Climate change - there are options for investors

Topic of the month November 2015

Global warming is no good news for investors as a whole. The most recent IPCC[1] report predicts an increase in the frequency and intensity of natural disasters (e.g. storms, droughts and floods), which represent significant risks in social and economic terms. Coincidence or not, weather-related events had a negative impact on US growth in the first quarter for the second year in a row.

A growing number of investors are concerned. In September 2014, 360 pension funds and management companies, including Pictet Asset Management, called on governments to sign a comprehensive agreement to limit global warming to 2 degrees Celsius – recognized as the critical threshold by the Copenhagen Accord in 2009 – by the end of the century. The world leaders will meet in Paris in December to work towards a common goal on reducing greenhouse gas emissions.

Some countries have already stated their intentions: the European Union aims to cut emissions by 40% by 2030[2] , the United States by 28% by 2015[3] , and for now Switzerland is leading the way having stated that it intends to cut emissions by 50%. In total, 146 countries representing nearly 86% of global emissions have already stated their commitments, but the announced cuts are not enough. China, which emits more CO2 than any other country in the world, would prefer to reduce emissions per unit of GDP, and therefore continue to increase its total emissions, despite the significant efforts being made in renewable energy. The same is true for India, whose emissions are increasing as a result of new coal plants being built there.

If an agreement on climate change is reached, pressure on fossil fuels – the main source of greenhouse gases – will intensify. If no agreement is reached, a scenario of adapting to climate change should take precedent. Faced with this uncertainty, what should investors do? The IIGCC[4], a forum of over one hundred European institutional investors committed to collaborating on climate change, recently published a guide outlining four options for integrating sustainability in a long-term investment strategy.

- Reduce the carbon footprint of one‘s investments. This can be done by limiting exposure to high carbon-emitting sectors and companies, such as coal power plants, cement and steel. Another approach is to reduce one‘s exposure to companies whose reserves of fossil fuels, such as coal and unconventional hydrocarbons, could become unusable if regulations are introduced. The Norwegian sovereign fund announced that it has halved its exposure to coal producers.

- Increase exposure to the energy transition. According to the International Energy Agency (IEA)[5], investment in renewable energy and energy savings is expected to reach 2.3 trillion dollars annually by 2035. Although wind and solar power can already compete with fossil fuels without subsidies in many parts of the world, advances are still required when it comes to energy storage. Investors have several options: listed shares, infrastructure or green bonds. Although further standardisation is required to maintain investor confidence, nearly 40 billion dollars-worth of green bonds were issued in 2014.

- Limit exposure to environmental unknowns. This refers to assets whose return on investment could become more volatile (e.g. due to greater climate variability) or whose very existence is threatened (e.g. located in flood zones). This means looking at investments in terms of their location and/or level of dependence on other at-risk activities.
- Increasing exposure to solutions to help adapt, such as water treatment and distribution infrastructure or systems to protect against the threats from climate change. According to sources, the investment needs are estimated at 100-500 billion dollars a year by 2050 and offer good opportunities in public/private partnerships, particularly in emerging countries.

The weight given to these four levels will depend on each investor's outlook on the political and energy scenarios for the future. Whatever the outcome of the conference in Paris, two certainties remain: the era of cheap energy is over and adapting to climate threats will require significant changes. All the more reasons to start thinking strategically about the kind of investments one should make and the kind one should avoid

yourSRI - Carbon Portfolio Screener

The innovative and easy to use Portfolio Carbon Screener by yourSRI and South Pole is an online based tool, which allows investors to easily understand their investments' climate impact. The tool helps to minimize climate change related risks and recognize investment opportunities. It also enables climate impact screenings of bond portfolios.

YourSRI.com allows investors to screen any equity and corporate bond portfolio online. On YourSRI.com, the investor simply uploads identifiers and sector weightings and then downloads an investment carbon footprinting report. The analysis includes overall portfolio emissions, sector and detailed company analysis. Moreover, most sustainable mutual funds can be found pre-screened for their carbon footprint on YourSRI.com. Finally, the tool also calculates an overall cost of externalities and allows for automatic emission reductions in developing countries.

YourSRI.com is endorsed by the Montreal Pledge to used by investors for reporting their greenhouse gas emissions. More information: yourSRI Fact Sheet

Footnote and References:

1) *Intergovernmental Panel on Climate Change, 2014*
2) *From 1990 levels*
3) *From 2005 levels*
4) *Institutional Investors Group on Climate Change - www.iigcc.org*
5) *World Energy Investment Outlook, 2014*

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