PENSIONS FOR PURPOSE PODCAST
Biodiversity and Natural Capital with Martin Belcher – Season 3 Episode 2

Laasya Shekaran, Pensions for Purpose: Hello everyone, and welcome back to the Pensions for Purpose Podcast. I'm your host, Laasya Shekaran, and today we're going to be talking all about Biodiversity & Natural Capital, which is one of our six Ecosystem Themes that we focus on at Pensions for Purpose. We have a whole program of work around this Theme, which includes events, research, Community Interest Groups and policy advocacy.

To support us in all of this work, we have partnered with Palladium. We have lots of interesting work planned with them, and we're kicking this all off with a soon-to-be-launched research project. So, for today's episode of the podcast, I'm absolutely delighted to be joined by Martin Belcher from Palladium. Martin, welcome to the podcast.

Martin Belcher: Good morning.

Laasya Shekaran, Pensions for Purpose: Let's get straight into it, and find out a bit more about Palladium, and why you decided to partner with us on our Biodiversity & Natural Capital Theme.

Martin Belcher: Palladium's a mid-sized, global company. We've got between 3,000 and 4,000 employees, and I think about 300 of those are based in the UK. It's a bit of a strange beast. It's quite complicated, but I think probably everyone says that about the companies that they work for. It is a positive impact company, so it's private sector, it's a profit-seeking company, but it's positive impact, and it's been that way for a long time. It has its background in international development project delivery. So, working in, low- and middle-income countries to develop different parts of the economy, the health sector, education sector, natural capital sector, etc. When I say it's a positive impact, it's basically the intentional creation of enduring social, environmental and economic value. Our clients are governments, businesses and investors, and I work around climate, environment and natural capital. So, we're involved in projects with all of those client types, so governments, businesses and investors, to develop and deliver climate, environmental, natural capital impact and investment opportunities in return.

That's the day-to-day work. And why collaborate with Pensions for Purpose? Well, the strategy and mission objectives of Pension for Purpose is very much aligned with some of the work that I'm directly involved in, and my colleagues and stuff as well. The positive impact of Palladium and the objectives that Pensions for Purpose is trying to achieve are very similar, in a way. So, I think, why collaborate? I would say there's a number of different reasons. First of all, there's some project-level drivers. I tend to work on projects. A couple of key ones. There's one with the FMO, which is the Dutch Development Finance Bank, and it's mobilising finance for forests. I'm involved in that to help scale private sector investment into forests and sustainable land use. Obviously, the ecosystem work that you're doing around nature and biodiversity really overlaps with that. That project, and my role in that, is really just to scale investments across the private sector by taking lessons and opportunities from that programme, which is a blended finance initiative run by the development bank, the Dutch Development Bank, and it's supported by the Dutch and British governments.

There's another project I'm involved in called Partnerships for Forests, and this is funded by the UK government. It's basically providing incubation, business incubation services to businesses across the tropical forest belt.

I've been working in that area for, well, just over 10 years now, and one of the key things is there's lots of businesses out there, there's lots of entrepreneurs out there, there's lots of people trying to deliver impact and, you know, financial returns, but there's a scarcity of investment.

I continue to work in that area, and I'm really keen to see more private sector investment flow into those opportunities to deliver positive impact that we're all trying to see, perhaps. Then, that all aligns with Palladium's strategic drivers, so that's why Palladium is involved. Also, my personal beliefs, like lots of people listening to this podcast – like yourself, like my colleagues, your colleagues – we're worried about the future. What does the nature of biodiversity crisis, climate change, all of these things. Delivering investment into nature and biodiversity, I think, is one way of trying to de-risk the future. There's lots of uncertainty, there's lots of terrible predictions that are coming true. So, how can we actually, mitigate those changes and those negative impacts, and look for positive, investment, and environmental and social impact returns?

That's the background, and we thought that Pensions for Purpose offer a really good network, and an opportunity to engage directly with asset owners and asset managers who are also interested, and maybe don't know as much as they would like to, perhaps, or want to get more involved. Also, looking at the opportunities for nature and biodiversity. So, it's a good opportunity for strategic and practical alignment.

Laasya Shekaran, Pensions for Purpose: Yeah, absolutely. There's so much alignment with what we both want to do with our missions, but also, it's so useful for our members to be able to learn from practical examples. Where people have done nature investments, they have worked with private capital in the past, and I think what's really important is how you approach about the enduring creation of these different types of value, because our members are long-term investors, they're often universal owners, so it's really important we think about the these things over longer-term time horizons. If we're looking a bit more about the practical side of this, what actually makes a good nature investment?

Martin Belcher: Yeah, good question. I think it's high-level. We need to treat nature as an asset that generates returns, but obviously, there are different kinds of returns – but first and foremost, it's got to generate financial returns. Otherwise, it's not really going to be sustainable, it's not going to be investable, and the sector isn't going to deliver the impact, either financial, environmental or social, that we want it to. So, basically, operational cashflows need to be there, yeah, so that is a nature asset, a key component of nature assets. They also need to deliver impact, so financial returns, environmental and social impact. Now, those can be different depending on what the particular investment opportunity is you're looking at, but basically, we need to see positive environmental impacts.

So, is nature degradation being slowed or stopped or reversed? Often, things like social impacts could be enhanced livelihoods, it could be resilience, it could be income security, but it could also be things like voice and participation, and representation as well. So there's a whole host of aspects to the asset and how it generates those returns. I think you could say, more traditional assets, operational cashflows, we need to see those. Yeah, where do those come from? Cost savings and efficiency might be a part of it, because well-managed nature has significant impacts in those regards as well as resilience. So, in climate change, in a changing world, depending on what sector and what context you're operating in, the effects of that change can be significant and negative.

So, actually, can we mitigate those by different interventions? Those might lead through to cost savings, efficiency gains, resilience and reliability of supply, etc. We're looking for some of that, and there might also be asset appreciation. A big challenge with nature and areas around natural resources is degradation. We probably are aware from listening to the news, reading newspapers, seeing things online, climate change is leading to agricultural productivity falls, it's leading to flooding, heat stress, all of these things. Actually, that is undermining asset values. So if you've got assets that are linked better to nature and they're managed in a sustainable way, they could be regenerative. Then you can actually have asset appreciation and avoid some of those negative stranded assets, depreciation, degradation, etc.

Then, there's also strategic benefits, yeah, so that might be around, like, environmental, social and governance (ESG) alignment, climate resilience, reputational gains and also, I think a lot of the public members, pension fund members, and what they want to see in the future, so it can be delivering returns from them that they value highly. Of course, they're going to want their pension, they're not going to want declines in that, but they might want to see positive nature biodiversity impacts as well.

Laasya Shekaran, Pensions for Purpose: Yeah, people can't really do much with their pension if there's no clean air to breathe, or food to eat, or water to drink, so I think that's always part of it, too. There is a lot to think about there when it comes to a good nature investment, in terms of the financial side of things, but also impact.

Can we bring it to life a bit and talk about some practical examples of this, because you have lots of experience doing this in practice? Perhaps you can talk us through some different types of investments that you've seen, and how they work from both a financial and an impact perspective?

Martin Belcher: Yeah, sure. There's different types of categories – it's a bit like saying, if we were going to have a discussion about investing in stocks, it's huge, there's different markets, there's different types, all of this stuff. So, nature is hugely complex, but there are some sort of investment types that we could usefully go over, and then provide some examples. So we've got more simple things, not necessarily simple, but some of the more easy-to-understand mainstream things might be things around sustainable forestry, restoration, conservation, forests, trees, those kinds of things. There could be other very important things like regenerative agriculture, like agroforestry, so shifting from monoculture production to agroforestry production with shade trees, etc.

Those are very important for nature and biodiversity. There's also an important difference between terrestrial, ie. the stuff that they're doing on the ground in forests and agricultural systems and aquatic, oceans and blue carbon, but they could also be brilliant. opportunities as well, fish farming, those kinds of things, but oceans and blue carbon are really important. I know a bit about those. I'm not an expert by any means.

There's also really important things like wetlands restoration. So, say in the UK, there's a lot of peat, and there's a lot of heavily degraded peatlands, so they're not so wet anymore, but there's also tropical areas, like mangroves, which in many places, have been degraded or ripped out for development purposes, but those wetlands restorations offer real significant nature impacts, biodiversity impacts. There's things like payment for ecosystem services. The most well-known is obviously going to be carbon, paying for carbon that's delivered from, say, a restored forest, or avoided deforestation, but there are other kinds of payments for ecosystem services as well, so there could be biodiversity credits, there could be water management, those things.

Then, there's things like flood and drought resilience. Maybe some urban things, like flood and water management, but also heat management.

I'm sure we've all experienced it in the last years and summers. If you live in an urban environment, it can be unmanageably hot at times. That's got significant impacts for the UK, but places all over the world. If you look at the maps that have been prepared for that, based on really reliable, hard evidence, it's going to get hotter, so how can you manage that in the urban environment, because urban environments aren't going to go away? In fact, they're going to get increasingly dense as well. So, those investable categories in those areas in terms of the financial instruments.

The mainstream ones can be equity, it can be debt, it can be blended finance, first loss capital, guarantees, concessional capital, all those things. I think one of the key things, often, is because nature, in some areas, as an investment sector is less mature. I think things like forestry and timber are super mature, hundreds of years of experience for those, but some of the other stuff that I mentioned – payment for ecosystem services balloon carbon, things like that – they're much more immature. So, there is often a need for better technical level, technical assistance, technical understanding, and that's what I've spent a lot of my time over the last 10-15 years providing. I think that's an important part of the investment ecosystem, that there are emerging a pleasantly large number of specialist fund managers, who can specialise in one or more of these nature-based investment types. So, that's an important thing as well. Would you like to maybe look at a couple of practical examples?

Laasya Shekaran, Pensions for Purpose: That'd be great, let's get into it.

Martin Belcher: I'll give a couple of examples, then. One of the big things about nature is where are we going to invest in nature and biodiversity? There's often a big split is this an emerging markets issue, or something that I can do in my county, or in the north of England, or in the southwest, or is it something that is particularly important if you're looking at forests in Canada? Obviously, you can get nature, and you can get nature and biodiversity investments in all of those places.

For emerging markets, a couple of examples. What I'll try and do is give an example, let's say, maybe more mainstream, and another example that's maybe newer, more innovative. We were doing some work that started over 10 years ago with sustainable rubber production in Indonesia. A lot of rubber is produced in tropical forest belts, and there's an increasing demand for natural rubber, so where's this natural rubber coming from? There's a mixture of established plantations, there's quite a number of degraded plantations and there's natural rubber harvesting: people going into the forest, tapping rubber trees, and bringing that out. So, this was a project working with a big multinational who wanted to secure sustainable rubber supply for environmental reasons, but also bottom-line business operational reasons. They wanted rubber, they wanted to manage it, their business is rubber, so they can't have any risks in supply.

So, working through a green bond and debt financing on what I would say is quite significant sale, around 100,000 hectares, to basically create and expand a rubber plantation. I know that sounds like not very nature, that sounds like plantation, what's going on there? Well, if you do that in the right way, so some of the area is a degraded concession; the way land is managed in Indonesia is through concessions, or largely managed food concessions. Degraded area forests had already been unsustainably locked, turning it into a rubber plantation, but earmarking areas that were important for biodiversity, wildlife corridors and restoring those.

So, you can actually have restoration and a sustainable supply chain with good security and resilience, into a standing multinational corporate supply chain that delivered jobs, tens of thousands of jobs, a large area of sustainable production, and restoration and conservation. That's one example.

Another example, which comes from Colombia. This is a innovative new business, it was equity and debt financing. Basically, natural blue dye. I didn't know this before I came across this, working with this business, but blue dyes are basically all artificial, because blue doesn't – for various reasons, I don't quite understand – but blue dyes degrade, they can't be processed, industrially. But anyway, there are some berries that grow in tropical forests, in parts of the Amazon in Colombia, that have particular qualities that make them suitable for industrial production methods that are blue, and it's blue and it's natural, it's not artificial. It was also interesting, because it was painting the ball about the processing and all of this. So, investing in that company. It's a relatively small area of production, but a mixture of orchard-type production, and natural harvesting and agroforestry systems, so you can add value to standing forests, you can add value to sustainable production and you can represent real growth opportunities.

A couple of other examples. Let's think about timber – that's like a gateway drug for nature investing. So, it's probably the easiest thing to invest in in nature, because, as I said earlier, it's got hundreds of years as an investment sector track record, so timber is well established – but there's different places to invest in timber. You could invest in a timber plantation in Scotland, or you could invest in a timber plantation in Brazil, West Africa, or wherever. Now, there are different opportunities. So, there's some very interesting models happening at the moment, where you've got, basically, timber being put onto degraded pasture lands in Brazil. I've got places like that, so in Latin America in particular, where, rather than just put plantation over everything, which isn't going to give you much biodiversity benefit, really, you put it over 50%. Some people choose 40%, some 50%, but the ones that I'm really interested in, that have really been successful in the market at the moment, are basically 50% natural restoration.

So, put the forest back naturally, plan where you put it, so you can create wildlife corridors, again concentrations around water causes, and turn those degraded pastures, which were once forest, back to natural forests – half of it to plantation forests for production, all of the economic, job creation and wealth creation opportunities that that represents. Now, we've seen that, as I say, is really successful in Latin America.

There has also been some interesting stuff in West Africa, where your more traditional teak plantation type things are, but can you do that in a more socially impactful way? Yes, you can, in the right circumstances. You can engage the communities. You can allow them to come in and do intercropping within the plantation to provide income opportunities. You can use job creation for the timber, but there are other side businesses as well. You've got carbon credits in there as well. You can work with those communities to do things like by their engagement, by them getting returns and fire risk management. So, that's the key. That's one of the real risks for, timber plantations, timber assets – what happens if they all catch on fire? You don't want that. So, can you get the local communities involved? Yes, you can. So, you can then produce much more sustainable, much more socially impactful, as well as areas of restoration, with areas that aren't timber production, they're actually for forest restoration, and in a blended mosaic landscape. Still with a key emphasis on timber, it must be said, but you've got a real opportunity for growth there, because of the booming economies, the growing populations, etc, and the need for timber to support those aspects of society.

Finally, maybe I'll give you a couple of examples, say, from the UK. So, it's also possible there to invest in nature and biodiversity. One thing I would say is, if you're investing in payment ecosystem services in tropical environments, they tend to come on tap much more rapidly, because things like trees grow much quicker, all plants grow much quicker. The breadth of biodiversity in the Amazon is well known. The breadth of biodiversity, equally important, but smaller in, say Yorkshire – but I'm not saying it's not as important, it's super important, but these are different things.

So, depending on what timeframes you're looking at, depending on what your impact objectives, your investment objectives, returns, expectations are, etc, the UK can be great. So, there are a number of impact funds that specialise in nature restoration projects. So, that could be things like creating woodlands, or restoring woodlands or wetlands. I mentioned peat earlier – that's really important. The carbon impact opportunities for restored peat is significant, and there's a lot of degraded peatlands all over the UK. You've got flood meadows. These are important for water course management to alleviate flooding. There's some well-known – well, maybe it's a bit specialist, but there's some opportunities in places, say, like the Somerset levels. You look at the hills that are around the Somerset levels, there's very few trees, and they've all been deforested over many hundreds of years, if not thousands, but if you can put trees back in places like that, then you can help manage the water flows when it does rain.

We've also seen increasingly heavy rain through climate change that can help you manage the water flows and the flooding risk, and the opportunities for investment returns there for water companies. One of the few good things water companies might have been in the news for in the last few years is that they have been making investments into natural restoration and flood management and they've got some biodiversity net gain. That's the UK's legal requirement, to have an uplift in biodiversity of increasing damage in that case and to repair it in another place. So, there are those opportunities in the UK, and there are other things. I've seen some really interesting cases, things like oyster beds, where they're planting oyster beds in the marine coastal environment. There are environmental benefits, so that actually you've got much cleaner water, filtered water, but you've also got economic benefits as well, if these things are being done with harvesting in mind, with niche in mind, with shellfish, etc, as well as the natural restoration. So there's a whole load of opportunities all over the world. We're spoilt for choice if we know where to look.

Laasya Shekaran, Pensions for Purpose: That's brilliant. It's clear from that that there's just such a breadth of opportunities available, and depending on what your geographic objectives, or your impact objectives are, you can probably find something that fits what you need, which is definitely very exciting.

So, you've been doing some research with us, finding out a bit more about how asset owners are actually thinking about this and how far along they are in their journeys, when it comes to nature-based investing. What were some of the key findings from this research that we could maybe tease to our audience?

Martin Belcher: Yeah, sure. The Pension for Purpose team have been doing some great research work on this, and they've been interviewing 15 asset owners and five asset managers. It's quite a nice sample. We're still processing the findings. I think you can confirm when they'll exactly come out, but it's next month, in February. There's some very interesting findings. First up, there's the pension sector there, so the membership, where there's an interesting range of levels of experience. There's actually some really super experienced pension funds that have been investing in this sector for more than five years.

There's a large group who are looking like they’re putting their toes in the water. We've been looking over the last couple of years, and are actively looking for investments. That is really pleasing to see; that's a real positive, I think. There's a small number who are not aware, of course, but they're not active, and that's usually because of mandate or other investment decisions, that actually this isn't something we're looking at the moment.

I think the vast majority of the sector is either active, or looking to be active. I think that's really positive, because even if you had a 1% asset allocation to nature, that would be significant investment that could flow into nature and biodiversity, climate resilience, those kinds of things. So that would be great to see, and I think there's some evidence that is emerging. I think, there's a couple of other things that I think are interesting, such as many of the people we spoke to are working with specialists. There is no denying it that investing in nature, at first, looks daunting for a whole variety of reasons – we can look at those if we have time – but one of the routes is a specialist fund manager that we can trust to guide us in this, and deliver the returns on the strategy we've got, and help us think that through.

What's really interesting is the selection process, as well. So, how have the different asset owners gone about that selection process, and selected the fund managers to work with? This obviously is a critical step in the process after some of the asset owners get more experience, and they can manage those things in-house. Some can manage it in-house; because of their size, their setup or their strategy, they can manage it in-house from the beginning. Some is with fund managers, some will remain with fund managers, but some they'll bring it in-house over time. So, what is the process of identifying and working with those fund managers? I think there's some interesting findings coming out in that area.

I think a couple of other things that were really interesting from the asset owners that are active. So, they're active, and how does that align with their strategy, what is their strategy to be active in the nature-based biodiversity space? There's some really interesting thinking, and evidence they've been sharing with us, and it will be in the report around the long-term timelines of returns, and how the returns, how investing in nature helps balance risk across their wider investment portfolio. So, for instance, things like timber. If you're going to plant a tree and you want to harvest timber.

It's going to take, you know, 20 to 30 years for that to happen, and it might take longer depending on the type of timber, and depending on the geography of where you're growing it, basically. If you're looking for different types of restoration, some areas of forest or some areas of landscape can get restored pretty quickly, actually. They can get degraded very quickly, but luckily they can get restored very quickly. Some take a long time and the capital is intensive, etc, but this balance of opportunities helps these asset owners and fund managers bounce the long-term risk assessment, and their long-term return horizons that pension funds have.
It was really interesting about the usual complaint about investing in nature is.

10 years isn't long enough if you're a traditional fund setup: 10 plus one, 10 plus two, is that going to deliver returns in time? Whereas, if you're talking about a 20, a 30 or 40-year timeframe, then actually that aligns very well with nature. There are some things about different asset types within the nature space that are also very interesting, and the people we spoke to in the research, they called out some of this. I think those research findings would be really interesting for the members of Pensions for Purpose.

I'm not a specialist timber person, but they just point out things like the correlation between private markets and timber prices. It's favourable if you've got timber assets, it's favourable in private markets, but also, you don't have to chop the trees down. when there's an economic

recession in a building under pressure. You can actually leave them, and actually the asset will accrue value over that time, because the trees would get bigger, there'd be more harvest volume, etc. So there were some really interesting findings in there, as I say, from these early movers who have really got quite a lot of experience, so I think there is some facts and figures to share, but there's also the peer learning opportunity case-based results to be shared. I think leadership from some of our colleagues, who can lead if people are interested in taking a similar journey, then there's some real leaders out there who can do it, but doing it from the same contextual investment requirements, the same fiduciary expectations, requirements, etc. So, there's some really good stuff around there. There's also some learnings around the risks, how they've identified, how they've assessed those and how they manage them, because one of the common things coming up from the research was the investment decisions: yes, you're interested in investing into nature to resources being allocated. There's basically a standard journey, and you come up with the same sticking points, You can't avoid them, because the investment committee will ask about those same risks and the risk committee will need to see that risk dealt with.

So, the same journey happens, and there's ways, I think, to support people along that journey – maybe speed it up, maybe not speed it up in terms of time, but speed it up in terms of impact, so that things can operate at scale more rapidly. It's very interesting. I've seen a draft of the research, and we were actually meeting about the later in the week to look at the next situation, so I'm really excited about that coming.

Laasya Shekaran, Pensions for Purpose: Yes, absolutely. It's going to be a great piece of work, and we'll share it, of course, everywhere for our listeners to take a look at. We'll also be running our first Community Interest Group meeting for Biodiversity & Natural Capital at the end of February, so again, another great opportunity, not just to find out more about the research, but to actually, get together and do that peer-to-peer learning with other asset owners that are in the room. So, please do get involved.

It's been a really fascinating conversation. I think we've really brought to life the practicalities around a lot of this when it comes to biodiversity and nature. Sometimes it can feel very nebulous, so it's good to just go through real-world examples of how it works. If there was one thing you wanted listeners to take away from this conversation, what would it be, Martin?

Martin Belcher: I think that the one thing I'd like people to take away is investing in nature and biodiversity is important. I think that's a given. What's not less clear is how, as an asset owner, can I allocate resources into this? I think what I'd like people to take away is that there's UK pension funds, we're doing that at scale, but there's many more who could be doing it, but there's people who are doing it at scale. So, there are routes to do it, there are strategies to deliver those returns. I'm really keen on, is that working through Pensions for Purpose.
We can, basically, as a peer group, as a sector, learn from each other to drive this forward, because it does seem a bit daunting, seems a bit risky, it seems a nebulous time. There's an increasingly robust track record of our friends and colleagues, so not advocates for these things, but people who are making pension fund investment decisions on a day-to-day basis of doing that. So, I'm really keen to flag that, and flag the work that you and your colleagues would be doing to share that understanding, and hopefully we can move the whole centre field together.

Laasya Shekaran, Pensions for Purpose: Absolutely. I think you couldn't have put it better. The ability to learn from each other and work together as a community can just be so powerful. So, to all of our listeners, please do get involved with our work, and hopefully it'll be very powerful and exciting stuff.

Thank you so much for joining us today, Martin. It's been a really useful discussion, and we're really excited to be partnering with Palladium more generally. Listeners, if you want to make sure that you never miss an episode, you can hit the follow button, find us on all your podcast platforms and we'll see you on the next one.