

Transitions to a Sustainable Economy

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How to navigate through the transitions?

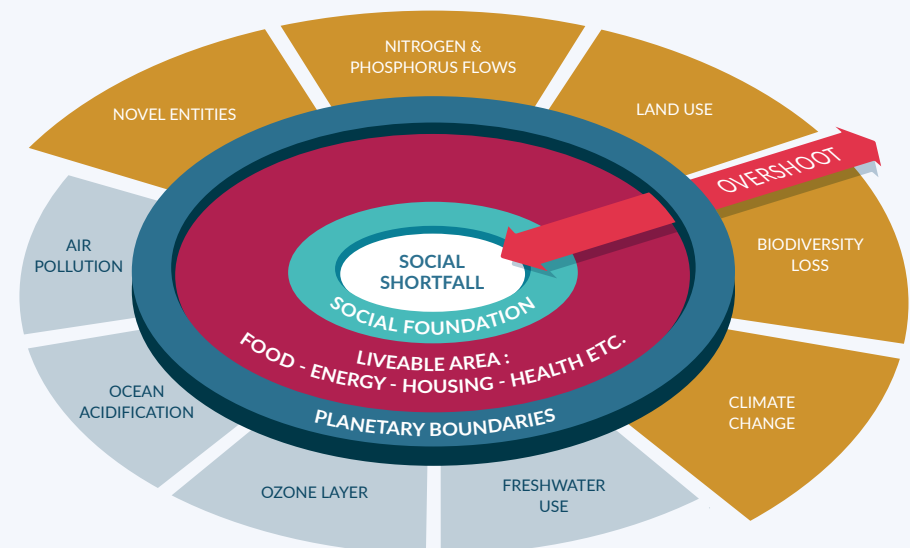
Our planet is threatened by the way we produce and consume. Climate change and biodiversity loss, to name some of the most obvious issues, continue to affect people and society profoundly. These issues call for a global transition to a more sustainable economy. Virtually all economic sectors and all companies are therefore facing necessary and inevitable changes. This provides opportunities as well as poses threats. At Van Lanschot Kempen, a major priority is to help our clients navigate through these transitions. What needs to be done and how will we do it?

Why act?

It has become increasingly clear what the negative aspects of unsustainable economic growth has meant for people and our living environment. Think of frequent floods and extreme droughts due to climate change and the pressure on our food production systems because of growing populations and rising living standards.

Research shows that the natural boundaries of our planet, within which humanity can safely operate, are already being exceeded on five separate levels.¹ These planetary boundaries are shown in image 1. They involve (1) climate change, (2) biodiversity-loss, (3) land use (including loss of forests and rainforests), (4) depletion of (agricultural) land (nitrogen & phosphorus

Why do we need to change?



Anna Ferschtman
Sustainability writer
Van Lanschot Kempen

¹ (Rockström et al. (2009). A safe operating space for humanity. Nature, 461, 472-475. A safe operating space for humanity | Nature Steffen et al.(2015). Planetary boundaries: Guiding human development on a changing planet. Science, 347. <https://www.science.org/doi/10.1126/science.1259855>

flows) and (5) the introduction of man-made products into natural environments with undesirable consequences - think plastic pollution.

The crossing of these boundaries also compromises the social foundation of a society: people's access to water, food, energy, education, healthcare and housing (among other things) can become jeopardized. We can already see this reflected in the Human Development Index, a measure of social development, dropping for two years straight for the first time ever. Many countries experi-

enced ongoing declines.² Achieving the United Nations Sustainable Development Goals (SDGs) by 2030 is at risk as well.³

This underlines the urgency of making the transition to a sustainable economy and society. There is also a strong case for developed economies to lead the way, being the largest consumers of goods produced, as well as being countries with a longer history of production, pollution and economic development. These countries may act as a foundation for further, global action and become 'role

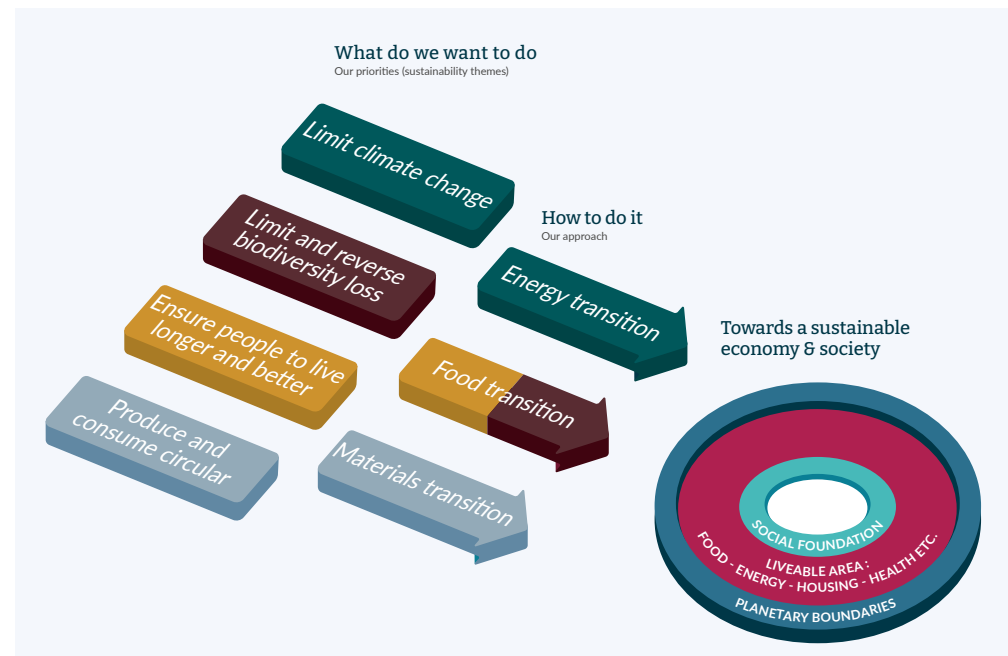
models' for other countries – leading by example is crucial.

Our focus

How can Van Lanschot Kempen help its clients to navigate the sustainable changes needed to mitigate the harmful effects of certain economic activity on the planet? Navigate through the transitions, in which winners (and losers) ultimately emerge.

To be more effective and have impact, Van Lanschot Kempen has identified the following priority themes: limiting climate change and biodiversity loss, improving people's health and well-being, and circular production and consumption. We link these themes to three transitions: the energy transition, the food transition, and the (raw) materials transition.

Transitions are complex processes that ultimately lead to fundamental changes that affect all aspects of the economy and society. **Our primary focus will be on the energy transition and the move towards a low-carbon economy. Through our focus, we aim to increase our impact.** However, we will also continue to work on the food and materials transition.



² HDI report 2022

³ UN SGD report 2022

Energy transition

Humanity has experienced several energy transitions which were pivotal for human development: from wood as our main fuel source to coal, and later to a broader range of hydrocarbons (e.g. oil). The challenge in the current transition is the speed at which the change must take place: in order to keep global warming limited to 1.5C, renewables must account for almost three quarters of total energy by 2050, up from roughly a tenth in 2021.

Meanwhile in the International Energy Association's (IEA) net zero scenario, fossil fuel supply will need to decrease by three quarters in absolute terms.

WHAT NEEDS TO BE DONE?

Companies: more investments in clean energy needed

- × Annual global energy investment needed for the energy transition should triple, from \$1.3 trillion now to \$4.3 trillion a year.
- × Long-term commitments are now in place for 70% of the global economy (for 2050), but intermediate targets for 2030 are lagging.
- × Companies in all sectors need to accelerate their policies, targets and actions to prepare for a transition to a net-zero emission economy.
- × All sectors still have much to do to deliver on ambitions in the medium term (2030). Some examples:
 - Electrification in the transport sector
 - Coordinated action on emission reduction and efficiency in the industrial sector
 - Changing production methods and consumption patterns in the agricultural sector
 - Energy-efficient buildings in the construction sector

Opportunities:

- × Investment in renewables and electrification will need to rise sharply.
- × Demand for net-zero solutions in sectors such as real estate and transport could generate over \$12 trillion in annual sales by 2030, according to a McKinsey calculation.⁴
- × Demand for new technology required for the transition, such as hydrogen and CO₂ capture, will also increase substantially, amounting to sales of \$200 billion, annually, up to 2050, according to the IEA⁵.

Risks:

- × Demand for rare minerals, such as copper and lithium, will rise sharply. This greater dependence creates supply risks, often from countries with poorer human rights records and less stable political systems.
- × Limited availability of new technologies for the energy transition, which will require some sectors to make additional investments in Research and Development (R&D).

Countries: scale up ambitions

- × An increasing number of countries have set net zero targets, but most have not yet taken enough action to meet them. Ambition is weakening, partly because of the current energy crisis and war in Ukraine.
- × Stronger renewable energy ambitions and larger investments in the energy transition are precisely the solution to the current energy crisis. In the medium term, renewable energy would ensure more energy security and affordable energy.

A socially-just transition

The transition must take place in a socially just manner. It will affect employment, people's income, and their access to (and cost of) energy. In all IEA scenarios, more jobs will be created through the transition than lost. However, there will be economic dislocations which will require different skill sets.

⁴ McKinsey, 2022, *Playing Offense to create value in the net-zero transition*

⁵ IEA WEO 2022

Food transition

The combination of a growing world population and rising living standards has led to a food production system that depletes natural resources, pollutes the environment and marginalises farmers. Although about half of the global economy depends on nature for at least a part of their food consumption, about 40 per cent of agricultural land has been depleted. This is mainly due to our unsustainable methods of producing food.

WHAT NEEDS TO BE DONE?

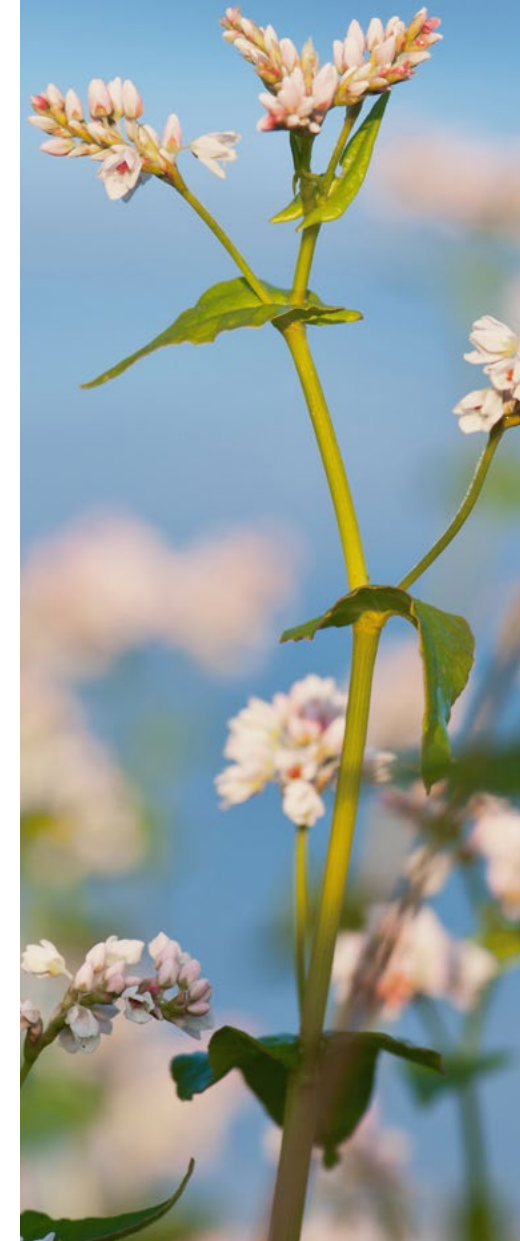
- × A food transition should lead to a more diverse and nutritious production system. Think crop diversification, combination of annuals and perennials, sustainable agricultural intensification, crop rotation and agroforestry (combination of agriculture and trees, shrubs).
- × Investments in more sustainable forms of agriculture will create farmland rich in organisms and thus able to feed people again, even without damaging pesticides and fertilisers.
- × Consumption patterns will also have to change, with a shift to a more plant-based diet. Farmland can then be used to produce food for humans, rather than for feeding animals for human consumption.
- × Transport and supply chains will have to be shortened to avoid waste.

Opportunities

- × Major investments are needed to change the food production system. According to the OECD⁶, the annual ‘finance gap’ around biodiversity restoration and conservation activities is \$600-825 billion - more capital is needed to contribute to this.

Risks

- × The food system poses serious (physical) risks to biodiversity and ecosystems through land use and climate change, among other things. But at the same time, food production and related economic activities also depend on these ecosystems.



6 OESO 2021, “Biodiversity, natural capital and the economy”, www.oecd-ilibrary.org

Materials transition

Raw material extraction, such as fuels, metals and food, put pressure on various planetary resource boundaries. For instance, concrete has a major impact on climate change, while electronic products impact biodiversity, and so too wooden furniture on land use. The extraction and processing of raw materials, such as metals and food, is responsible for more than 90% of global biodiversity loss and about 50% of global greenhouse gas emissions.

WHAT NEEDS TO BE DONE?

- × A shift is needed towards more circular production and consumption. We must produce goods using fewer material inputs, extend the life period of products/goods, and promote circularity (e.g. recycling).
- × Governments should set guidelines and targets, coupled with price incentives and other methods to change the behaviour of producers and consumers. For example, the European Union has recently drafted legislation banning the sale of products grown on deforested land.

Opportunities

- × Again, new ways of (circular) production offer investment and growth opportunities. Recycling or reusing (think batteries, transport, plastics etc.) can bring financial benefits for companies, while technologies designed to enable this present growth opportunities.

Risks

- × Globally, there are no targets or policies yet in place to accelerate the materials transition. Compared to the energy transition, the materials transition lags behind.
- × In addition, there is a risk of disruptions in global value chains. This could, for instance, lead to a shortage of certain raw materials, including materials that are needed for the energy transition (e.g. precious metals for electric vehicle batteries).



Managing the Transitions at Van Lanschot Kempen

Van Lanschot Kempen has been focused on solutions and possibilities for almost three centuries since our founding in 1737 - a mentality that is essential for understanding and moving with the fundamental changes of our time. Today as well, we will help our clients navigate through these transitions, seize the opportunities presented by their changes, and manage the associated risks as much as possible.

We want to play an active role in the necessary changes. Our initial focus is on climate change and the energy transition. How will we do this?

- × **A sustainable business strategy:** we have fully integrated sustainability into our business strategy. We aim to be a 'net zero' wealth manager by 2050, with an intermediate target of at least 50% CO₂ reduction by 2030.
- × **(Re)allocation of capital:** we (re)allocate our clients' assets towards the opportunities presented by the transition. This is done through our in-house funds as well as externally-managed funds.
 - We apply extensive climate risk modeling and scenario analyses to determine the impact of climate change and the impact of the three transitions on the risk and return characteristics of our clients' investment portfolios. For example, we apply data-driven modeling of physical climate risks (e.g. floods and hurricanes) to assess risks for real estate and infrastructure investments. We also model risks to equity markets from developments in carbon pricing increases.⁷
 - We advise our clients on how to align their portfolios with net zero ambitions and support them in doing so. For example, in collaboration

with MSCI, we have developed customised equity benchmarks to reduce CO₂ intensity and mitigate the impact of climate risks on our clients' equity portfolios.

- For our own internal funds and our sustainable asset management solutions, we have set targets in line with (and mostly ahead of) the route to net zero emissions.
- We invest through our own funds as well as external funds in impact solutions, including infrastructure and renewable energy. At the same time, we try to avoid the investments which we feel are not well adapted to the three transitions (i.e. "the losers").
- × **Change through dialogue:** we use our influence as an active shareholder and engage with companies and asset managers to encourage them to make the transition to net zero. This leads to positive results and real world change.
- × **Impact through loans:** to help customers make their homes more sustainable, we are introducing a new sustainable mortgage product in early 2023.

⁷ See for a summary of these results: [Kempen \(2022\), Carbon Shock Analysis](#).

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