns.

Paige Perrin explores how pension funds integrate biodiversity into investments, the impact of the TNFD, and the challenges of managing nature-related financial risk

The urgency to address climate risks beyond climate change and net-zero commitments is growing, with pension funds increasingly recognising the need to integrate biodiversity considerations into their portfolios.

However, despite this awareness, the Pensions and Savings Lifetime Association (PLSA) reports that only 17 per cent of surveyed pension funds have a 'strong familiarity' with the Taskforce on Nature-related Financial Disclosures (TNFD) recommendations.

Moreover, 55 per cent of funds have yet to identify nature-related financial risks in their portfolios, indicating that awareness of TNFD does not always translate into direct action or a positive understanding.

Pensions for Purpose chair and founder, Karen Shackleton, acknowledges this 'major shift' in priorities for the pension industry. Its analysis from the group reveals that 65 per cent of asset owners have already integrated nature and biodiversity into their sustainability strategies, with an additional 20 per cent planning to do so within the next year.

Despite this accelerating trend, Shackleton points out that it is primarily driven by financial materiality, rather than regulatory mandates, with 75 per cent of asset owners acknowledging the financial risks associated with biodiversity loss.

This financial dependency on nature is further emphasised by Hymans Robertson DB investment consultant and biodiversity lead, André Ranchin, who highlights that over half of global GDP ($58 trillion) is reliant on nature.

He also points to a joint report from the Environmental Change Institute and the Green Finance Institute, which indicates that nature-related risks could have a greater impact on the UK economy than the 2008 global financial crisis or the Covid-19 pandemic.

However, Phoenix Group sustainable investment nature lead, Chris Hart, challenges the separation of climate and nature risks, calling it "increasingly unhelpful".

Instead, he says: "Investors need to quickly move to integrated decision making that balances nature, climate, social and economic factors, redirecting finance at scale towards more optimal and sustainable outcomes, while meeting our most pressing environmental, social and economic priorities."

Regulations

Regulatory frameworks are gradually adapting to reflect the interconnectedness of climate and nature risks, with policymakers increasingly emphasising the need for pension schemes to align with broader sustainability goals.

WTW Thinking Ahead Institute co-founder, Roger Urwin, acknowledges that implementing nature-reporting frameworks is "a lot more challenging" than handling market risk metrics.

Urwin emphasises the principle of "what gets measured gets managed" and suggests that as trustees face increasing demands on their time, prioritising nature considerations can become difficult.

PLSA policy lead, George Dollner, emphasises the importance of the Financial Markets Law Committee (FMLC) paper, which, although primarily focused on climate change, also suggests applications for nature, biodiversity, and environmental issues.

Dollner explains: "This should provide reassurance to trustees that they can apply the principles of the FMLC guidance to a range of new objectives and issues."

At a global policy level, Ranchin views the Kunming Montreal Global Biodiversity Framework as a "key milestone" for biodiversity and nature-related considerations.

He states that this framework "helps pension funds and other financial institutions understand the direction of travel and scale of change required to reverse biodiversity loss".

Ranchin also highlights various biodiversity measurement frameworks, including guidance from the Finance for Biodiversity Foundation, the Science-Based Targets Network, and the Nature Positive Initiative, which help pension funds integrate biodiversity into their financial decision-making.

In addition to these frameworks, Shackleton says some funds are using corporate engagement strategies, pushing asset managers to disclose their nature-related dependencies and risks.

However, Hart argues that nature and biodiversity-related regulatory requirements are still "some way" behind climate and carbon emissions considerations but says the upcoming Environmental Improvement Plan, expected in mid-2025, could improve this as it will outline statutory actions necessary to meet environmental commitments and targets.

Challenges and opportunities

Hart also emphasises the urgency of addressing nature loss, stating: "Nature's continued degradation has very significant consequences in terms of the outlook for the global economy and financial system stability. Without action to stop and reverse nature loss, physical risks will rise significantly but it is harder to identify where these risks will manifest within investment portfolios."

Adding to this challenge, Shackleton remarks that few pension funds have dedicated governance structures for biodiversity, with most still embedding it within broader environmental, social and governance or climate policies.

However, she notes that this is beginning to change with the adoption of the TNFD framework.

"Reporting remains in its early stages, with many funds initially incorporating nature-related sections into responsible investment reports before committing to full TNFD-aligned disclosure," she says.

Hart highlights the success of the framework, noting that over 500 organisations have committed to producing TNFD reports and predicts that the adoption of voluntary disclosures on nature will grow in 2025 and 2026.

Beyond its usability, Hart stresses that TNFD's "substantial" guidance material and support for capacity building in both private and public sectors have helped drive its adoption.

Despite the growing momentum, Hart also points out a key challenge: Many investors perceive biodiversity initiatives as likely to yield sub-market-level returns.

He says that this perception creates tension for fiduciaries, especially those operating under mandates that do not explicitly include impact criteria but believes there is a growing alignment between restoring nature and delivering competitive, risk-adjusted returns for investors.

"Gaining exposure to the winners from economic system transformation can deliver attractive and competitive risk-adjusted returns across asset classes for investors again aligning fiduciary duty with climate and nature goals," he explains.

Next steps

To better integrate nature-related considerations into their portfolios, Dollner encourages pension funds to take proactive steps, emphasising that action does not need to be "perfect" or involve "drastic innovation".

He suggests engaging in training opportunities, conducting portfolio assessments, reviewing engagement and stewardship activities and exploring nature-based investment opportunities as useful starting points.

"We also urge pension funds to consider what they can learn from their experiences with Task Force on Climate-related Financial Disclosures reporting," he adds.

Ranchin highlights recent innovations in the nature investment space that can help pension funds manage biodiversity and nature-related risks. These include nature-based climate solutions, innovative technologies supporting the transition to sustainable practices, green and blue bonds, and biodiversity credits.

Looking ahead, Shackelton suggests the pension industry should view nature-based solutions as an investment opportunity, explaining: "Proactively investing in nature-positive strategies can help mitigate financial risks while unlocking long-term value."

She stresses the importance of integrating biodiversity risk into decision-making processes, supporting TNFD-aligned disclosures and engaging with policymakers.

It is crucial for both the pensions industry and policymakers to recognise the link between environmental stewardship and financial stability.

By prioritising sustainable investments, pension funds can secure strong returns for their members while contributing to a healthier planet for future generations.

Written by Paige Perrin