

Thoughts from the sustainable investing team

Why is biodiversity important for investors?

For thousands of years, our economies have been organised around the extraction of raw, natural resources from the environment to then sell for a profit. We retrieve these resources from nature and have developed sophisticated techniques to cost up the end products, but not put a price on the processes that exist to allow us to retrieve the key components.

In July 2021, the World Bank estimated that biodiversity loss as a result of over exploitation and climate change would cost us \$2.7 trillion worth of decline in GDP¹ each year. This would make biodiversity loss comparable with COVID-19 in terms of the financial risk posed to society. We are seeing a shift by certain stakeholders from traditional capitalism to a system which rewards long term value creation which is inclusive of nature.

How can we begin tackling biodiversity?

In order to understand the risks and opportunities biodiversity has, investors and companies need to start mapping the dependencies that supply chains have on nature. This includes how changes in water supply, soil quality and deforestation will impact the ability of nature to provide for those supply chains. Going forward, companies will need to look beyond measuring impacts and dependencies on nature and start working towards science-based targets for how much they will contribute to restoring forests, soils, and freshwater systems.

Moving towards circular business models and products, such as constructing buildings that absorb pollutants or investments to protect mangroves for flood prevention, will be key to transforming the economy. The United Nations has called for investments in nature-based solutions to triple by 2030 and increase to around USD \$133 billion by 2050² for the world to meet these climate and nature targets. This funding gap demonstrates the size of the challenge, but also the scope for tremendous opportunity.

Biodiversity in our portfolios

From an investment perspective, biodiversity is incredibly difficult to analyse, due to the interconnectivity of ecosystems and their dependencies. At present, businesses don't tend to measure their direct impact on biodiversity, resulting in limited data sets and a prominent gulf between how scientists measure species abundance and investor metrics. We use the LGT Wealth Management's internal proprietary sustainable data tool to review a series of biodiversity indicators that help us understand the risks businesses can face. The associated risks pose as a consequence of biodiversity loss, but also how businesses are contributing to that loss themselves. The tool considers biodiversity through a company's exposure to biodiversity hotspots and land use risk within the environmental pillar of the ESG assessment. This exposure covers the adverse biodiversity impact of the company by measuring the number of lost/reduced species from business operations, as well as any land devaluation and contamination. The extent to which a company's operations are in regions that have fragile ecosystems, and how likely these operations are to degrade them further is also measured. Our tool reviews inputs like water usage and water stress, as well as exposure to plastics and packaging waste.

A long-term game

Novozymes, a company held in the sustainable portfolios, has created a biological solution of microbes and enzymes that are naturally occurring in the earth to increase crop yield and improve soil quality. These practices allow us to begin measuring hectares of land restored and in time will help us measure the number of species preserved due to these more natural methods.

As the green thumbs and avid gardeners amongst you will know, the difficulty with improving nature is that it's a long-term game. Seed-raised wisteria can take up to 20 years to flower, and apple trees are often planted with the next generation in mind. To us, investing should be viewed in the same way. Biodiversity is something we should all look to conserve and preserve for the long term, investing in business that consider the health of our planet is one way of ensuring it will be there for future generations.

¹ <https://openknowledge.worldbank.org/handle/10986/35882>

² <https://www.unep.org/resources/state-finance-nature#:~:text=This%20year's%20report%20calls%20for,2050%20from%20the%20current%20level>

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