

# Sustainable private equity poised to boom

**Robert Rubinstein**, CEO, TBLI Group and Brooklyn Bridge, Amsterdam, The Netherlands

**Private equity investment on socially responsible principles is a sector set to take off. It offers 'profit-plus investing' – that is, investing to achieve a substantial return with a social and environmental added value, and is therefore very attractive to pension funds with a socially responsible agenda facing a Baby Boomer retirement funds shortfall. Multinationals are also increasingly willing to pay a high price premium for CSR brand values. With the world facing serious problems, all the macro-economic signals indicate that industries offering sustainability and innovation are poised to grow.**

**S**ocially Responsible Investing (SRI) has been increasing in acceptance and awareness. Most leading investment houses have created SRI funds or are in the process of creating these funds. Some have even started entire departments, with research, product development, and asset management functions. ABP, based in the Netherlands and one of the largest pension funds in the world, has launched Loyalis, a pension fund manager offering SRI fund management services to other pension funds. However, what most fail to realise is SRI principles only apply to public equity, which represents a very small percentage of the total amount invested in companies. Most of the world's companies do not have stock market listings; they are funded privately through instruments such as debt financing, private equity, micro-financing and grants.

## Public versus private equity

Sustainable private equity or TBLI (triple bottom line investing) private equity is therefore moving up the investment agenda. Sustainable private equity (private investment on socially responsible principles) is of more importance than SRI, mainly because public equity impacts comparatively few companies and does not provide working capital. Most importantly, the innovation that is needed to create a sustainable economy tends to come from small and medium-sized companies, which are not usually funded through public equity. BP, Shell, BASF and Dow, for example, are not noted sources of creativity and innovation.

How are innovative companies to achieve financing for technological developments? This has to come from private equity or venture capital, of course. The looming black hole facing pension funds, due to the 'greying' of

the population, will further push demand for private equity, with its traditionally higher returns than conventional public equity investment. Timing, public awareness, and environmental concerns are coming together to create a shift in the investment climate towards sustainable private equity. Many of the industries

Timing, public awareness, and environmental concerns are coming together to create a shift in the investment climate towards sustainable private equity.

that will benefit from this new cashflow are closely involved in the 'cleantech' or sustainable industries of the future.

## Boost for sustainable private equity

There have been two important recent developments concerning sustainable private equity. First was the announcement that Alpinvest (formerly NIB capital) was to receive an additional €6 billion of investment from Dutch pension providers PGGM and ABP. Similar asset allocations have been carried out by Calpers and other large pension funds. Then, on 1 January 2004 Robeco launched the innovative new private equity fund of funds, Robeco Sustainable Private Equity. The Fund applies sustainable investment criteria to the selection of a portfolio of private equity investments. This confirms what many in the sustainability field knew and felt, namely that sustainability is a real market with real returns and excellent opportunities. This means that more money will flow into private equity and more attention will be paid to this investment sector generally.

There is already a significant number of sustainability funds which have been achieving the level of return that a private equity fund requires (15-20%+ historically). A recent survey by the Cleantech Venture Network, found that cleantech venture capital was involved in 7.4% of all venture capital investments in the USA. Countless new sustainable private equity funds have sprouted up, often started by some of the wealthiest entrepreneurs. The Brenninkmeijer family recently started the Andromeda fund and four other sustainable investment funds, including one devoted to solar energy. The Kadoorie family, one of the wealthiest in Hong Kong, has started a sustainable private equity fund in mainland China. Fenter van Vlissingen has made significant biodiversity investments, as well as wildlife preservation activity in Africa. Recently, one of the more innovative funds was started in France by CDC IXIS, raising only one-third of its equity from the public sector as an interest-free loan.

## Pension schemes and 'dissaving'

There are two significant drivers here. The first is 'dissaving' (withdrawals from funds exceeding inflows) by an aging population, and the second is the high value placed on leading sustainability brands.

If you examine macro-economic conditions with respect to money flows, pension systems and asset classes, it becomes clear that, from 2010 onwards, there will be great difficulties for pension schemes. The rapidly aging population in the developed world means that pension fund outflows will exceed contributions made; pensions funds will therefore not be able to maintain money flows into the stock market as well as meeting payment requirements. This will force

stock prices down; private equity offers one of the few returns to help compensate for the shortfalls in the public equity market.

“Global aging should be positive for the world’s capital markets through 2010. The outlook after 2010 may be less sanguine. We believe that public equity allocations in pension funds have peaked (as a percentage of the total not in absolute terms) in the United Kingdom and are near peak in the United States. ... Although some marginal increases may occur, primarily in international equities, the majority of the reallocation to public equity is complete. Flows into all asset classes should remain positive over the next 10 years. However, the major reallocation of retirement assets into public equities is complete.” (Source: *Global Aging – Capital Market Implications*, Goldman Sachs, 8 February 2001)

Dissaving by governments and individuals could result in high real interest rates and reduced equity returns in many countries with a rapidly aging population. From 2011, baby boomers will begin to retire in large numbers. As individuals receive benefit payments from defined benefit plans, these plans will

have negative cash flows. These outflows should peak between 2030 and 2040. Withdrawals from defined contribution plans and personal pension plans will also occur but at a slower rate and in certain countries, such as the United States, flows could be positive throughout the period.

Dissaving by governments and individuals could result in high real interest rates and reduced equity returns in many countries with a rapidly aging population.

In a study by the World Bank, it was estimated that returns on investment in rapidly aging economies would drop by 200 basis points between 1995-2050.

High prices for CSR champions

The second driver is the high price premium paid by multinationals to purchase brands with recognised high sustainability or CSR (corporate social

responsibility) values. There has been a significant shift in ownership from small independent brands to multinationals over the past five years:

- Ben & Jerry’s was purchased by Unilever;
- Odwalla was purchased by Coca-Cola;
- Celestial Seasonings was purchased by Hain, which was in turn purchased by Heinz;
- Light Life was purchased by Con Agra;
- Powerbar was purchased by Nestlé;
- Cascadian Farm was purchased by General Mills;
- Balance was purchased by Kraft;
- Horizon Organic and Silk were purchased by Dean;
- Stoneyfield Farm was purchased by Gervais Danone.

Extremely high prices were paid for these CSR champions. Purchase prices representing 3.2x sales, ebitda of 28x, and net income of 57x have been quoted. On top of this purchasing frenzy, the food multinationals have been creating many of their own high-

Source: Stocks for the Long Run - The Definitive Guide to Financial Market Returns and Long-Term Investment Strategies, Jeremy J. Siegel

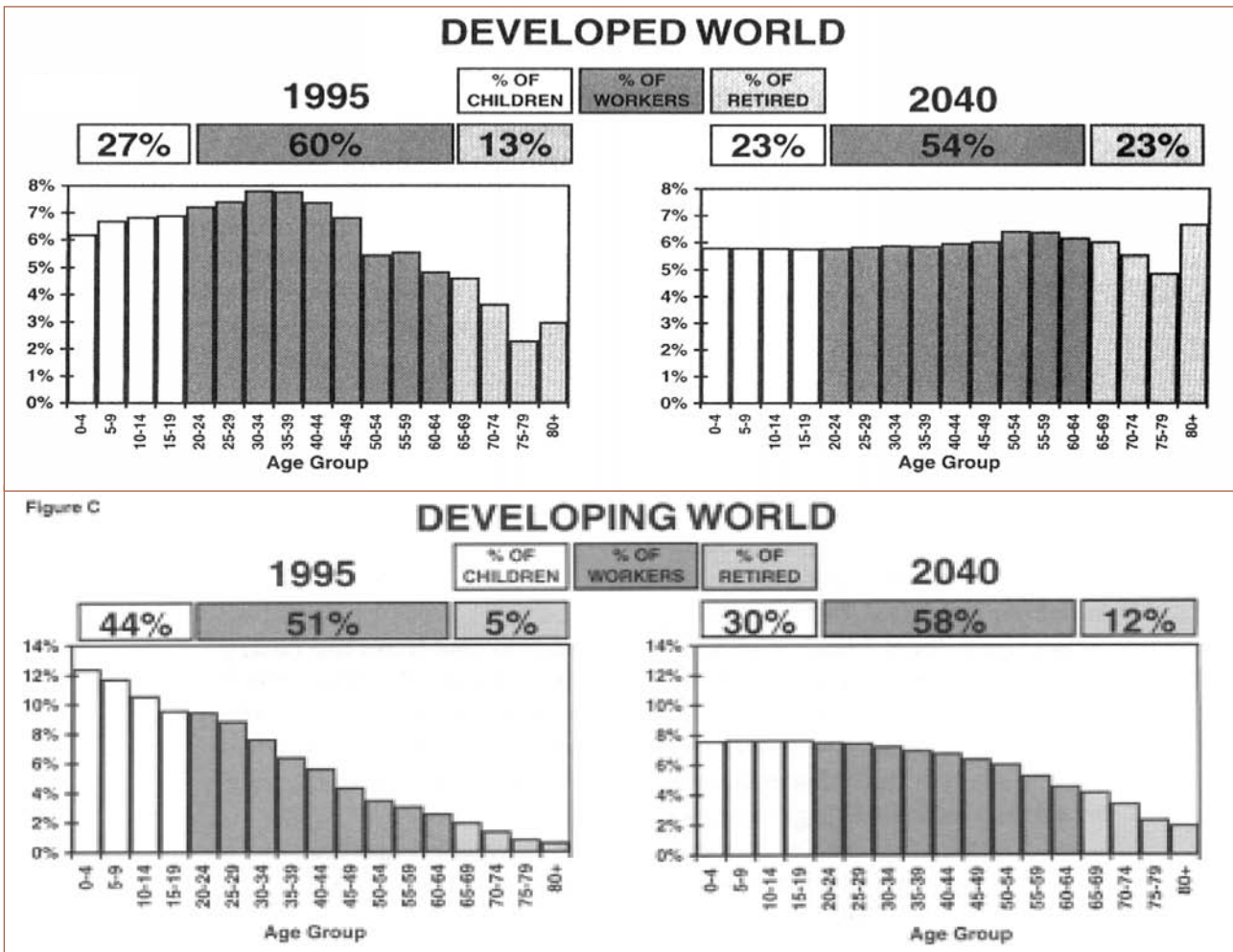


Figure 1. World Population Trends and Pension Flows.

Source: Jeremy J. Siegel (see Figure 1)

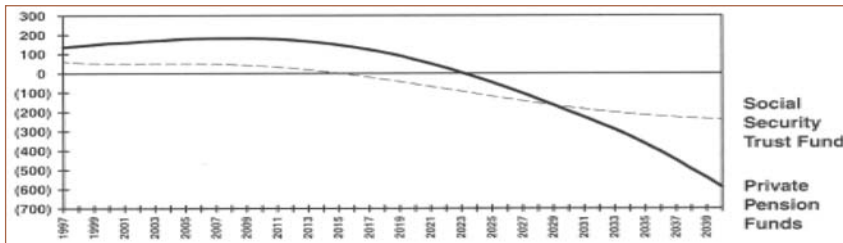


Figure 2. Projected inflows and outflows in US pension funds (Real 1997 US\$ billion).

Source: US Census Bureau, Global Aging - Capital Market Implications, Goldman Sachs 2001

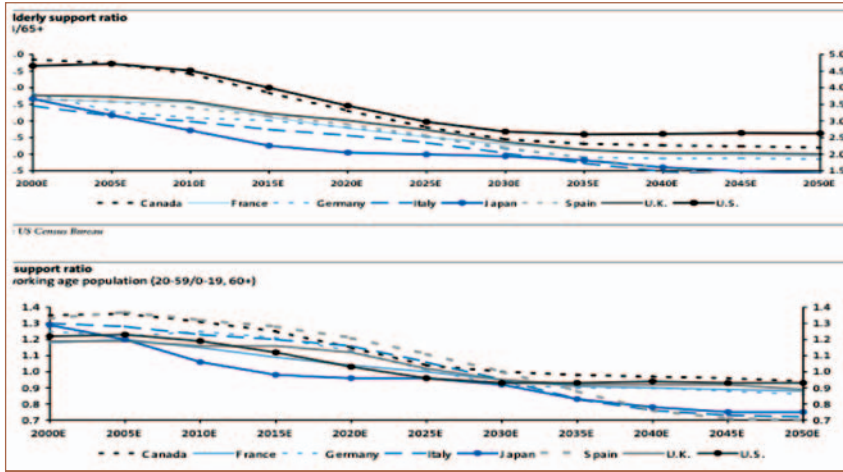


Figure 3. Capital market implications for an aging population.

value natural or organic brands with a high CSR value (source: Gary Hirschberg, Stonefield Farms).

### Growth industries of the future

Nearly all scientific projects predict serious global problems such as global warming and its associated problems, water and oil shortages, congestion and pollution, continuing poverty in the

developing world, and unsustainable development. In a recent study, the Pentagon warned that climate change posed a greater global risk than terrorism. Looking at all the macro-economic signals, industries that seem poised to grow are food production, energy, transportation, health, and new materials. Companies in these fields are focusing on doing less with more and creating more with less. Their focus is

on sustainability, with low resource requirements and energy consumption. Nevertheless, there is still a perception that sustainability does not equal profitability. However, Toyota, for example, has a huge success in its sell-out Prius hybrid fuel car.

### Conclusion

A group such as Robeco that is investing in sustainable private equity is part of a small but growing trend. It is a small but major step that has yet to be fully embraced by the financial sector. I am sure we will see many more to follow. Profit and returns are driving these developments, as investors discover sustainable investment is not philanthropy. It is 'profit-plus investing' – that is, investing to achieve a substantial return with a social and environmental added value. Time will tell how much of a success it will become.

©Robert Rubinstein

#### ABOUT THE AUTHOR

Robert Rubenstein is CEO of TBLI Group and Brooklyn Bridge, both based in Amsterdam, The Netherlands. He has been active in CSR for the past 20 years. During this time he has worked mainly in publishing, creating five different magazines. His last publication, Source, was a management magazine dealing exclusively with CSR. He has been influential in getting CSR into the mainstream of business strategy, by focusing on finance and personnel issues. Mr. Rubenstein has served on various profit and non-profit boards, and advises various organisations, including EU DG Environment (sustainable financial tools), WE-TV editorial advisory board, IMSA (International Sustainability Consultancy), Chairman, Swift Prize of the King Boudewijn Foundation, 3IG-International Interfaith Investment Group, and the Social Adventure Foundation. He is also a commissioner for the State of the World Commission on Globalization.

#### ABOUT THE ORGANISATION

Brooklyn Bridge actively arranges funding for large-scale sustainable projects that will dramatically improve the planetary condition. Brooklyn Bridge is a knowledge broker, specialising in Triple Bottom Line or Social Responsibility. It makes connections for companies and individuals from the old to the new economy, by utilising its extensive global network. The focus is on finance and personnel. Brooklyn Bridge is also the organiser of the TBLI Conference, taking place for the sixth time this year on November 11 and 12 in Amsterdam.

#### ENQUIRIES

Brooklyn Bridge  
 Watteaustraat 36-1  
 1077 ZM Amsterdam  
 The Netherlands  
 Tel: + 31 (0)20 428 6752  
 Fax: +31 (0)20 778 5504  
 E-mail: robert@brooklynbridge.nl  
 Web site: www.tbli.org