



Beyond ESG risk integration: Impact investing

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Environmental, Social and Governance (ESG) investment is taking root within the infrastructure investment community. Infrastructure assets have the potential to bring strong social, environmental and economic benefits to society but they are also particularly exposed to ESG risks. Most investment firms active in the space have by now implemented ESG considerations in their investment process. Logically, these policies have been initially focused on ESG risk assessments. While this is an important development, the asset class offers the opportunity to go beyond risk assessment and realize its significant potential for positive impact. Interestingly, according to a recent IFC publication, private investment fund managers pursuing impact investment strategies have deployed 62% of their capital in infrastructure assets¹

That is the approach adopted at Generali Global Infrastructure (GGI). With clear ambitions to promote and lead sustainable investing in the asset class, an essential part of our role is to help investors identify and channel capital to assets that are compatible with and contribute to sustainable development. Since inception our investment philosophy has been designed to go beyond “ESG risk integration” and strive towards an impact investing approach, supported by a proprietary methodology developed by a combination of strong internal and external expertise. In addition, to place sustainability at the heart of processes and decisions, our investment team, and not only ESG experts, is involved in the extra-financial rating of investments.

Our methodology uses a holistic approach with key ESG factors captured to ensure that we select assets that contribute to sustainable development as a whole and not just to a single aspect of sustainability. For example, we would exclude renewable energy projects facing severe social or governance controversies.

Our approach to integrating impact is based on evaluating investment decisions against the UN Sustainable Development Goals (SDGs). A defining element of our understanding of sustainability is a ban on investments in sectors with potential to cause strong obstructions to the SDGs. This has notably led us to (i) exclude assets principally involving coal, oil, or unconventional fossil fuels and (ii) implement a tool capable of recognizing the contribution of investments to the SDGs (i.e. electric rail / green transportation, renewable energy, or very high speed fiber networks in rural areas have been key focuses of our investment strategy).

This position is further driven by our belief that capital should be deployed to maximize financial and extra financial performance. Ignoring this reality represents an opportunity cost to society, and a mid to long term financial risk for investors.

We are further strengthening our impact approach by supporting the development of an innovative methodology to assess our portfolio's alignment with targeted climate scenarios (i.e. 1.5°C). This tool goes beyond the measure of carbon footprint and allows to evaluate carbon impact of portfolios against the larger goals of reduction of carbon emissions established by the Paris Agreement. This will eventually guide investment decisions and, in our view, will become one of the most important impact indicators for the asset class.

With infrastructure central to global challenges, investors need to remain at the forefront of sustainability and acknowledge that ESG issues are constantly evolving, due to scientific progress and evolving regulations and public opinion. At GGI, we see biodiversity as a critical issue of growing importance. Scientists have been warning about the risks posed to biodiversity by human activity all over the planet. The IPBES (Intergovernmental Science-Policy Platform on Biodiversity and Ecosystem Services), the equivalent of the IPCC (Intergovernmental Panel on Climate Change) for biodiversity, issued a landmark new report in April 2019 describing the alarming rate at which Nature is declining globally².

The report details the causes of this decline, as well as possible ways to prevent further destruction of natural habi-

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tat. According to this body of experts, “landuse change has had the largest relative negative impact on nature since 1970”. Thus, the potential negative pressures on biodiversity of the infrastructure asset class needs to be recognized and addressed. While this is already the case to some degree - for example our starting point on this issue has been to evaluate how infrastructure assets integrated biodiversity in their planning and operations, including environmental site impact assessments (particularly on protected areas), we anticipate that more will need to be done. We expect to place increasing focus on:

- use of land, and associated compensation measures to achieve “no net loss of biodiversity”;
- climate change impact on biodiversity, and their interrelation (with global warming being a significant factor driving species extinction, and deforestation accelerating climate change).

Further integrating biodiversity within ESG strategies will perhaps be even more challenging than climate change. Whereas the exposure of portfolios to climate change can be measured with globally accepted metrics, such as carbon footprint and avoided emissions, there is no equivalent for biodiversity. This is a more localized issue, making it more difficult to adopt universal quantitative metrics to measure the destruction of biodiversity. In response to this challenge we welcome the emergence of some initiatives, such as the biodiversity footprint methodology developed by CDC (Global Biodiversity Score).

Reporting frameworks, such as the European Union’s non-financial disclosure guidelines will require the inclusion of biodiversity impact and management³. Our sector needs to prepare for this, with a view to direct capital to infrastructures minimizing negative pressures on biodiversity and to green infrastructures⁴ protecting ecosystems.

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Generali Global Infrastructure

The creation of GGI represents a cornerstone in building Generali Investments* multi-boutique platform bringing together highly-specialized investment skills and attracting capital both from Generali Group and third party investors. GGI invests through the entire debt capital structure to capture attractive relative value across a wide range of geographies and sectors.

FOOTNOTES

¹Creating Impact - The Promise of Impact Investing, April 2019.

²Summary for Policymakers of the global assessment report on biodiversity and ecosystem services of the IPBES, May 2019

³European Environment Agency, Briefing on Biodiversity

⁴https://ec.europa.eu/environment/nature/ecosystems/strategy/index_en.htm