KEYNOTE INTERVIEW

A natural fit

Nature-based solutions could offer opportunities to meet financial goals while addressing global challenges such as climate change and loss of biodiversity, says Nuveen Natural Capital's Nick Moss

According to Nick Moss, head of nature-based solutions at Nuveen Natural Capital, emerging trends are providing opportunities for investors to benefit from diversified investment strategies and exposure to maturing environmental markets while contributing to improvements in nature and reducing greenhouse emissions.

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Q How has natural capital evolved as an investment asset class in recent years?

For several decades, natural capital as an asset class has become an increasingly important part of institutional portfolios. This has traditionally included investments in timberland and farmland. Investors in the asset class have come to appreciate and value the wide range of benefits that natural capital can bring to an investment portfolio. This includes both traditional financial benefits as well as sustainability benefits.

Over the last few years there has been an evolution of the asset class, driven by the convergence of critical trends. Natural capital is increasingly recognized for its importance in being able to provide solutions to address the challenges of climate change and biodiversity loss. We have also seen increasing levels of government action, growth in environmental markets and the maturity of assets and business models which aim to tackle these challenges.

Q What do you mean by nature-based solutions?

Put simply, we define nature-based solutions, or NbS, as using natural capital to solve key environmental challenges while generating positive financial returns for investors.

Natural capital can be thought of as a stock of environmental assets – the earth's air, land and water and all their biodiversity – that yield a flow of benefits or ecosystem services over time, whether it is raw materials, water, flood protection, biodiversity or pollination. Critically, nature provides the fundamental capital base that businesses and whole economies needed for the production of goods and services.

However, the earth's stock of natural capital and the benefits they provide are declining. Globally we have seen a loss of species, habitats and ecosystems, with a commensurate decline of ecosystem services, such as the ability to maintain, absorb and regulate carbon in the atmosphere. Investing in the protection and restoration of natural capital is critical.

There are a range of technical definitions, but in its simplest terms, NbS is often defined as a set of actions that restore, manage and protect natural and modified ecosystems. For natural capital investments, such as farmland and timberland, an NbS approach allows for value recognition for more than just timber and crops, but also provides the potential to produce quantifiable ecosystem services – for example, carbon sequestration, soil health and water quality.

Increasingly, there are options to realize benefits and returns from these activities and investments. One example of this is through environmental markets such as the carbon markets, offering investors additional returns and diversification opportunities.

Q What are the trends in the market that are driving investor interest in NbS investments?

While there have been many developments in the sector over the last few years, there are a few trends of note contributing to growing interest in NbS investments.

Firstly, we have seen growing investor interest in natural capital broadly. The sector's attractiveness has been driven by certain fundamental macroeconomic trends, such as the growing demand for food, fiber and timber alongside a shrinking supply of productive land.

This has been accompanied by an increasing recognition globally of the importance of nature in supporting livelihoods and economic systems. The watershed moment really came in 2022, when the Global Biodiversity Framework was agreed upon by global governments, establishing a global target for nature restoration and funding. This has been complemented by increasing levels of government action via a range of policies, subsides and financial incentives.

Environmental markets have also grown in prominence, particularly as a tool to mobilize investment into addressing climate change and biodiversity loss. The most prominent of these has been carbon markets, which, despite recent headwinds, has seen increasing activity with large tech firms making substantial commitments to purchase high-integrity, nature-based carbon credits.

Beyond carbon markets, there has also been the growth and maturity of other environmental markets for ecosystem services, including the mitigation bank credit market in the US and the more recent biodiversity net gain market in the UK.

And finally, corporates and financial institutions are also ramping up their efforts to identify and mitigate impacts on climate and nature within their supply chains and portfolios. This is partly driven by broader sustainability trends, as well as voluntary measures including the Taskforce on Nature-related Financial Disclosures, and a growing number of regulated measures such as the Corporate Sustainability Reporting Directive.

Q Why are NbS attractive, and what are the benefits to investors?

Along with the core portfolio-level benefits of natural capital investments that come with timber and agricultural

Q What are some examples of investible NbS?

NbS encompasses a range of different approaches, not all of which are investible at scale. Our approach focuses on strategies which aim to balance returns from natural capital, including from crops, timber and land, while providing opportunities for exposure to revenue streams from existing and emerging environmental markets and delivering nature and climate benefits.

We have identified three core areas that we consider to be investable at scale: regenerative agriculture, a mixture of practices that aim to improve soil health and other ecosystem services; carbon forestry, which aims to conserve, improve and restore forests to increase carbon sequestration or avoid future emissions; and ecosystem restoration, investing in ecosystem assets that provide an ability to monetize restoration and protection through environmental markets.

crop production – such as acting as an inflation hedge, offering income and appreciation return and the asset's low volatility – we believe NbS investments can offer a range of other potential benefits for investors.

NbS assets offer positive contributions to nature and climate, opportunities for additive and diversified sources of uncorrelated returns through exposure to environmental markets, and asset-level diversification opportunities through investments in new projects or operational strategies. In addition to the financial benefits outlined, there is the potential to contribute to realizing a net-zero and nature-positive portfolio.

What's more, there are a range of other potential benefits which can be realized at an asset level. This could include access to new markets, payments for practices through price premiums or subsides, reduced operating costs from improved efficiency, or more jobs and sustainable employment opportunities.

As an example, we have recently acquired an NbS asset in Australia which will be developed as a mixed farming operation, applying regenerative practices and restoring an area of native vegetation at the site. While the crops and land provide income and appreciation, the practices have the potential to reduce costs long term and replenish the soil and other ecosystems, while the restoration activities will provide the potential to generate and sell carbon credits in the local carbon market.

"In its simplest terms, NbS is often defined as a set of actions that restore, manage and protect natural and modified ecosystems"

Q What should investors consider when looking at NbS, and what can be done to reduce the risks?

For those familiar with investing or managing agriculture and timberland assets, many of the aspects of NbS strategies are not necessarily new. The fundamentals of managing land to grow crops or timber still exist. However, NbS strategies may introduce new practices, revenue streams, markets and operational strategies, which can come with additional complexity and risks. To realize the benefits and manage these risks, investors need to consider a number of items.

Firstly, when originating and building a portfolio of NbS assets, target markets with mature natural capital and environmental market opportunities. For instance, the US has strong agricultural and timber markets as well as mature environmental markets, such as for carbon and mitigation banking. Similarly, portfolio diversification is important, including diversification of crops, species, geographies and NbS revenue streams to manage risk.

Operating and managing assets with multiple activities and return opportunities will require flexibility in operational strategies and working with a range of stakeholders and additional technical advisers. As a result, local asset management teams are crucial, working with teams that know the asset, can understand and address risks, and can identify and work with local partners.

And finally, it is important to have measurement and reporting systems to understand impacts on climate and nature, identify risks, report on progress and then adapt where needed.

Q What does the future hold for NbS?

We believe the future is bright for investments in NbS. We have seen growing investor interest driven by increasing government and corporate action, maturing markets and scalable investment opportunities.

The untapped opportunity is significant, with availability for private finance to play a critical role. According to UNEP, over $500 billion a year is needed by 2030 to restore and conserve biodiversity.

However, to earn a spot in institutional portfolios, NbS investments must also deliver competitive performance, diversification benefits, and measurable positive impacts on nature and climate.

We believe that a balanced approach to investing in NbS, drawing on the traditional benefits of natural capital, proactively contributing to improvements in nature and climate, complemented by returns from environmental markets, has the potential to deliver this ambition. ■

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