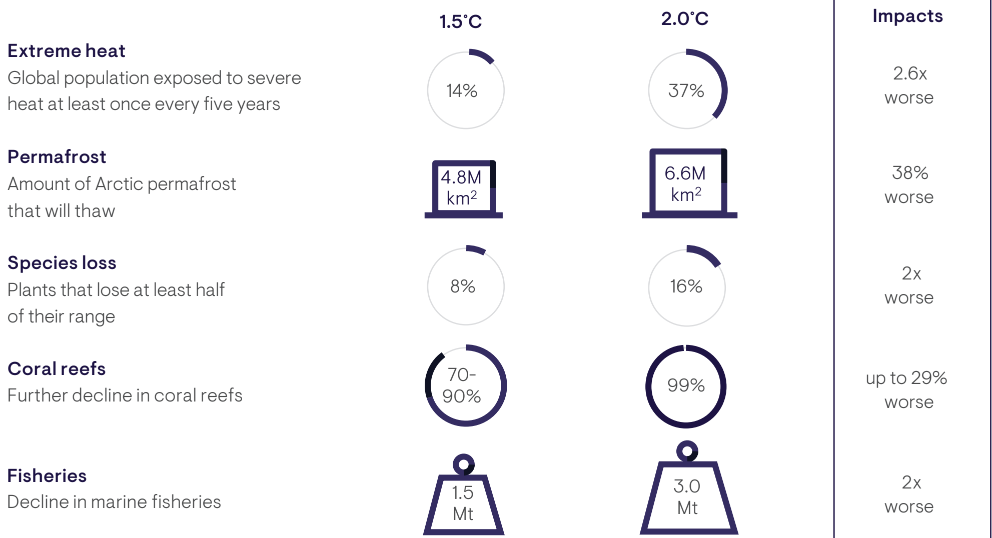
HKRSA 香港退休計劃協會
The Hong Kong Retirement Schemes Association
PREMIER SPONSOR ARTICLE SERIES
Jun 2020

Climate changing for asset owners

Climate change is one of the greatest tests ever faced by humanity. According to the Intergovernmental Panel on Climate Change (IPCC), the UN body for assessing climate science, we have until just 2030 to radically reduce carbon emissions if we are to limit global warming to the critical level of 1.5ºC above pre-industrial temperatures.

It is vital that asset owners address climate risk (or ensure that asset managers do so on their behalf). This means integrating carbon analysis into investment research and decision-making, and assessing both the transition risk associated with a shift to a decarbonised economy, and the physical risk posed by climate change itself.



A central role for asset owners

Asset owners have long-term liabilities, which makes them particularly subject to the long-term challenges facing society and the planet, including climate change. Many of them already consider environmental, social and governance (ESG) factors to be important – as evidenced by the fact that at the end of 2019 there were over 2,300 signatories, including 432 asset owners[1], to the UN-backed Principles for Responsible Investment (PRI), the first of which states that institutional investors should incorporate ESG issues into investment analysis and decision-making[2].

But signing up to the PRI is not an end in itself. The opportunity is to turn this commitment into meaningful action on climate risk. Some of this is being forced on asset owners by regulators and governments, but much must come from asset owners themselves.

1. Pension funds

The stewards of long-term retirement assets have led the way in integrating ESG issues over the past few decades (pension funds founded the PRI). But they can do more. For example, in the UK, just 5% of the top corporate pension funds have developed and implemented a climate-change policy by the end of 2018[3]. Globally, the Asset Owners Disclosure Project[4] (AODP) assessed the world's 100 largest public pension funds and found that:

— Climate-change related risks are largely unidentified and unassessed by global pension funds.
— The vast majority of pension funds are failing to align with the Paris agreement.
— Around half of global pension funds undertake company engagement on climate change.

2. Sovereign wealth funds

Sovereign wealth funds (SWFs) are state-owned investment funds that typically invest globally across all of the main asset classes and instruments. Total SWF assets under management are some US$8.1 trillion[5], but just 1% of this is estimated to be allocated to 'green finance' assets. Nevertheless, over the last 10 years SWFs have increased their focus on climate change, spurred particularly by the 2015 Paris Agreement, under which signatory nations are determining their own plans to achieve climate targets. In 2018, six SWFs representing US$3 trillion[6] agreed to a climate-change charter, which commits them to investing in companies that factor climate change into their strategies. They also committed to publishing data on how they are reducing their own carbon footprints.

3. Insurers

Insurers are at the front line of climate change and have been active in researching and mapping it longer than perhaps any other industry. According to Swiss Re, climate change is a key driver of "a 'new normal' of higher-frequency, more severe localised natural disasters, many related to extreme weather, that are causing ever greater damage"[7]. In 2018, economic losses from natural disasters amounted to US$155 billion[8], the fourth-highest total ever despite no major single event during the year.

In the life insurance sector, where providers' liabilities can stretch for generations, many insurance companies have tilted their portfolios towards sustainable investments, including renewable energy. But this vast pool of assets, around US$1.9 trillion[9] , could be directed far more effectively towards addressing climate risk.

Invest positively to hedge against climate change

In many ways, asset owners have led efforts by the investment community to address climate risk, aiming to fulfil both their duty to savers and their wider responsibility to society and future generations. But is there more they can do?

Efforts to manage the portfolio impacts of climate change still tend to focus on mitigating risks, avoiding carbon sectors (i.e., divesting) and applying ESG screens. In our view, there is a significant opportunity that is largely untapped: investing in positive action on climate change – that is, allocating capital to companies and projects that are enabling the massive transformation that must be undertaken to shift the global economy to a lower-carbon model. Doing so will not only benefit society by helping to accelerate decarbonisation; it may also help to offset portfolio-level climate risk and provide exposure to an area of long-term structural economic growth.

The fact is that the world still has a massive task ahead to transition from today's unsustainable economy to one based on cleaner energy and transport, more efficient industrial production and more energy-efficient buildings.

With swathes of economic activity on hold during the pandemic, decarbonisation may be delayed in the near term. But given the still-urgent need for climate action, we see no change in the mid- to long-term potential growth drivers of select businesses across all three pathways to a more sustainable, lower-carbon economy: renewable energy, electrification and resource efficiency. In a growth-challenged world, that may prove a lifeline for asset owners.

Endnotes

[1] Source: PRI 2019 data
[2] Source: unpri.org
[3] https://www.professionalpensions.com/news/3065751/climate-change-policy-adopted-corporate-pension-funds
[4] Source: Asset Owners Disclosure Project, 2018
[5] https://www.swfinstitute.org/sovereign-wealth-fund-rankings/
[6] Norway, Kuwait, Qatar, Saudi Arabia, United Arab Emirates and New Zealand
[7] Source: Swiss Re, Dec 2019
[8] https://www.swissre.com/media/news-releases/nr_20181218_sigma_estimates_for_2018.html
[9] https://www.statista.com/statistics/784971/uk-insurance-companies-by-total-assets/

Source: Ninety One

Important information

This document is for information and general circulation only. It does not have regard to the specific investment objectives, financial situation and particular needs of any specific person who may receive it. Any opinions stated are honestly held but are not guaranteed and should not be relied upon. It does not constitute investment advice, or an offer to sell, or a solicitation of an offer to buy any security, investment product or service. In Hong Kong, this document is issued by Ninety One Hong Kong Limited and has not been reviewed by the Securities and Futures Commission (SFC).

Source: Ninety One

About HKRSA

The Hong Kong Retirement Schemes Association (HKRSA) was established in 1996 to promote the interests and best practices of retirement schemes in Hong Kong including provident and pooled retirement funds. The HKRSA is a not-for-profit, non-political association, which represents retirement schemes and their members, providing a forum for discussion of issues of current and topical interest.

About Ninety One

Ninety One, previously Investec Asset Management is an independent global asset manager dedicated to delivering compelling outcomes for its clients, managing £103.4bn in assets (as at 31.03.20). Established in South Africa in 1991 almost three decades of organic growth later, we offer distinctive active strategies across equities, fixed income, multi-asset and alternatives to institutions, advisors and individual investors around the world.

Disclaimer

This document is intended to be for information purposes only and it is not intended as promotional material in any respect. It does not constitute any solicitation and offering of investment products. The views and opinions contained herein are those of the author(s), and do not represent views of the Hong Kong Retirement Schemes Association (the "HKRSA"). The material is not intended to provide, and should not be relied on for investment advice or recommendation. Information herein is believed to be reliable, but the HKRSA makes no guarantee, representation or warranty and accepts no responsibility for the accuracy and/or completeness of the information and/or opinions contained in this document, including any third party information obtained from sources it believes to be reliable but which has not been independently verified. In no event will the HKRSA be liable for any damages, losses or liabilities including without limitation, direct or indirect, special, incidental, consequential damages, losses or liabilities, in connection with your use of this document or your reliance on or use or inability to use the information contained in this document. This document has not been reviewed by the SFC. Any link to other third party websites do not constitute an endorsement by the HKRSA of such websites or the information, product, advertising or other materials available on those websites and the HKRSA has no responsibility for the accuracy or availability of any information provided by linked websites.