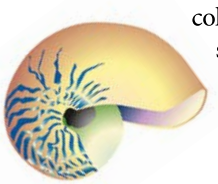
Biodiversity in the spotlight

Summary
- Pension funds are under pressure to increase investment in protecting biodiversity.
- Investing for impact can be highly compatible with fiduciary duty.
- The financial industry is innovating to make it easier to measure biodiversity risk and to invest for positive impact.

Gill Wadsworth reflects on the important role pension funds have in protecting biodiversity and why it matters today and into the future

"Without significant policy change or investment, the interplay between climate change impacts, biodiversity loss, food security and natural resource consumption will accelerate ecosystem collapse, threaten food supplies and livelihoods in climate-vulnerable economies, amplify the impacts of natural disasters, and limit further progress on climate mitigation."

This is the stark assessment from The World Economic Forum's *Global Risk Report 2023,* which places biodiversity and ecosystem collapse as the fourth most significant global risk over the next 10 years.



And given that the UN says more than half of the world's gross domestic product – which amounts to $44 trillion – is moderately or highly dependent on the services nature provides, the need for urgent action is clear.

Governments and policymakers are responding. The UN COP15 biodiversity summit in Montreal last December established the Kunming-Montreal Global Biodiversity Framework (GBF) which includes the '30x30 pledge' – an agreement to safeguard 30 per cent of land and water by 2030 to halt and prevent biodiversity loss. This means finding at least $200 billion per year by 2030 in biodiversity-related funding and raise international flows towards developing countries to at least $20 billion per year by 2025.

Analysis provided by the Paulson Institute shows that while investment in reversing biodiversity decline is increasing – in 2019 financial flows were between $124 billion and $143 billion – these are far short of the estimated $722 billion and $967 billion needed over the next 10 years.

Taking responsibility

Pension funds are seen as pivotal in ensuring the requisite finance reaches projects that will both limit further decimation of the natural world and contribute to preserving and restoring it.

This June the Zoological Society of London (ZSL) and Caceis Investor Services published a guide to biodiversity and nature for pension funds, in which ZSL senior sustainable finance specialist, James Pilkington, said: "Instead of passing the responsibility of these issues on to their asset managers, pension funds must start to understand and take ownership over the risks and impacts of their portfolios, and put clear policies and actions in place."

This view is shared widely across the pensions industry.

Scottish Widows head of responsible investments and stewardship, Maria Nazarova-Doyle, says: "It is imperative that pension fund investors seek alternatives that preserve and enhance our planet's natural capital. Given the size of their portfolios, pension funds hold considerable sway as asset owners and shareholders to promote positive corporate action on reversing nature degradation."

Meanwhile, Cardano co-head of

sustainability, Will Martindale, says that without action on biodiversity it will be impossible for pension funds to meet their carbon reduction targets.

"We see biodiversity as the other side of the coin to climate change and so it matters because we're going to be unable to achieve our climate change targets without addressing biodiversity loss. And biodiversity loss, as an issue in its own right, is as serious if not more serious than climate change; the implications of that for societies and economies are profound."

A report from Pension for Purpose and Gresham House, which assessed UK asset owners on their approach to natural capital and biodiversity, found that most pension funds consider biodiversity in relation to climate change, and found that "the level of interest in biodiversity and natural capital solutions has mainly been driven by pension funds implementing climate mitigation strategies. For most funds, natural capital investment is seen as part of their journey towards net zero".

That said, 62 per cent of pension funds surveyed held no natural capital investments, a figure that Pictet Asset Management head of business development, Kate Rickards, says reflects the levels of knowledge and understanding of biodiversity issues.

"When we are talking to our UK client base and the consultants that advise them, there is a top-level understanding that we have this crucial need to halt biodiversity loss. That message is starting to climb up the agenda rapidly, to the point where it's as important as bringing down global warming. But it is still early days and many pension funds haven't worked out what actions they want to take," Rickards says.

Investment consultants are central to informing that action, and the Pensions for Purpose/Gresham House report finds "some investment consultants are better informed on biodiversity than they were at a similar stage when pension funds first started considering climate action".

It notes that advisers have invested "significant resources" to develop expertise on ESG, sustainable and impact investment, and they are "well placed to help pension funds embed biodiversity into an investment strategy".

But the challenge, according to Pensions for Purpose founder, Karen Shackleton, is the "limited universe of natural capital investment managers" in which to invest.

However she adds: "*[Natural capital asset management]* is a really fast-moving space and asset managers are piling in to areas such as sustainable forestry and agriculture."

Fiduciary duty

Integrating ESG issues into

What does it all mean – defining the terms

Biodiversity: The natural world around us, and the variety of plants, animals, insects and microorganisms that can work together in ecosystems to maintain and support life on earth, and exist in delicate balance.

Natural capital: The world's stocks of natural assets, which include geology, soil, air, water and all living things. It is from this natural capital that humans derive a wide range of services, often called ecosystem services, which make human life possible.

Source: ClientEarth and Convention on Biological Diversity

investment practice and decision making is becoming a standard part of the regulatory and legal requirements for institutional investors, but concerns persist over the possibility that trustees may be accused of pursuing social causes over financial return.

Pictet client portfolio manager, thematic equities, Yi Shi, who runs an Article 9 classified fund under the Sustainable Finance Disclosure Regulations, says investing for impact can be highly compatible with fiduciary duty.

"The fundamental thesis that drives the creation of this fund is that the true value of nature, natural and social capital is not properly priced in to a company's stock price today, but the action they take will be reflected later on."

He adds: "High quality companies that have acted on climate change and are providing solutions to reducing environmental footprint have seen their multiples improved, as they could capture the underlying secular growth in the environmental solutions market, vis-à-vis those of companies that didn't. The same principle applies to biodiversity."

Pensions for Purpose is attempting to tackle some of the concerns investors may have about jeopardising returns by looking at performance of impact funds.

"Although there is much less fear from trustees about losing return *[from investing sustainably]*, it is still there. There is no definitive evidence on how impact funds contribute to positive performance, so we're hoping to try and address that for UK pension schemes," Shackleton says.

Establishing metrics

A major challenge for proponents of biodiversity investment is measuring a company's impact, but there are notable advances in overcoming this obstacle.

The Taskforce for Nature-related Financial Disclosures (TNFD) is, like its carbon-related predecessor, focused on "developing and delivering a risk management and disclosure framework for organisations to report and act on evolving nature-related risks".

At the same time, the Science Based Targets Network – a global coalition of more than 80 environmental non-profits and mission-driven organisations – has released the first corporate science-based targets for nature.

These initiatives are complemented by industry efforts including a joint sponsorship between Cardano, Fidelity International and Nomura Asset Management of Green PRAXIS, a nature-based solution provider, to conduct a bioacoustics study.

Martindale says the study, which monitors and measures biodiversity levels associated with varying land use intensities at a palm oil concession and conservation areas, produced "encouraging and clear results".

"As an investor we're waiting for a company disclosure, which may be incomplete or inaccurate, or a company may file one or two years in arrears from when the activity then took place, and so we're getting data that's really stale."

Martindale continues: "Bioacoustics tools measure the noises associated with the variability of species in those areas, which in theory is going to provide datasets that allow us to have much richer conversations with those companies about their ability to reforest and manage biodiversity issues within the land for which they're responsible."

Written by Gill Wadsworth, a freelance journalist