Business Green

Investing in the Sustainable Revolution

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Jim Totty of Sustainable Technology Investors Ltd argues there has never been a better time to invest in the fast-expanding sustainability sector

Over the next 20 years global industries will transform as they make the necessary but disruptive changes towards creating a more sustainable economy. As Al Gore recently said: "What we are seeing in the world today - I am convinced - are the early stages of a sustainability revolution that has the magnitude of the industrial revolution, but the speed of the digital revolution."

This sustainable transition offers many attractive investment opportunities that give exposure to long term, non-cyclical investment drivers. By 2050, an estimated 9.8 billion people will drive 55-80 per cent more demand for water, energy and food. Security concerns will arise from fossil fuel depletion, and food, water and resource scarcity. Institutional investors both need to mitigate insurance loss increases and the impacts of sea level rise and water shortages, as well as meet their stakeholder demands for ESG compliant investments.

From an investment perspective, there are clear sustainability themes for investors to consider:

- Decarbonisation, Decentralisation, and Digitisation
- Efficiency, Storage and Recovery
- Electrification and Autonomisation

Why sustainability?

The case for sustainability is clear. Clean water is an increasingly sought-after resource with 98 per cent of the world's water saline and two thirds of the remainder frozen. There are more than 260 river basins in the world crossing international boundaries which raise the risk of disputes over extraction and pollution. Rapidly growing Asian economies contain 60 per cent of the world's population but only 36 per cent of the world's available water. We expect water scarcity to lead to intense global pressure to become more efficient with how water is used for domestic, agricultural and industrial production purposes.

The US Energy Information Administration forecasts that world energy consumption will increase by 48 per cent between 2012 and 2040. Energy independence and security is a key concern for economies around the world, and in the UK there is heavy reliance on imported gas with consequent exposure to rising prices and interruption of supply.

Agriculture is estimated to account for 70 per cent of all water withdrawn by the combined agriculture, municipal and industrial sectors. Changing consumption patterns, including shifting diets towards highly water-intensive foods such as meat (e.g. 15,000 litres of water are needed for 1 kg of beef) will worsen the situation. It has been estimated that unless dramatic steps are taken to improve efficiency, global water consumption is forecast to increase over 50 per cent by 2030.

So why should investors consider a sustainable investment allocation in the UK?

Since the Brexit vote in 2016, we have seen the number of sustainable investment opportunities in the UK continue to grow, with our dealflow in 2017 and 2018 at a record high. Entrepreneurial activity in UK sustainable industries has never been stronger. Whatever the Brexit outcome, the UK will continue to play to its strengths in global markets in sustainability innovation and creation of businesses at the cutting edge of change.

As the UK government's Clean Growth Strategy sets out, the UK is a global leader in sustainable demand, market supply and opportunities. Since 1990, the UK has reduced emissions faster than any other G7 nation and in 2016 was the fastest of any G20 country to decarbonise. It was also the first country in the world to introduce legally binding emissions reduction targets.

Sustainability is now far higher up the public consciousness than it ever has been and the impact of the BBC's *Blue Planet* series is just one example of this. There are now 430,000 low carbon businesses in the UK and a fifth of all European electric vehicles are made here. The UK has the most productive science base of the G7 countries, and is currently the third most innovative country in the world, and ranked second in global IP protection rankings.

There is plentiful early stage funding in the UK through investment structures such as EIS. However, when sustainable businesses start to need growth equity investment in the £5-10m range there is limited capital available. We believe this equity gap offers strong investment opportunities and it is where we are focused.

At the same time, large strategic corporates are now recognising the disruptive nature of change facing them and are becoming more acquisitive of UK sustainable businesses as they seek to reposition themselves to address new sustainable markets. This provides a significant exit opportunity to well positioned investors.

Good knowledge of the whole investment ecosystem is a critical part of bringing sustainable businesses to market. UK focused investors have the skills, and networks to work with management teams to navigate these funding issues.

Why now?

The transition to a sustainable economy is driving ESG investment opportunities across all asset classes. There is now emerging evidence of companies with strong ESG performance having better share price performance. Similarly, there is now greater understanding of the impact of sustainability on economic and political stability.

The 2015 Paris COP21 conference highlighted the immediate challenge for investors to address their approach to climate change. In 2017 the UK Pensions Regulator issued guidance on sustainability which asks pension trustees to decide how relevant climate change and unsustainable business practices are, so as to better inform their investment strategy. Sustainability themed investments in Europe have continued to grow for multiple reasons:

- An increase in political pressure for environmental clean up
- The continuing energy demand growth in global economies which needs to be met sustainably
- A recognition that climate change risks disruption to economic and social activity and that climate change and sea level rise will impact investment returns.

There are exciting developments in a number of 'hot' sustainable investment areas across energy storage, electrification of transport, foodtech/agtech, and the internet of things. We are seeing many game-changing innovations which involve the adoption of technological advances to tackle sustainability issues. For instance, the adoption of drones and data technologies to solve challenges in agriculture, and internet of things solutions for energy infrastructure. In the water sector, advances in treatment and energy-efficiency technologies can deliver large bottom-line benefits for industrials and utilities.

Innovation is taking existing technologies such as electric batteries and artificial intelligence and using them to build the foundations of the new sustainable transport industry. As transport begins its journey to becoming electrified and autonomous, it will see more disruption in the next 10 years than it has in the previous 100 years.

All these factors are converging to create an attractive sustainable investment environment going forwards. We believe that now is a great time to invest in sustainable businesses.

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