Real assets, real impact

For investors to have a real impact on climate change requires tangible, achievable paths to net zero carbon emissions. Igneo Infrastructure Partners' Sophie Durham explains how this can be achieved through engagement and collaboration with portfolio companies.

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Addressing and combating climate change is one of the defining challenges of the 21st century. For asset managers, it presents myriad issues but also a wide range of opportunities to invest in forward-looking companies and assets that can have a real-world positive impact on society and the environment. Igneo Infrastructure Partners – the direct infrastructure investing business owned by First Sentier Investors – began reviewing its climate change policy in 2020 with the aim of being able to demonstrate tangible results from its engagement work with portfolio companies.

Beyond net-zero

Sophie Durham, Managing Director and Head of ESG for Europe at Igneo, recalls that the company's initial analysis work at a portfolio level soon proved to be limited in terms of actionable outputs, beyond setting net-zero emissions targets.

"There has been a lot of criticism of these targets because they can be seen as just ticking a box," Durham says. "Our whole ESG approach is about focusing on actions and results in portfolio companies. At the same time as setting our net-zero target, we launched Climate Action 1, 2, 3!, which we think is a much more important initiative."

Climate Action 1, 2, 3! is a straightforward set of three actions for decarbonisation and climate risk management that Igneo aims for all portfolio companies to implement by the end of this year, or within three years of acquisition.

With full or majority ownership of most portfolio companies, the asset manager engages directly with corporate leaders to develop a series of short-, medium-, and long-term targets for reducing emissions with a realistic plan for implementation.

Risk assessment covers physical risks from climate change and the challenges posed by the transition to a low-carbon economy, which should then be integrated into each portfolio company's plan.

Finally, governance structures are reviewed and improved where necessary to ensure that the risks and opportunities from climate change can be managed appropriately. Through this proactive engagement approach, 19 of Igneo's 25 portfolio companies have now set realistic and implementable net-zero emissions targets for 2050 or sooner, with the remaining companies working positively towards their own plans.

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Navigating challenges

While 19 of Igneo's portfolio companies have set net-zero targets, an important focus of the asset manager's work is helping the remaining six catch up. For some of these firms, establishing a realistic goal with a clear path to implementation has proven more complex, for various reasons.

Durham says: "When we first raised Climate Action 1, 2, 3!, some of the portfolio companies said that while they could set a net-zero target for 2050, they may not yet have a clear idea of how it would be achieved in practice. What we didn't want was for a company to set 'pie in the sky' targets – but we have to get to net zero by 2050. In these cases, we've been working individually with each company to set realistic targets."

One example of this work is enfinium, a UK-based energy company that generates power from waste – a key element of the UK's national net-zero energy strategy. Generating energy from waste is more environmentally friendly than sending the same waste to landfill, where it can result in increased methane emissions.

However, as Durham points out, as Igneo has worked with enfinium to set a net-zero target, it has decided not to include avoided emissions in any calculations or planning. This allows the two companies to focus on the carbon emissions still generated by enfinium's operations, emphasising the importance of a real-world impact.

"We've been working with enfinium over the past two years, and the company will soon be publishing its net-zero plan," Durham says. "The company has come up with a technical roadmap that shows it could reach net zero as early as 2033 based on installing carbon capture and storage technologies at its largest facilities."

Over time, enfinium plans to install these technologies at other facilities, meaning the company would be carbon positive, capturing and storing even the biogenic or renewable part of its emissions, potentially delivering 1.2 million net tonnes of verified CO2 removals each year by the end of the next decade.

However, to make this plan a reality will require engagement with UK policymakers and other stakeholders to address external dependencies, such as carbon pricing and offtake agreements. The next stage for enfinium and Igneo, therefore, is to work with policymakers to effect positive change. At the same time, the companies will work on the commercial elements of the plan as it will require significant investment. As Durham explains: "We still haven't translated the technical roadmap into formal targets for enfinium, as we need to do more work. But by the end of this year we will have a technical roadmap, a policy roadmap, and a commercial roadmap that will show net zero is achievable. As a result, the targets we eventually set will be much more realistic. It's been some incredible work from the management team of the company to get to this point."

Decarbonising shipping

As Durham explains, Igneo's engagement approach is not new; it is merely an extension of its approach to all other aspects of asset management, whether it is operational improvements, cost efficiencies, or expansion plans.

With each company, the approach is tailored with the aim of achieving real-world impacts that benefit the company as well as the environment and society.

In Northern Europe, Igneo owns Scandlines, which is the sole operator of two ferry routes connecting Denmark and Germany. The company has been striving to achieve net zero emissions for its ferry fleet since 2011 and has made significant progress through investment in green technologies.

By rolling out engines that combine diesel and electric battery power and a number of energy efficiency innovations, Scandlines has been able to cut its emissions by 25% compared to 2018 levels as of the end of last year.

Now, the company is working on building its first ferry to have zero direct emissions. The new ferry is designed to be seven times more energy efficient per freight unit than the 40-year-old freight vessel it is replacing. It will be able to operate solely on battery power if needed, and is forecast to save almost 15,500 tonnes of CO_2 a year when using its hybrid power system – equivalent to approximately 12% of the company's 2022 Scope 1 emissions.

Scandlines is also working with a third-party technology firm to measure the Scope 3 emissions of the new ferry, assessing the carbon footprint of each component across the expected lifecycle of the vessel by collecting data directly from suppliers. It will also model the use of other green technologies on the vessel to aid investment decisions.

Promoting collaboration

Igneo is keen to support its portfolio companies to work together wherever possible to explore what works and what does not work across various elements of ESG. This was particularly important when it came to helping companies tackle the tricky issue of Scope 3 carbon emissions.

For example, when working with Australia-based International Parking Group on a decarbonisation plan for the company's network of multi-storey car parks, Igneo was able to connect management with senior staff at Spanish car park firm Parkia to share ideas, particularly on the calculation of Scope 3 emissions and potential options for reduction.

When an initial data request for Scope 3 emissions two years ago only brought back information from seven of Igneo's 25 portfolio companies, and Durham says even this was "patchy" and "not a very good quality data set".

The asset manager persevered and engaged again with its portfolio companies – this time with the help of an external consultant. Through a series of training sessions for the relevant senior staff, Igneo was able to not only explain the importance of Scope 3 reporting and how it can be done, but also put different companies from similar sectors in touch directly to aid the consistency of approach.

"It was detailed training for the people who actually do the calculations," Durham adds. "Clearly, this kind of work is too detailed for board level, so we deliberately provided the training to the people we knew were going to be running the numbers because we know them already.

"As a result, last year we got Scope 3 emissions data from 20 out of 25 companies, up from seven a year earlier. That's a big increase and a much better quality data set."

Balancing ESG and investment performance

In recent years, while ESG strategies have become more prevalent, debate about their use has grown more polarised in some areas. Politicians in some countries have argued that investors – particularly those in charge of pension savings – should focus purely on financial returns.

Even outside of this debate, some investors still express concerns they will have to accept lower investment returns if they place more emphasis on non-financial metrics such as those related to ESG.

However, for Igneo's Durham, there is no trade-off – particularly when investing in real assets.

She explains: "We invest in big physical infrastructure assets. They have a big environmental impact and can have a big social impact too. Just as importantly, they can be materially impacted by the environment and the societies in which they operate. You cannot successfully manage these companies without also addressing material environmental and social issues.

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"Take diversity, for example. There are heaps of studies that show that more diverse boards and management teams make better decisions and are better at managing risks. There is no trade-off between promoting diversity and improving the management of your finances or other aspects of your business."

In addition, Igneo's portfolio assets are inextricably linked to climate change issues, particularly those in the power, utilities, and transport sectors.

"These are sectors that can be carbon intensive and are often thought of as being difficult to decarbonise," Durham continues. "On the other hand, they will be absolutely critical to delivering on net-zero ambitions – and our economies can't function without them. These companies have to be the ones delivering net-zero solutions. If you want a sustainable long-term business, you can't ignore energy transition risks."

For private market investors, this long-term focus is important though the life of a company will likely stretch far beyond the time horizon of a typical 10-year private asset fund. Increasingly, Durham explains, infrastructure funds are seeking high-quality assets with strong sustainability credentials, meaning that improving ESG performance is a key element of securing an attractive exit price for an asset.

Essential infrastructure

One example of such essential infrastructure is found in Northern Europe. Nordion Energi is a Swedish energy group formed through the integration of three portfolio companies and aims to drive the transition towards a fully green energy system in Sweden. Responsible for a significant portion of the country's gas transmission and distribution networks, Nordion is also pioneering biogas and hydrogen power infrastructure.

"Sweden has set a net-zero target for 2045, so clearly it needs to address the use of natural gas. That's a significant risk but also a big opportunity for the company," says Durham.

"We are pursuing initiatives around hydrogen, carbon capture and storage, and biogas. Last year, 40% of the gas in our networks was green and climate neutral, and we are going to keep driving that number up until we reach 100%."

Nordion aims to reduce its Scope 1 and 2 emissions by 80% relative to a 2019 benchmark by 2025, according to Igneo's latest annual ESG report.[1] Beyond this, it plans to reach an 86% reduction by 2030.

Meanwhile, in Australia, Igneo is an investor in Brisbane Airport, which handled more than 1.7 million domestic and international passengers in April 2023.[2] The airport has accelerated its net-zero target from 2050 to 2025 through investing in a renewable power purchase agreement to source energy from local wind farms. It also plans to expand its on-site solar power facility, and introduce carbon removal technology.

Through direct investment in real assets, investors can engage positively with companies and work collaboratively to solve some of the biggest challenges facing society – all while still generating a strong financial return.

FOOTNOTE

1 See: Igneo Infrastructure Partners Global Environmental, Social and Governance Report 2022.
2 Source: Brisbane Airport Corporation passenger statistics.

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