ESG – more than ecological investing

Topic of the month March 2019

by Alfonso Papa, NN Investment Partners Schweiz AG

Infrastructure projects offer higher returns combined with environmental and social benefits

Sustainable infrastructure investments are particularly attractive because they can provide investors with higher risk-adjusted returns while financing projects that bring social, environmental and economic benefits. "Renewable energy" is the best-known sustainable infrastructure investment. Such "green" assets help both governments and investors meet their targets, such as improving the carbon footprint that is essential for the transition to a low carbon economy. According to the European Commission, the investment required in renewable energies to meet the 2-degree global warming target set in the Paris Agreement over the next 20 years in Europe alone is around 180 billion euros per year.

While the "E" of ESG is important in renewable energy projects and relatively easy to measure in terms of greenhouse gas emissions saved or the amount of renewable energy produced, the benefits in terms of "S" and "G", i.e. society and corporate governance, may be overlooked. In addition, an exclusive focus on the renewable energy sector can lead to concentration risks in the investment portfolio.

As an asset class, infrastructure opens up a wide range of investment opportunities, diversified across many industries, and offers both social and environmental benefits. Infrastructure investments can be relatively clearly classified according to the UN Social Development Goals (SDG), as shown in the graph.

Some examples of concrete investment projects and their impact:

1. projects in the transport sector, such as railways, light rail, public transit terminals or charging stations for electric vehicles, increase the availability of low-CO_2 transport in urban and rural areas.

2. digital infrastructure, such as fibre to the home technology, promotes Internet communication and improves the provision of basic, wealth-enhancing services such as online banking and education, particularly in emerging countries, by increasing coverage of rural areas.

3. Social infrastructure, such as health and education facilities, offers access to basic services, even in socially disadvantaged areas.

SDGs & Infrastructure Sectors

3 GOOD HEALTH AND WELL-BEING	4 QUALITY EDUCATION	6 CLEAN WATER AND SANITATION	7 AFFORDABLE AND CLEAN ENERGY	8 DECENT WORK AND ECONOMIC GROWTH	9 INDUSTRY, INNOVATION AND INFRASTRUCTURE	11 SUSTAINABLE CITIES AND COMMUNITIES	13 CLIMATE ACTION	17 PARTNERSHIPS FOR THE GOALS
Hospitals Care Homes	Schools Universities	Water and Waste Water treatment plants	Renewable energy District heating	All sectors	All sectors	Schools Universities Hospitals Social housing Low carbon mass transit Data centers Smart meters Broadband Street lighting	Flood protection infra (Locks) Flood resilient infra	Public Private Partnerships (PPPs) Government Concession

What about the "G"?

The private nature of infrastructure financing means that investors can directly influence ESG aspects in negotiations with promoters. For private debt investors, ESG aspects are a central part of the due diligence process and negotiations on financing and documentation. Most investors in infrastructure loans need and require the inclusion of certain contractual clauses regarding transparency on ESG aspects and their measurement. Therefore, they can influence the management of ESG issues throughout the project cycle.

Investing in infrastructure can support multiple SDGs

The increasing institutional capital flows into the renewable energy sector is a good development that is crucial for the transition to a low-carbon economy. At the same time, it offers investors an attractive alternative due to its yield premium, its illiquidity premium over comparable publicly traded bonds.

To achieve long-term and sustainable growth, we believe that investors should consider the ESG benefits of different sustainable infrastructure sectors. This widens the range of investment opportunities beyond renewable energy and offers both better diversification and the ability to support multiple SDGs simultaneously.

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** Figures as of 31 December 2018*