

# Seeing the wood for the trees

Nature has become a critical issue for investment, with topics like climate change, biodiversity, natural capital and the Taskforce on Climate-related Financial Disclosures (TCFD) and Taskforce on Nature-related Financial Disclosures (TNFD) frameworks filling up meeting agendas and being discussed at conferences. But how do all these nature-related topics fit together? And what are the key things asset owners should know and do?

## Nature – three perspectives

Nature can have an impact on asset portfolios and asset owners via:



### Nature-related issues

influencing ESG aims and creating risks and opportunities.



### Nature-related guidance and regulation

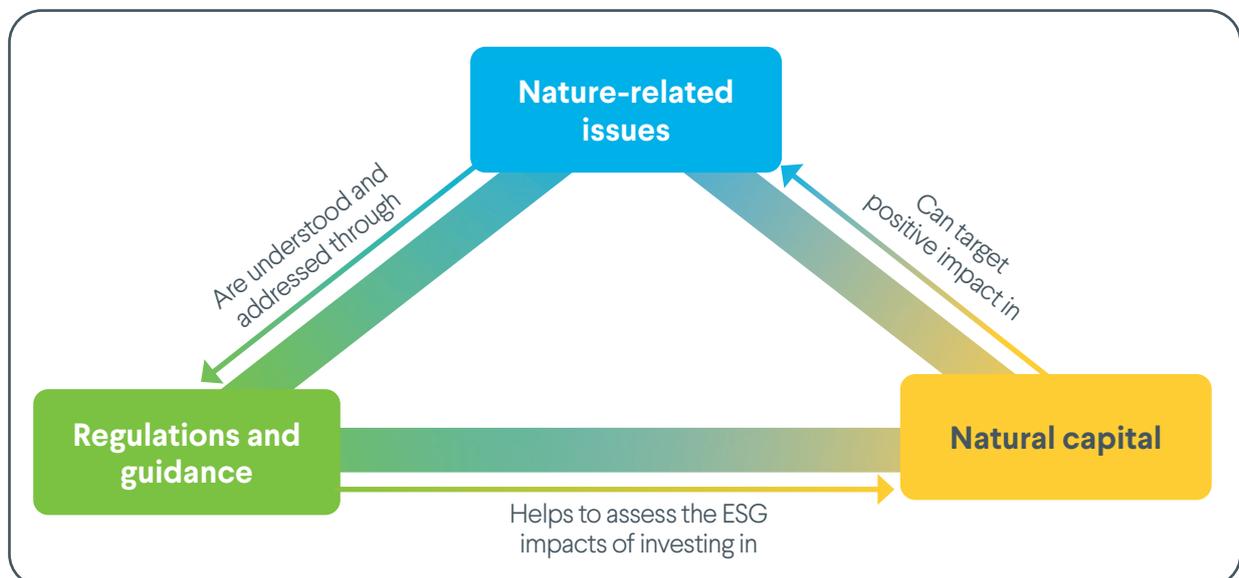
placing requirements on asset owners to report/act.



### Nature-related investments

investment in **'natural capital'**.

## How do they all fit together?





# Nature-related issues

Our economic system currently depletes natural resources while producing waste at an unsustainable rate. As we remove and damage natural assets without taking steps to preserve, protect or regenerate them, we jeopardise the benefits nature provides, creating global problems. Climate change and biodiversity loss are two nature-related systemic risks faced by our environment and society (and, as a consequence, our economic and financial systems).

## Climate change

To achieve the Paris Agreement<sup>1</sup> target of limiting warming to below 2 degrees above pre-industrial levels, we'll have to reach net zero by 2050 (a position of balance where greenhouse gas emissions match those removed from the atmosphere by natural or man-made processes) and produce net negative emissions thereafter. This transition must address the social needs of all – ie we need a 'just transition'.

## Biodiversity loss

Biodiversity is the variety and variability of life on Earth, measured at the genetic, species and ecosystem levels. Since 1970, there has been an average 69% decline in the populations of mammals, birds, fish, reptiles and amphibians<sup>2</sup> – an irreversible loss. Recognising the importance of halting nature loss, over 190 countries committed to ambitious targets under the Global Biodiversity Framework<sup>3</sup> in December 2022.

### Biodiversity and climate change are intrinsically linked

As well as providing food and clean water, natural ecosystems regulate the chemistry of our atmosphere. Oceans and forests each capture around a quarter of global greenhouse gas emissions from human activities. Biodiversity is our first line of defence against climate change – there's no route to net zero without prioritising it.

#### Climate change amplifies biodiversity loss

Existing habitats are disrupted by temperature changes, extreme weather events, rising sea levels and ocean acidification. ▶

#### Interrelated and compounding crises

#### Biodiversity loss amplifies climate change

Decreased carbon storage (deforestation releases greenhouse gases) and sequestration (pesticide use reduces soil health). Reduced resilience (eg loss of mangroves increases flood risk). ◀

## Why should asset owners care about these issues?



### They create risks

the change to a lower-carbon, nature-focused economy can create both physical and transition-related risks for asset portfolios.



### They create investment opportunities

investing in areas supporting the transition can bring strong returns in diversifying investments.



### They impact the environment and society we live in

asset owners can use their investments to make **positive impact**.

Understanding and measuring these risks and opportunities links to nature-related

**regulation and guidance**

**Natural capital**

is one of these opportunities



# Regulations and guidance

In response to these issues, regulation and guidance around nature is increasing, aiming to drive positive real-world change through:

- Increasing disclosure by companies and asset owners to encourage consideration of risks and opportunities.
- Forcing action in areas where change is essential.

## Two key disclosure frameworks impacting asset owners

### TCFD

The Taskforce on Climate-related Financial Disclosures Framework<sup>4</sup> includes recommendations for improved transparency by companies, asset managers, asset owners, banks and insurance companies with respect to how **climate-related risks and opportunities** are identified and managed.

In recent years, TCFD regulation came into place, requiring asset owners to measure and report on emissions and the climate-related risks and opportunities associated with their investments.

**There is a regulatory requirement for some asset owners to report against TCFD.**

### TNFD

The Taskforce on Nature-related Financial Disclosures<sup>5</sup> formally launched its framework and final recommendations in September 2023. This complements TCFD, setting out a risk management and disclosure framework for companies and organisations to identify, assess and disclose their nature-related issues. The TNFD's suggested approach is to identify where companies and institutions interact with nature then evaluate their **dependencies and impacts** on natural capital. This allows organisations and investors to assess **nature-related risks and opportunities**.

See our [Introduction to TNFD](#) for more details.

**Although TNFD reporting isn't yet a regulatory requirement, it's expected to become mandatory.**

The structures of TCFD and TNFD mirror each other with recommended disclosures across four pillars of governance, strategy, risk management, and metrics and targets.

**Taking a consistent approach across sustainability reporting frameworks will support integrated disclosures covering both climate and nature, such as the standards set by the ISSB<sup>6</sup> and GRI.<sup>7</sup>**

### Other regulations

Other recent regulation, particularly in Europe, will also have a direct impact on companies, asset owners and portfolios. For example:

- Common EU sustainability reporting directive
- EU regulation to limit global deforestation
- UK regulation to limit biodiversity loss

**Regulations like those aiming to limit deforestation and biodiversity loss place direct requirements on companies to tackle these issues. Nature risk is moving up the regulatory agenda, and investors must understand the latest developments to assess the impact on their asset portfolios.**



# Natural capital investment

Natural capital represents the physical assets and processes of the natural environment. This includes renewable (trees, plants, wildlife) and non-renewable (fossil fuels, minerals, water) resources as well as ecosystems like forests, oceans, wetlands and grassland. These ecosystems also provide us with services such as the provision of raw materials, carbon storage, flood control, and recreation. These benefit people and the economy by sustaining life, livelihoods and wellbeing.

## Why invest – three key drivers

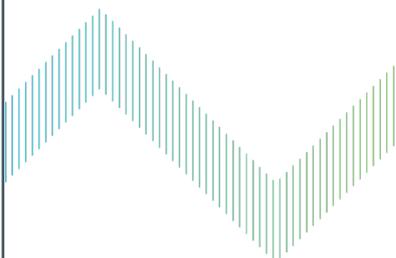
The increasing global focus on the importance of natural capital presents opportunities for investors. This includes investment in assets that contribute to the direct or indirect preservation of natural capital, or which derive returns from nature-based services.

### Return potential

- **Increased demand for sustainably managed natural capital assets and products** – as populations grow, natural resource remains finite and focus increases on the role of renewable resources like timber in the long-term transition to a low carbon economy.
- **Additional return sources** – from the growth in carbon markets and the potential future development of biodiversity markets.

### Risk management

- **Diversification** – through low correlation with traditional assets.
- **Link to inflation** – as products made from natural resources are key inputs to inflation calculations.



### ESG/impact goals

- Many natural capital investments aim to create measurable, positive environmental outcomes. Asset owners may look to natural capital as one of the ways to make progress towards their specific sustainability aims.

Linked to **nature-related issues**

## How to invest

‘Natural capital investing’ is a theme that sits across traditional and private asset classes. There’s a broad range of investment funds that could be categorised as natural capital investments – from listed equity and debt strategies to illiquid assets such as timberland. Some options are more established, with long track records, while others are newly emerging and may require some years before offering sufficient scale for meaningful institutional investment.

We’ve grouped the opportunities into three categories:



**Investing directly in natural capital assets** – eg timberland or farmland.



**Financial credits based on regulating (and other ecosystem) services**, such as carbon credits or biodiversity net gain credits.



**Technology supporting natural capital** – or into businesses looking to support ecosystem services. For example, providing debt or equity to a company focused on developing a new fertiliser or delivering a clean-water project.

**Natural capital investment strategies will be built from a combination of these three areas.**

# What can asset owners do?

<p><b>Education - Training on</b></p> <p><b>Nature-related issues</b></p> <ul style="list-style-type: none"> <li>• Climate change, biodiversity and potential impacts on asset portfolios.</li> <li>• 'Impact investing' and how to set focus areas for making impact within asset portfolios.</li> </ul> <p><b>Guidance and regulations</b></p> <ul style="list-style-type: none"> <li>• The requirements of both TCFD and TNFD.</li> <li>• Other relevant regulations that may impact companies and, in turn, asset portfolios.</li> </ul> <p><b>Natural Capital</b></p> <ul style="list-style-type: none"> <li>• Types of natural capital assets, expected risks, returns, and practicalities of investing.</li> <li>• Questions to ask 'natural capital' managers to ensure risks and opportunities are fully understood and useful data is provided.</li> </ul>	<p><b>Engagement</b></p> <p><b>Nature-related issues</b></p> <ul style="list-style-type: none"> <li>• Agree engagement themes – focusing on areas of highest risk/where assets owners want to make positive impact.</li> <li>• Engagement with managers to understand how they're incorporating these risks and opportunities.</li> </ul> <p><b>Guidance and regulations</b></p> <ul style="list-style-type: none"> <li>• Engagement with managers to understand their ability to provide data and reporting in line with these frameworks.</li> </ul>
<p><b>Reporting</b></p> <p><b>Guidance and regulations</b></p> <ul style="list-style-type: none"> <li>• Produce TCFD reporting in line with regulatory requirements.</li> <li>• Begin to include some elements of TNFD in TCFD reports.</li> </ul>	<p><b>Monitoring</b></p> <p><b>Nature-related issues</b></p> <p><b>Guidance and regulations</b></p> <ul style="list-style-type: none"> <li>• Understand the options and choose a set of metrics to monitor climate and biodiversity risk that are aligned to the frameworks and key ESG areas of focus.</li> <li>• Consider setting targets against some of these metrics.</li> <li>• Set out clear action plans for working towards these targets (eg Climate Transition Action Plans).</li> </ul>
<p><b>Strategy</b></p> <p><b>Nature-related issues</b>   <b>Guidance and regulations</b></p> <ul style="list-style-type: none"> <li>• Assess current strategy to identify key areas of risk and opportunity.</li> </ul> <p><b>Natural Capital</b></p> <ul style="list-style-type: none"> <li>• Assess whether an allocation to natural capital could be beneficial to return, risk reduction, or a means of implementing specific ESG or impact targets.</li> <li>• Assess which types of natural capital assets would be best suited to your asset portfolio.</li> </ul>	

## Contact us

We have the skills and resource available to support you in all of these essential areas. Please get in touch if you'd like to discuss how our consultants can help you address nature and natural capital issues in your asset portfolio.

[Get in touch](#)



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## References

<sup>1</sup> [Paris Agreement](#)

<sup>2</sup> [WWF Living Plant Report 2022](#)

<sup>3</sup> [Kunming-Montreal Global Biodiversity Framework](#)

<sup>4</sup> [Task Force on Climate-Related Financial Disclosures | TCFD](#) ([fsb-tcfd.org](https://fsb-tcfd.org))

<sup>5</sup> [The Taskforce on Nature-related Financial Disclosures \(tnfd.global\)](#)

<sup>6</sup> The [International Sustainability Standards Board](#) aims to harmonise sustainability standards

<sup>7</sup> The [Global Reporting Initiative](#) helps organizations understand and communicate their impacts

## Important information

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