Biodiversity: the next big focus for investors

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There is no denying that natural capital – renewable and non-renewable natural resources like plants, animals, soils, minerals, and water from which humans derive a wide variety of services – is critical to our economic wellbeing. According to the World Economic Forum, more than half of the world's GDP (USD 44 trillion) is moderately or highly dependent on nature and its services.[1] But we are exhausting the resource that is 'nature' at an unsustainable rate. In an especially troubling finding, the Dasgupta Review found that the 'stock of natural capital per person declined by nearly 40% between 1992 and 2014'. Further, the Review states that the demands we put on nature far exceed its capacity to supply us with goods and services, estimating that we would require 1.6 Earths to maintain the current world's living standards.[2]

At the heart of natural capital is biodiversity, defined as the variability among living organisms from all sources including terrestrial, marine, and other aquatic ecosystems and the ecological complexes of which they are a part; this includes diversity within species, between species and of ecosystem.[3] It represents the *living* portion of natural capital. Historically, an individual company's behavior with respect to biodiversity preservation or destruction was simply seen as a reputational issue --a gold star or a black eye, noted only by 'green' investors. However, it is increasingly obvious that biodiversity loss has serious financial knock-on effects for companies in the form of missing or more costly raw materials, supply chain interruptions, reduced crop yields, and even ecological system collapse and political unrest. Further, the 'diversity' in 'biodiversity' makes ecosystems more resilient in the face of shocks, even those related to climate change. The ability of mangroves to protect communities from storm surge, or peat bogs to act as effective carbon sinks are good examples of complex living systems adding to resiliency. We are just now at the beginning of efforts to properly value biodiversity.

There has been considerable focus on finite and *inanimate* resources like fossil fuels and minerals in recent years – both with respect to their depletion and the consequences of their use. The existential threat posed by climate change has merited the all-hands-on-deck approach that we see presently! Until recently, there has been far less effort put into understanding and valuing our living world. Thankfully, we see investors starting to awaken to the risks of ignoring the biodiversity crisis, and the potential for positive impact by adopting strategies that seek to bring solutions. In a recent survey done by Credit Suisse and Responsible Investor (RI)[4] of 327 institutional investors from 35 countries, 55% said that they believe that biodiversity loss needs to be addressed in the next 24 months, with 67% addressing it 'to some extent' in their portfolios (most often through engagement and negative screens). Standards

[1] World Economic Forum, *Nature Risk Rising*, 2020
[2] Dasgupta reference here
[3] Convention on Biological Diversity, 1992
[4] Credit Suisse and Responsible Investor Research, *Unearthing Investor Action on Biodiversity*, 2020

setters are also starting to get on board in earnest. For example, in September 2020, the Task Force on Nature-related Financial Disclosure (TNFD) working group was launched – inspired by the TCFD's efforts on climate, this organization is made up of investors, government bodies, regulators, and other stakeholders who will work toward creating a framework to assess and report on nature-related risks and impact, improving data and metrics for investors.

Much like climate risk, biodiversity risk is more acute for some industries than others. Viewed from the perspective of *dependence*, companies in the agriculture, food/beverage, apparel/textiles, and pharma industries face outsized risks. From the perspective of *impact*, agriculture, mining, transport, and energy have all done considerable harm to biodiversity. The financial sector is also at risk with respect to its indirect dependence (via clients), but its impact on biodiversity may be positive or negative, depending on what is funded or insured. The industries that are at greatest direct risk from biodiversity loss will experience intense pressure to evolve their practices if they are to survive (á la what we are witnessing now with respect to the biggest CO_2 emitters). And those with indirect exposure will need to think carefully about their dependencies if they are to remain competitive. Importantly, there will be opportunities for companies willing to step forward with nature-positive solutions -- witness the dramatic rise of meat alternatives.

In sum, we see 'biodiversity' as occupying the same space as 'climate' did five, or even ten years ago. A large swath of investors, lenders and insurers, government institutions, NGOs, regulators, and standards setters have woken up to the fact that biodiversity underlies our economy in ways that many never stopped to imagine. We can model our approach to biodiversity on our approach to climate, leveraging lessons learned including the economic benefit of immediate action. For investors, the takeaway is clear: biodiversity should be our next big focus. As we have seen with 'climate', companies that lead on biodiversity should have an advantage relative to their peers, given the overwhelming importance of biodiversity to the existence of companies, our economy, and ourselves.

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