UKSIF Response: Environmental Audit Committee inquiry, Aligning the UK's economic goals with environmental sustainability

Introduction

The UK Sustainable Investment and Finance Association (UKSIF) is the membership organisation for those in financial services committed to the growth of sustainable and responsible finance in the UK. We look to promote a more sustainable and inclusive financial system that works for the benefit of the environment and wider society. UKSIF represents a very diverse range of financial services firms committed to these aims and our 270+ members, managing over £10 trillion of assets under management, include investment managers, pension funds, banks, financial advisers, research providers, NGOs, among others.

UKSIF and our members have played a prominent role in helping integrate sustainability in UK policymaking over recent years, and we will look to drive this forward further in the coming years. For example, through our membership of the UK government's Green Technical Advisory Group, we look forward to helping ensure the UK's 'green taxonomy' can set the highest standard possible for green investment for the rest of the world to follow and address the serious risks posed by 'greenwashing' for consumers.

We know there is far more government, industry, regulators, and others can do to ensure the UK can meet its sustainability ambitions and cement its global leadership. We therefore welcome the Committee's inquiry, 'Aligning the UK's economic goals with environmental sustainability,' which we hope can effectively contribute to and move forward the debate over how current economic measures and indicators can be better suited to sustainable development and environmental sustainability.

UKSIF's response largely focuses on the government's recent response to the recommendations of Professor Sir Partha's Dasgupta Review of the Economics of Biodiversity, including how biodiversity could be more meaningfully incorporated into its policy decisions, and the vital need for the UK to shift from GDP as the key indicator of prosperity and towards sustainability factors, which we know have a considerable impact on the long-term value of the economy.

How effective has the Government's response to the recommendations of Sir Charles Bean's Independent Review of Economic Statistics (2016) and Professor Sir Partha's Dasgupta Review of the Economics of Biodiversity (2021) been to date?

UKSIF and our members strongly welcomed Professor Sir Partha's Dasgupta Review of the Economics of Biodiversity for HM Treasury, and we voiced our support for his Review in our 'Policy Vision' report published last year (this outlined recommendations for how the UK can advance its global leadership on sustainable finance).

We see the Dasgupta Review as a seminal piece of work that has significantly contributed to biodiversity and nature issues becoming a much more prominent part of the environmental debate and public discourse. It has raised awareness of the seriousness of the challenges we face in this area, including the systemic risks that the destruction of our planet's biodiversity poses to the economy, companies' financial returns and the future success of the financial sector, and the urgent action to be taken. The sharper focus the Review has brought is necessary, with the World Economic Forum's 2020 Global Risks Report ranking biodiversity loss and ecosystem collapse as one of the top five global risks facing us in the coming decade.[1]

For too long, discussion around environmental issues has been focused on climate change and the Review has helped broaden the focus to encompass biodiversity, which has been neglected by all stakeholders. **There remains some way for biodiversity considerations to be put on a more equal footing with climate change, and we believe the government's formal response to the Review's recommendations could go much further to help address this.**

We did endorse some of government's actions announced as part of its response to the Review, including: requiring a new legally-binding target on species abundance in England for 2030 aiming to halt the decline of nature (tabled as an amendment to the Environment Bill) and ensuring nationally significant infrastructure projects deliver biodiversity net gains. However, this does not, in our view, represent a sufficiently ambitious and wide-ranging response to the Review and **further work is now urgently needed in the UK to take forward the Review's work**. This is particularly necessary as the Review's focus was not on policy recommendations per sei, but intended to raise awareness of the challenges we face.

As a first key step, we would like government to commit to establish a formal process for considering the implementation of the Review's findings into policymaking over time. A group of investors, regulators, civil society, and other groups should be convened for a series of discussions to consider recommendations for finance and business. We called for this action in a letter to the Chancellor of the Exchequer in October last year, believing that government should look to build off the momentum generated by the Review and seek to more

[1] World Economic Forum, 'Nature Risk Rising: Why the Crisis Engulfing Nature Matters for Business and the Economy', January 2020.

explicitly integrate biodiversity risks and opportunities into financial services and companies' decision-making and its own policymaking.

We would also like government to consider how biodiversity and natural capital can be embedded in financial services regulation, including in the newly announced Sustainability Disclosure Requirements (SDR) regime which will mandate financial services and companies to disclose how they are addressing sustainability risks and opportunities. Government should explore how to incorporate disclosures against the Task-force on Nature Related Financial Disclosures framework (this aims to provide a clear nature related financial risk framework to encourage better corporate disclosure and redirect financial flows towards nature-positive outcomes) following its launch in 2023, and commit to launch a formal consultation at this point to seek the sector's views.

We want the UK to play a prominent leadership role in supporting the work of the Taskforce on Nature-related Financial Disclosures (TNFD), including encouraging a broader group of countries, such as the G20, to engage with the TNFD and endorse its critical work. This would build momentum off the G7's endorsement last summer of the Taskforce, which UKSIF and investors strongly welcomed. We would like the UK's Infrastructure Bank to deliver positive net bio-diversity gains, and this objective should be reflected in its investment criteria, forming part of its net-zero mandate. We understand Treasury will shortly be reviewing the case for expanding the Bank's mandate.

Finally, we support the calls for a 'Global Goal for Nature' that is nature positive and based around the objective of reversing biodiversity loss by 2030, and would like the UK to play an active role in the adoption of this 'Global Goal,' and the objective of making all financial flows consistent with this Goal, in the upcoming Post 2020 Global Biodiversity Framework that we hope will be finalised at COP15 in China later this year. Collectively, these actions would form part of a more effective response from government to the Review's findings, and signal the UK's intention to adopt global leadership and real ambition on biodiversity.

Now is an opportune moment to take this series of actions given the UK's Presidency of COP26 throughout this year ahead of COP27 in Egypt and the upcoming COP15 Summit. **We have concerns the Review's work will not be taken forward comprehensively by government,** and would like to see government and regulators develop greater expertise on biodiversity issues more broadly and allocate additional resources to avoid this scenario.

How might the public, businesses, financial institutions and the financial system react to any move away from GDP as the primary indicator of prosperity? What challenges could this present for policymakers, and how might these be overcome?

We very much support calls for the UK's economy, and the global economy more broadly, to shift away from GDP as the main indicator of prosperity, believing that sustainability indicators and considerations, including in relation to natural capital, should be taken far more seriously by policymakers, financial services, businesses and others to assess economic growth and prosperity, and also integrated more meaningfully into traditional economic indicators.

This is because we know and the evidence is increasingly growing **that environmental, social, and governance (ESG) issues have a significant impact on companies' long-term value and the economy.** Various studies show companies which take into account, and address, ESG issues will create greater value in the long-run for investors and savers, and we would argue that investments not aligning with environmental principles will likely, in time, not deliver good returns especially as policymakers reform subsidies and regulations impacting these companies.

For example, a recent study from BNP Paribas has indicated that over the last five years a range of sustainable equity indices have outperformed standard non-sustainable benchmark stock indices. It noted that the MSCI World SRI (Socially Responsible Investing) index saw a 14.1% compound annual growth rate in returns since the beginning of 2016, 1.1% more than the MSCI World standard benchmark.[2] Similarly, the independent research provider Morningstar evaluated the performance of 4,900 funds and found a majority of surviving sustainable funds – those that existed 10 years ago and still exist today – outperformed their average surviving traditional peer.[3]

We strongly believe GDP alone does not capture the full picture at a macro-economic level nor at the company level, and that is why governments, regulators, the industry and others are increasingly taking steps to measure and assess the material impact of climate change and sustainability more broadly on the economy. Measuring

[2]BNP Paribas, Does Sustainable Investing have to cost performance?, https://wealthmanagement.bnpparibas/content/dam/bnpparibas/pdfs/june/White%20paper%20ESG%20cake%20and%20eat%20it%20too%20040621%20V3%20ES.pdf, June 2021.
[3]Morningstar, How do Sustainable Funds Measure Up?, https://www.morningstar.co.uk/uk/news/203214/do-sustainable-funds-beat-their-rivals.aspx, June 2020.

ESG factors does come with challenges and they cannot simply be reflected in a single neat metric, in part due to the different definitions for ESG investments and complexity of data and information. Steps are being taken in the right direction, such as through the UK's 'green taxonomy' which will define a common list of economic activities that can be classified as 'green' (UKSIF is a member of an advisory group advising government on the development of the 'green taxonomy').

Policymakers need to reflect sustainability issues and concerns far more prominently in traditional economic indicators and to assess economic prosperity and growth. We have actively called for every Budget Statement delivered by the Chancellor to include a dedicated section on net-zero, highlighting how the tax and spending decisions announced bring the UK closer towards this goal. We believe there should be, in time, an expectation of Treasury that each Budget has net-zero at its core, and our position mirrors the Climate Change Committee's argument, outlined in its recent progress reports, calling for a 'net-zero test' to be applied to every area of government policy for compatibility with its climate ambitions.

A dedicated net-zero chapter in every Budget would signal Treasury's commitment to embed this across its decision-making, and help ensure every tax and spending decision is viewed through a net-zero lens. We would be very pleased to explore our proposal in further detail with members of the Committee in due course. Linked to this ask, all government legislation in future could include a net-zero impact assessment. A more holistic view from government is needed that goes beyond simply viewing its policy decisions impacting traditional economic growth measures, such as GDP.

Another step government could consider is further reform to the Treasury's 'Green Book,' which is the guidance issued by Treasury on how to appraise policies, programmes and projects and provides guidance on the use of monitoring and evaluation before, during and after implementation of policies. Last year, Treasury conducted a review of its 'Green Book' and this could be re-examined regularly to ensure sustainability factors are embedded in the appraisal of policies, programmes, and projects using the 'Green Book' guidance.

Within the financial services industry, we are seeing increasing consideration given to explicitly incorporating ESG issues into financial decision-making and investment decisions alongside traditional economic indicators, including in investments mandates with clients. **A pure focus on traditional economic indicators is now less common among investors, with a recognition that investing in companies which take into account, and actively address, ESG issues and risks will lead to greater returns in the long-run.** This is why investors exercise stewardship, which encompasses the activities undertaken by investors to promote the long-term success of companies, including voting at a company's Annual General Meeting, and we continue to strongly support investor stewardship to promote long-term value in the economy.

In conclusion, we believe there is an incontrovertible case for the UK and other countries to shift away from GDP as the sole indicator to assess economic performance and prosperity, and towards a more holistic view which reflects far more the very considerable impact of sustainability issues and indicators on the wider economy and our livelihood.

Further information

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