Vantage Infrastructure

Sustainability is a genuine investment driver and objective

Carla Peterson, managing director, infrastructure, for Institutional Real Estate, Inc., recently spoke with **Oliver Schubert,** senior partner of Vantage Infrastructure, about solutions in sustainable infrastructure investing. Following is an excerpt of that conversation.

What does sustainability in infrastructure mean for Vantage Infrastructure? How does this influence your investment strategy?

From our perspective, sustainability in infrastructure is basically a "do good" versus "avoid harm" approach to investing, which targets market returns, but also seeks to enhance value through active ESG practices. It is a proactive approach with the intention of having a positive impact across all three ESG dimensions, while also creating value. It is not just a risk-management approach.

Secondly, the impact we are talking about needs to be measurable throughout multiple environmental, social and governance dimensions. For example, energy consumption, greenhouse-gas emissions, job creation, the reduction of the number of accidents in a given year, better capture rates of vulnerable customers. There are lots of examples of measurement dimensions one can use, but it is important that the impact be measured and reported. For us, that means that our investments need to measurably contribute to a net-zero economy. We are convinced that infrastructure must be one of the driving forces for decarbonization, both in terms of adapting existing infrastructure, but also building new infrastructure.

Sustainability is not only about climate change. Rather, climate change is a very important topic and drives a lot of investment decisions, but climate change also overproportionately impacts the most socially vulnerable population. Therefore, if you invest in low-emission and climate-resilient growth, that is the best way to unlock lasting socioeconomic and environmental benefits.

Our strategy focuses on investments that positively respond to all of these three questions: First, can this investment provide a positive ESG impact while delivering market returns? Second, can we measure this impact? And third, does this investment — and the impact it is supposed to generate — fit our overall objective of contributing to a net-zero economy?

What do you think is driving the investment opportunity in Europe?

Europe is really a mid-market investment universe. We define the mid-market as investments with an enterprise value up to €500 million ($566 million). This market segment historically has delivered 80 percent to 90 percent of all transactions in Europe over the past 10 years (in volume), which is probably related to the economic structure of Europe. That volume and the proportion of deal flow in the mid-market are unlikely to change anytime soon. A second driver is that Europe is at the forefront of sustainability regulation and initiatives, driven by the European Union's 2030 and 2050 climate targets in line with the Paris Agreement. The European Union wants to achieve net-zero GHG emissions by 2050. There is a technical expert group mandated by the European Commission a few years ago that has spent considerable time defining what sustainable economic activities are and how to drive capital — with direct investments, both public and private — into genuinely sustainable activities that help achieve those 2030/2050 climate targets. We are convinced these frameworks for investments and disclosures drive investment opportunities, especially since there is a massive gap between the investments required to achieve the 2050 targets and the amount of capital available. The currently smaller number of managers focusing on sustainable infrastructure investments, like Vantage, provides those managers with more investment opportunities in Europe. Finally, several E.U. governments have developed their own support schemes for their own national net-zero targets. These measures all support mid-market investment opportunities in the European markets for the foreseeable future. Especially in the periods from today to 2030 and then from 2031 to 2050, we will see massive investments into decarbonizing the European economy. Infrastructure is one of the main beneficiaries of this movement.

How do you measure the net-zero impact?

It is a simple question with a complex answer. The simplest response would be to measure Scope 1 and Scope 2 GHG emissions. All of our portfolio companies do this, but this is only one element. Scope 3 emissions, which are the emissions that come from up and down the value chain, are more difficult to measure. We are most likely to be in a position to report those for all of our portfolio companies by the end of the year, but it requires quite a bit of work. The other question is, if you offset emissions (for example, if you acquire green certificates or if you invest in decarbonizing projects), should you include that offsetting in your approach and in your calculations to achieve net-zero emission? For now, there is no universal standard in reporting what net-zero actually means, and so how do you measure the impact? And are you actually comparing apples to apples when you talk about net-zero impact? We, therefore, use the E.U. taxonomy as our main measurement tool. It is a very comprehensive framework that objectively defines what sustainable activities are against a number of quantitative and qualitative criteria, and it is mainly, but not exclusively, driven by climate-change and decarbonization considerations. The E.U. taxonomy has been developed by the European Commission through a technical expert group over several years and has come into effect this year. It will permeate the whole investment market, whether public investments, private investments, debt or equity. When you apply this tool to investments, you calculate an alignment percentage to the E.U. taxonomy. To oversimplify, the higher the percentage, the more the activity contributes to net-zero, while also maintaining minimal social standards, so it is quite a comprehensive framework. The Sustainable Finance Disclosure Regulation, which is also about to become applicable and is in the process of being implemented in the European market, will hopefully provide investors with a clear classification of investment products and their pursuit — or not — of sustainable investment objectives.

Do you integrate climate risk in your risk assessment during acquisition and asset management?

Yes, we absolutely do. Vantage has been a TCFD [Task Force on Climate-related Financial Disclosures] supporter for a number of years, and we have started to implement TCFD recommendations with our portfolio companies. We designed a climate-related risk-assessment tool, which is aligned with the TCFD framework, to analyze the materiality, the risk to value and the time horizon of three factors: transitional risks, including policy and legal risks, technology risks, and market and reputational risks; physical risks to the assets, which could be acute or chronic depending on the type of risk; and the opportunities that come out of these climate risks. We have already applied this tool to all of our portfolio companies, and we have run pilots with two of our portfolio companies for more in-depth climate-risk assessment. These are complicated assessments that require quite a bit of work to be comprehensive. Our objective is that all of our portfolio companies will be in a position to provide TCFD-compliance disclosures over the coming two to three years, in line with the TCFD adaptation timeline. It is absolutely critical that our portfolio companies are able to identify the risks, identify ways of mitigating those risks and then, obviously, be able to report them to the broader stakeholder community.

Which sectors do you think are the most attractive for sustainable investments in infrastructure?

Quite a few, actually. The markets we feel are the most attractive are driven by very strong sustainability macro themes, such as the decarbonization of power, heat and data; the electrification of transportation; the digitization of energy supply and the efficiency that it creates; and circular economy. These themes give us the comfort that whatever investments we are making along those thematic lines will be resilient against future regulatory changes and will also be uncorrelated from economic cycles in the long term. They also allow us to deliver very sector-focused buy-and-build investment strategies, which we consider to be able to deliver more robust returns. These sectors provide resilience and, very often, proprietary transactions.

The main sectors we focus on currently are renewable heat, solar photovoltaic, battery storage, energy metering, electric-vehicle charging, water and data centers. We are also looking at a few opportunities in the biogas-to-the-grid and hydrogen space, although these will take more time to materialize.

Do you see a danger of greenwashing in infrastructure? What differentiates a genuinely sustainable investment manager?

I don't want to call it greenwashing because that implies an intention I don't want to imply. What we do see is what I would call "green veneering" of investment activities and some reporting. We appreciate that it is difficult for investors to distinguish this from genuine sustainability strategies, given the lack of universal standards and definitions that everybody agrees with, and we recognize and commend the fact that a lot of effort has been made in terms of sustainability reporting. Putting myself into an investor's shoes, there are a number of questions I would ask a manager: How long have you applied ESG or sustainability criteria to your investment lifecycle? How integrated is that approach within the investment team? Do you pursue an overarching sustainability objective, either as a firm or with whatever product you are marketing? How is this objective articulated? How do you measure the impact of that strategy, and how sound is the measurement methodology? What investments do you currently hold, and what is the sustainability story for each of these investments? That is the level of granularity where, typically, you really figure out whether these investments have been green veneered or have been acquired for a sustainability objective. Finally, I would look into the current sustainability reporting — the level of reporting, the frequency of reporting, the comprehensiveness of the reporting tell a lot about what the strategy is trying to achieve. Does the manager apply best practices in terms of ESG and sustainability across portfolio companies? There are a number of questions along these lines that help reveal to what degree sustainability is a genuine investment driver and objective.

CONTRIBUTOR

Oliver Schubert
Senior Partner
Vantage Infrastructure

Oliver Schubert joined Vantage Infrastructure in 2012 and brings more than 20 years of relevant experience. Based in London, he leads equity transactions. He is a member of the Equity Investment Committee and of the firm's global Executive Committee.

CORPORATE CONTACT

Oliver Schubert
Senior Partner
Oliver.Schubert@vantageinfra.com

CORPORATE OVERVIEW

Vantage Infrastructure is an independent infrastructure debt and equity specialist committed to delivering sustainable investment solutions as a long-term partner to its clients, with approximately $5.0 billion assets under management as of Sept. 30, 2021. The firm has a heritage as one of the world's first infrastructure investment firms with a long track record of partnering with global clients to implement leading investment solutions within the infrastructure sector while aiming to protect its clients against downside risks. Fundamental to its approach is responsible investing and embedded ESG considerations in its processes as a driver of value and risk. Reflective of this, Vantage is a signatory to the Principles for Responsible Investment, a supporter of the Task Force on Climate-related Financial Disclosures, a GRESB Infrastructure Member and an investor member of the Institutional Investors Group on Climate Change. Through its managed investments, the firm contributes to 10 of 17 U.N. Sustainable Development Goals.