Community of Practice
Financial institutes and Natural Capital (CoP FiNC)
Summary February 4, 2015

- Investing Strategy -

Opening

Caroline van Leenders opens the fourth meeting of COP FiNC. Central question is which investment strategy improves the impact on natural capital the best? Caroline summarizes the developments since the previous session (November):

- The focus on natural capital increases: meeting on Impact investing at Triodos, WRI about finance for climate at SER (New Climate Economy), iMVO Covenant and the Natuurtop.
- International developments in natural capital: presentation EU Platform B@B workstream Finance, participation CoP FINC participants in Natural Capital Protocol.
- The Green Table FINC starts on 19th of March and aims to mobilize system actors around FiNC for upscaling. Participants: IUCN, True Price, WRI, WWF, VBDO, MVO NL, Green Business, PBL, SFL, IDH, Avans University, Ministry of Economic Affairs, Ministry IenM, PBL and Green Deal board.
- Caroline and Anne-Marie published the findings of the Community of Practice Business and Biodiversity (2011-2013). The publication provides insight into the relationships of dependence and impact on natural capital from business. It gives insights for financial institutions as enablers of green growth.

Presentation Annona, Nathalie Brouwer-Fast

Host SPF Beheer has asked one of its funds to give a presentation about their methods regarding natural capital. Annona ("Goddess of the Harvest") is a venture capital fund that wants to show that positively investing is possible. Annone invests in agricultural SMEs from Africa and Latin America to achieve economic growth in areas with labor-intensive processes. The funds running for 5 years now and the exits are expected to be realized within a period of 5 to 8 years. Annona chooses companies that have a track record; companies with customers and suppliers in countries where legislation exists. The whole chain must be traceable; it comes to long-term relationships with suppliers and customers and to shorter chains. Annona has a social purpose, but also wants to meet a required return for its shareholders. The social goal is a higher price for the farmers and training in order to prevent diseases. Natural capital is preserved by preventing land degradation by set aside land for a year. Depending on the situation, companies pay 5 to 13% interest on loans. And there are equity loans for a period of 5-8 years. Annona is a closed-end fund, because SPF Beheer at one time needs money to pay pensions. Annona is an "alternative investment fund" with a report obligation to DNB. DNB sees it as an investment fund, although pension funds are the owners, and annual detailed reports have to be delivered to the supervisor. Together with the quarterly reports to shareholders, this poses a substantial administrative burden.

Presentation Sustainalytics, Wilco van Heteren

Sustainalytics analyzes ESG data for investment decisions. The presentation concentrates on which investment approaches (exclude, best-in-class, impact investing, active ownership and ESG integration) work well for different asset classes (listed equity, non-listed and private equity, corporate bonds, sovereign bonds and lending / project finance). Important is the question "why you invest". Is the aim is to pay retirement later, or is it to contribute to a better world? Achieving two objectives with one instrument is tricky. You need long term thinking and enough opportunities to connect these goals. Some highlights:

1. *Exclude*: Research by Sustainalytics shows that exclusion has little to no effect on behaviour of large companies, because they can attract investors elsewhere.
2. *ESG*: the impact of ESG (particularly considering the impact on, and the dependency of companies on natural capital) shows limited impact on investment decisions of listed companies.
3. *Best-in-class*: there appears to be limited influence.
4. *Sovereign bonds*: there appears to be a relationship between companies and countries. This is not yet reflected in models of investors. With government bonds the degree of dependence of an economic structure in a country can affect the creditworthiness of a country. Therefore government bond investors also look at impact of companies and sectors that are of great economic importance for a country.
5. *Lending*: not many new conditions are set with regard to natural capital.

The Global Sustainable Investment Review 2014 by GSIA shows the growth of sustainable investing per strategy from 2012 to 2014: Exclusion 74%, ESG integration 117%, Best-in-class -1%. Also mentioned are Sustainability Themed Investing 136% growth, Impact Investing 26%, Engagement 54% and norms-based screening 82%.

Lessons exploring Investment Strategy improving the impact on natural capital

Strategy

- There should be more focus on *resilience* and dependency on natural capital.
- When the relationship between *risk and return* and attention for natural capital are demonstrated to be positive, there will be more for natural capital positive investment decisions.
- *Exclusion* can precede commitment. In an era of change, one should continue to exert influence and not exclude too quickly.
- You can achieve much with a *combination* of strategies. For example, combine impact investing with best-in-class, active ownership and possibly exclusion beforehand.
- Global Compact violators are 2 years on the 'watch-list' of Sustainalytics. You can apply *ESG engagement* with companies that violate before investing in them.
- An intensive and *long-term dialogue* with companies is crucial. This calls for an increase in knowledge and training for the investor and the investee. An example is the Strategic Equity Portfolio a portfolio with 60 to 80 companies and a scope of 7 years. Companies are positively selected and regular meetings take place on the structure and operations.
- Impact is possible by applying *positive selection*.
- With *best-in-class* check the relevance of available data.
- *Voting* at shareholders' meetings may have an impact, but the voting chain is used so far on governance, bonuses and appointments.
- By 'doing good' you create demand (pull, impact investing), by 'doing less harm' you stimulate divestment (push).

Targets, criteria, data and measurement

- ESG investors should not only look at *impacts* on biodiversity, but also at how to know / measure the *dependence* of a company of natural capital.
- How transparent are *indices* and do they really work? Do companies adapt to it? They are based on the company policy and do not look at the actual implementation and results.
- Formulate *pro-biodiversity targets* in impact investing
- *Models* do not fit investments in biodiversity with regard to risks, time frame, size etc.
- There is a lot of *data* available to set goals.
- Avoid an unnecessary and complex measurement culture by to much focus on monitoring policies of financial institutions.
- Use *criteria* that have causality with natural capital, such as CO2, water, land use and pollution.
- GIIN (Global Impact Investing Network) is working on with *measurement methods*.

Awareness

- Increasing awareness is necessary at *asset owners*. They do the job and should be more involved.
- The demand for sustainability among *consumers* is increasing. What does natural capital mean for them?

Knowledge return and risk

- On what *scale* can you invest and generate *impact*?
- What is known on *risks* and *returns* of investments in companies that deal with their dependence and impact on natural capital compared with "index investments".
- It is difficult to act on *impact investing*; what are the risks and returns? And short-term liabilities and long-term results?
- *Climate risks* are not in the models. The appropriate language, correlations and examples are needed.
- Should risks related to natural capital / climate be reported as *systemic risks*?

Context / system aspects

- 15 years ago renewable energy was a form of impact investing. Now it is almost *mainstream investing*.
- There is a lot of *money available for sustainable investment*. Investors (including wealthy families) don't find their values reflected in current portfolios and ask for more sustainable investments.
- The role of *regulators* is crucial. Members of CoP FiNC want a dialogue with DNB (institutional investors) and AFM (consumer products) in order to adapt the system.
- More *collaboration* and knowledge sharing is needed.