

EXPERT COMMENTARY

Nature-related disclosures are becoming vital for investors but require careful calibration, according to Paine Schwartz Partners' CEO Kevin Schwartz and head of sustainability Rachel Hurley



Lessons in TNFD reporting for PE firms

Despite the recommendations having been finalised two and a half years ago, more than 700 institutions worldwide have now committed to start reporting in alignment with the recommendations of the Taskforce on Nature-related Financial Disclosures (TNFD).

These recommendations encourage businesses and financial institutions to report on how they are managing nature-related impacts, dependencies, risks and opportunities across four different pillars: governance; strategy; risk and impact management; and metrics and targets.

Considerations like these are particularly significant for private equity firms investing in areas such as

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sustainable food and agriculture – a sector that disproportionately contributes to nature loss and is disproportionately impacted by it. That's why, as the largest PE firm dedicated to this space, we at Paine Schwartz Partners were one of just two US financial institutions to become an early adopter, committing to reporting in alignment with the TNFD recommendations for 2024.

Now, after a full year of reporting, we believe TNFD reporting has broader utility across the PE industry than is commonly appreciated,

bringing structure to an area of sustainability that is becoming increasingly material to investment decisions and stakeholder expectations.

So, where does its value lie, and what does it take to do it well?

A shared vocabulary for a complex world

Environmental considerations have long played a role for PE investors, but how those are understood and implemented can vary greatly. Just as the Task Force on Climate-related Financial Disclosures (TCFD) offered clarity around language, metrics, materiality and best practices related to climate change, TNFD presents a

Analysis

standard that allows individuals, businesses and investors to speak the same language when it comes to nature – a more complex topic. Approaches may differ, but the language can and should be more consistent.

Real-world risks and opportunities

Fundamental to TNFD is the understanding that nature is a system of which all people and businesses are a part, both impacting it and being impacted by it. This awareness – long possessed by indigenous peoples but only recently incorporated into mainstream business thinking – changes the paradigm by which we relate to nature and the environment. It moves us away from the moral duty to ‘take care of’ the environment in favour of a more practical imperative to prevent the collapse of a critical, interdependent system.

This view recognises that there are real-world business risks and opportunities that come from companies’ dependencies and impacts on nature; nature loss can mean supply chain disruptions, increased costs of inputs and regulatory exposure. The management of business risks and opportunities is part of an asset manager’s fiduciary responsibility, meaning that consideration of nature becomes not just about *values* but, importantly, about *value*.

Because of its high degree of influence and its exposure via portfolio companies, PE is particularly well positioned to identify and manage these risks proactively.

Rising sophistication

The link between nature and business value is a large part of why investors’ interest in nature and biodiversity has grown so rapidly in recent years. Across a variety of asset owner surveys, the majority of respondents are saying they either have or are planning to incorporate nature into their strategies. This mirrors what we’ve seen among LPs: an increase in interest and

Case study: From assessment to action

Results from Paine Schwartz’s firm-level TNFD-aligned assessment were shared with a portfolio company’s sustainability leadership. The analysis was then translated into a practical dashboard that maps nature- and climate-related risks across the company’s 800+ global sites.

The portfolio company’s sustainability team is now using these insights as the basis for internal engagement with the CEO and site managers, with the goal of prioritising high-risk locations and integrating risk management actions into operational planning.



sophistication regarding the consideration of nature as part of investment decision-making.

The implementation of the TNFD recommendations helps PE firms assure investors that nature-related business risks are adequately managed. Furthermore, alignment allows PE firms to respond to nature-related LP inquiries with decision-useful data.

Meanwhile, nature is also growing in importance to regulators and consumers. While TNFD hasn’t yet influenced regulatory reporting requirements the way that TCFD has, nature is a growing topic of regulatory consideration, and major companies like Nestle and Unilever are making nature commitments and engaging with their suppliers on nature.

Portfolio companies can leverage the assessments and insights generated at the firm level to accelerate their own nature-related reporting and risk management efforts, whether that’s in support of voluntary TNFD reporting, responses to customer inquiries or regulatory-related disclosures.

Perspectives on TNFD reporting

The TNFD itself acknowledges that the first year of reporting can be a big undertaking, and our experience affirmed that. The most intensive part of TNFD reporting for most PE firms will be the assessment of the actual dependencies, impacts, risks and opportunities specific to their portfolios, as this requires detailed location data and a deep understanding of the intersection between nature and each portfolio company’s operations and value chains. Although the results of this first assessment will represent only a point in time, the process itself will provide insight into data and resourcing needs for developing a strategic and durable approach to the governance, strategy, risk management and measurement necessary for comprehensive TNFD reporting.

The TNFD provides plenty of guidance on how to conduct these assessments, but here are some of the key takeaways and best practices gleaned from the successes and challenges of our first year of reporting.

“Consideration of nature becomes not just about values but, importantly, about value”

» Seek the right tools and providers

The TNFD guidance is detailed and clear, but even the highest-level assessment can be quite an undertaking. Using third-party tools and providers that are deeply familiar with TNFD guidance and that have seen common pitfalls will ensure a more valuable final product.

When choosing tools and providers, consider not just familiarity and alignment with the TNFD approach, but also an understanding of the industries in which you invest. Ensure alignment, not just on scope and work product, but also on the outcomes you are seeking.

» Get the data right

As they say in data science, “garbage in, garbage out”. The quality of insight from a TNFD nature assessment will be limited by the quality of the data analysed. It’s important to aim for comprehensive, precise and specific data on the type, footprint and location of companies’ sites, with the understanding that, especially in the first year, perfect data is likely unachievable.

It helps to aim for good quality inputs across the board and to push for even better data quality where it matters most. Where you choose to push for better quality data should be informed by what you are hoping to get out of the assessment.

» Understand the limitations

No tool or provider is perfect. Perfect portfolio data is unrealistic, which means that the results of any nature assessment will be imperfect too. Having clarity about these limitations will help contextualise the results and illuminate errors or inconsistencies.

Before you even look at the results of your assessment, ask yourself about the limitations of your approach. Consider the limitations of your inputs, the assumptions and data that underly the assessment, the comprehensiveness (or lack thereof) of what is being assessed and the types of data that are not being included which may affect the results. Having a sense of what the results can’t tell you will help you gain meaningful insight from what they can.

» Drill down into the details

In formal TNFD reporting, PE firms may report risk and opportunity assessment results at an aggregated fund or portfolio level. This aggregation makes reporting simpler and helps demonstrate the most common or prominent risks and opportunities throughout a portfolio, but aggregated results can obscure portfolio company or site-level results at the extremes.

If the goal is to understand and manage nature risks and opportunities at portfolio companies, those individual data insights matter just as much as, if not more than, the commonalities across the portfolio. Additionally, a close look at site- or portfolio-level data can help identify data entry errors or instances where results are misleading due to limitations inherent to the approach.

It’s best to get into the weeds of your nature assessment results, even if you’re only reporting at a fund or portfolio level. This will give you more actionable insights, as well as providing the opportunity to refine

your inputs to improve the accuracy and value of the results.

» Partner with portfolio companies and investment teams

Investment teams and portfolio company management teams know their companies best, and so their insight and feedback are critical to ensure the accuracy and value of nature assessments. They can provide input data, share relevant context and offer valuable insight into how risks and opportunities are already being addressed – all of which can impact your assessment results.

Buy-in from investment teams and portfolio companies will also be critical for addressing any identified risks and opportunities. These stakeholders will benefit from education on key nature terms, the methodology of the approach, and real-world examples of how nature impacts business. Their feedback will help ensure that your approaches to governance, strategy, risk management, measurement and reporting are pragmatic and linked to value.

Partnering with investment teams and portfolio companies early is key. Educate them on the real-world business risks and opportunities posed by nature; contextualise your data requests, and seek their feedback; and finally, give them the tools and resources to implement risk mitigation and value-maximising efforts.

The first year of TNFD reporting is just that: the first year. The insights, gaps and limitations that surface in that initial cycle will shape a more focused and efficient approach in subsequent years. With each iteration, PE firms will gain sharper insight, better data and greater clarity – all essential for managing the nature-related factors that increasingly shape business outcomes. ■