ShareAction»

Laying the Track: The Race to Zero

The role of asset managers in tackling the climate crisis

Led by the UNFCCC Champions for Climate Action, the global "Race to Zero" campaign aims to rally leadership from investors for a resilient, zero-carbon recovery that unlocks sustainable growth. This is the first in a series of briefings that will outline how we can lay the track for the financial services sector to reach net-zero by 2050.

This briefing sets out key issues on how the asset management industry is responding to the climate crisis. It aims to shine an independent spotlight on the state of play in the industry and sets out how policymakers should regulate to move investors in the right direction. The picture that emerges, while indicating a rising awareness of climate change as a financial risk, falls well short of what is needed to achieve net zero by 2050[1].

Climate-related policy commitments

The issue

Just over half of asset managers make formal climate-related policy commitments but only a small percentage adopt concrete measures around analysis and decarbonisation of their portfolios.

The details

While climate-related policy commitments are broadly used across the investment industry, few asset managers have committed to specific investment measures that address climate change.

61 per cent of asset managers reference climate change in their publicly available investment policies. However, only 35 per cent have committed to invest in low-carbon opportunities

1 This briefing is a distillation of the Point of No Returns III – Climate Change report which surveyed 75 of the world's largest asset managers. https://shareaction.org/wp-content/uploads/2020/06/ShareAction-Climate-Report-III-Final.pdf

to align with the low-carbon transition, and just 16 per cent of asset managers have a coal exclusion policy for all portfolios under management.

Scenario analysis allows asset managers to explore how climate-related risks impact portfolios over time. However, the use and incorporation of scenario analysis into corporate strategy decision-making is inconsistent and insufficient.

35 percent of asset managers have conducted scenario analysis and only 15 per cent showed evidence of integrating scenario analysis into their company-wide strategy formulation processes.

The barriers

Persistent short-termism means that the majority of asset managers are not taking concrete action to conduct scenario analysis and decarbonise their portfolios.

Our recommendation is for Governments and regulatory authorities to introduce mandatory climate-related disclosures in line with TCFD recommendations for asset managers, companies and asset owners, and develop guidance on complying with the disclosures[2].

Prioritising action-focused engagement

The issue

Investor engagement on climate change focuses on the disclosure of climate-related risks, while action-focused engagement remains low.

The details

Asset managers' engagement with investee companies focuses on encouraging them to disclose climate-related data, rather than take action to address climate change. Some of the world's most polluting companies stand out in terms of their compliance with disclosure best practice (e.g. 100 per cent of FTSE 100 electricity, gas and oil companies are fully aligned with TCFD recommendations).

Focusing on disclosure as a priority for engagement means that asset managers are less likely to prioritise action-focused engagement, inhibiting the impact they could have on climate change. 75 per cent of asset managers declared disclosure in line with TCFD recommendations as one of their top five engagement priorities but only 44 per cent state

2 NB this recommendation is merely a first step: necessary but not sufficient. Companies and asset managers need to assess and disclose climate-related risks and opportunities to ensure that they are priced in by financial markets. To ensure that we reach net-zero by 2050, it is crucial that governments ensure that companies and investors become Paris-aligned.

that corporate strategy alignment with a <2C scenario is among their top five engagement priorities.

Equinor 2019 Case Study

86 per cent of those who voted against the proposal at Equinor to set and publish emission targets had stated their company engagement priority was emission reduction[3].

The barriers

Climate-related risks take a long time to materialise, so the effects of action-focused engagement might also take a long time to appear. Commercially driven asset managers are not currently incentivised to take into account such time horizons.

Our recommendation is for the Financial Reporting Council to continue engaging strongly with asset managers and encouraging them to become signatories of the new Stewardship Code. The new Code prioritises action-focused engagement with companies to inform long-term investment decisions.

International policymakers should encourage asset managers to make public commitments to action-oriented engagement, by setting clear expectations on climate-related issues with investee companies, through regulation or voluntary codes.

Climate-related risks and impacts in investment portfolios

The issue

When describing climate-related risks in connection with investment portfolios, most asset managers focus on the financial risk that climate change poses for investments. Less consideration is given to the climate-related impacts of investments.

The details

57 per cent of asset managers identify some of the climate-related impacts of their investments, with this largely limited to ESG or sustainably labelled funds. When impacts of investments are described, 53 per cent of asset managers focus solely on positive impacts.

3 For more information on this case study see page 23 of the Point of No Returns III – Climate Change report. https://shareaction.org/wp-content/uploads/2020/06/ShareAction-Climate-Report-III-Final.pdf

Only 27 per cent of asset managers give a balanced account of both negative and positive impacts of their investments.

Focusing only on climate-related risks in terms of the financial risk they pose to investments in the short term means that asset managers are less likely to consider the climate-related impacts their investments have on the environment and society. Asset managers have a better chance of fulfilling their fiduciary duty if the impacts of their investments are well understood and accounted for.

The barriers

A key barrier is that regulators have historically framed climate change in terms of individualised risks, meaning that investors tend to think about adaptation rather than mitigation.

Our recommendation is to introduce legislation requiring companies, asset owners and asset managers to report on how they are aligning their portfolios with the Paris Agreement goals.

In the UK, this would involve the Department for Business, Energy and Industrial Strategy, the Department for Work and Pensions, the Treasury and the Financial Conduct Authority, working collaboratively together to create a consistent mandatory reporting framework.

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ShareAction is a UK registered charity working globally to lay the tracks for responsible investment across the investment system. Its vision is a world where all finance powers social progress.