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welcome to brighter

shifting to green:

Planning your portfolio's transition to a low-carbon future

One big systemic risk - the global COVID-19 pandemic - is all most people want to experience in a lifetime. But another one looms right ahead of us: climate change, which, if left unchecked, will also massively disrupt the global economy, communities and quality of life.

Scientists tell us that we are running out of time. We are headed to an increase of 2°C in average global temperatures[1], which would result in temperatures never before experienced by humankind. This increase radically raises uncertainty: storms, wildfires and natural catastrophes will occur with greater frequency and with even more catastrophic results for economic and community stability.

For any investor with a long-term view – like a pension fund, large or small – this systemic risk is too great to ignore. This degree of uncertainty puts a pension fund's ability to deliver against its commitments in jeopardy.

But for every downside risk, there is an opportunity that can be seized. Increasingly, Canadian institutional investors are committing to integrate climate change and environmental, social and governance (ESG) factors into their investment practices. This includes not only universities[2], but also many of the country's largest pension plans[3] — who recently called on corporations to adopt greater transparency in their Environmental Social and Governance (ESG) disclosures.

From Biden to Trudeau, from Paris to Ottawa, it is becoming clear: the time to act is now. It is no longer a question of "if" investors should address and integrate climate change.

It is now a question of "how": how you can mitigate these risks, how you can seize these opportunities, how you can create a climate plan.

[1] Mercer. Investing in a Time of Climate Change – The Sequel, 2019. https://www.mercer.ca/en/our-thinking/wealth/climate-change-the-sequel.html

[2] Investing to Address Climate Change: A Charter for Canadian Universities https://sustainability.utoronto.ca/wp-content/uploads/Investing-to-Address-Climate-Change_18-June-2020.pdf

[3] In unprecedented move, Canadian pension funds unite to call for greater ESG standards https://www.thestar.com/business/2020/11/25/pension-fund-mangers-call-for-strengthened-esg-disclosure-by-companies.html

A green shift

The Bank of Canada's Tiff Macklem recently stressed the urgency[4] for business and investors to become more climate-smart - not only to mitigate the threats but also to capitalize on the opportunities afforded by the impending transition to a low-carbon world.

Across the globe, policy makers are moving on climate change.

Given regulatory momentum to cap emissions, shifts toward new technologies and business models many investors are beginning to map a climate transition plan: a plan to assess portfolio holdings and companies' ability or capacity to transition toward limiting global emissions and how well-positioned they are for the low-carbon economy.

Moreover, make no mistake – the transition to a low-carbon economy is already underway[5]. Consider how technology has driven down the cost of renewables. In just ten years[6], from 2009 to 2019, the price of solar energy has decreased by 83%, and the price of offshore wind energy has decreased by 51%. These declines will continue. Green energy is no longer just the right thing to do – it is often the smart thing to do. Shifts are underway also in how we design our buildings, cities, infrastructure and grow our food all with a lens to a lower carbon world. A fundamental shift in the way we live, work and consume is underway. Investors must be armed with the information they need to better position their portfolios for this shift – so that they can better see the risks and the opportunities a lower-carbon future holds.

[4] Bank of Canada warns climate change will have profound impact on economy https://financialpost.com/news/economy/bank-of-canada-says-canada-must-move-quickly-to-tackle-climate-change-risks

[5] See the United Nations Framework Convention on Climate Change (2015) Paris Agreement. In October 2018, the Intergovernmental Panel on Climate Change (IPCC) released a report on 1.5°C and the difference between that and 2°C to illustrate the additional impact that 0.5°C is expected to have and why the Paris Agreement ambition for "well below" 2°C is warranted.

[6] Global Trends in Renewable Energy Investment 2020 https://www.fs-unep-centre.org/wp-content/uploads/2020/06/GTR_2020.pdf

A time to ACT

Mercer's Analytics for Climate Transition (ACT) draws on Mercer's ten years of experience assessing climate risks and opportunities to generate a holistic, portfolio-wide assessment of climate risk. By applying several different types of analysis, it segments assets into "grey" assets — those that generate high emissions and have limited capacity for transition, "green" assets — those with low emissions, including the solutions to the net-zero transition, and everything in-between.

This analysis provides investors with a portfolio-wide view of the emissions reduction needed to meet a net zero target and to plan the portfolio changes required in order to transition. The results are intended to help investors assess where emissions reductions could come from, compare different strategies, engage with asset managers and companies, plan for and make portfolio changes to reduce emissions.

Planning for every scenario

Mercer's ACT solution looks to align portfolios against a scenario where global temperatures are capped to a 1.5°C rise on pre-industrial levels. This is an ambitious climate target, but one the signatories of the Paris climate accords are striving to meet.

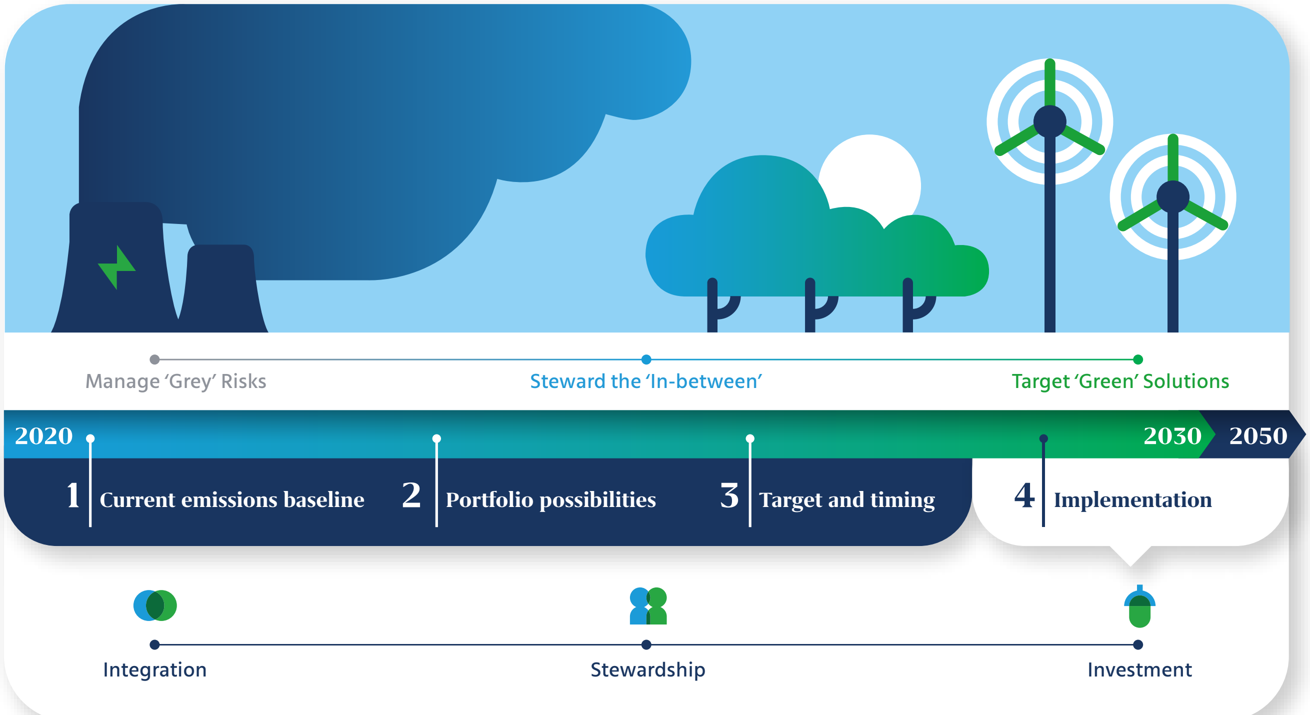
Whatever scenario you believe is most likely, you need a plan. And that plan begins with understanding where emissions are generated now and what capacity companies have to transition and keep ahead of industry and regulatory changes.

A transition plan takes investors through a process that includes:

- Setting current emissions baselines
- Mapping the transition capacity of current holdings
- Assessing portfolio opportunities for emissions reductions
- Setting targets for reduction milestones
- Developing implementation plans that can be integrated within strategy, active engagement and portfolio construction decisions

At Mercer, we believe that strategic transition planning should also recognize short-term flexibility where needed and keeping in mind that some asset classes will take longer to transition than others.

Mercer's Transition Framework



Source: Mercer

Ultimately, a plan to transition requires a comprehensive approach to risk and opportunity. It must go beyond just identifying one-off "green" investments and instead take a total portfolio approach to a low-carbon world.

A Canadian and Global imperative

As highlighted by the Canadian Expert Panel on Sustainable Finance, Canada has a strong, diversified and resource-rich economy; a world-leading financial sector; and excellent capacity for innovation. By harnessing these advantages Canada can be a leader in the global transition to a low-emissions future[7].

Canadian investors, in particular, have much to gain from this type of analysis. There are many developments underway as the Canadian government makes stronger commitments to emissions reductions, and applying a climate lens to many areas of public policy. Large businesses applying for COVID-19 relief, for example, are required to conduct climate scenario analyses[8].

Efforts are also ongoing internationally. Beyond the Paris climate accords – to which Canada is a signatory, - the United Nations campaign to aggregate commitments to achieve net zero carbon emissions is gaining momentum. As part of this global effort, hundreds of countries, cities, universities, companies and investors (representing over $5 trillion AUM in USD[9]) have committed toward a net zero carbon emissions target.

To meet climate challenges it is anticipated that there needs to be more investments in infrastructure. This presents an opportunity for Canadian firms and investors. Pension funds and firms with deep expertise in infrastructure, for example, can help develop the infrastructure that will be needed to transition Canada and the globe toward a low-carbon and climate resilient future. This is not limited to energy. Opportunities abound in transit systems, building design, food production and natural resource management, to name a few. The opportunity is there for Canadian firms and investors to grasp.

The direction the world is going is clear. Organizations of all sizes, and governments across the world, are working to reduce emissions and make a low-carbon future a reality.

This is a fundamental change in production and consumption. Every investor with a long-term view would do well to pay attention to these trends.

The time for waiting is over. The time to act is now.

[7] Final Report of the Expert Panel on Sustainable Finance - Mobilizing Finance for Sustainable Growth https://www.canada.ca/en/environment-climate-change/services/climate-change/expert-panel-sustainable-finance.html

[8] Prime Minister announces additional support for businesses to help save Canadian jobs https://pm.gc.ca/en/news/news-releases/2020/05/11/prime-minister-announces-additional-support-businesses-help-save

[9] United Nations Race to Zero Campaign https://unfccc.int/climate-action/race-to-zero-campaign

Reshaping the future.

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With more than 70 years of experience, we provide trusted advice and solutions by understanding data and applying it with a human touch. We drive change by turning ideas into action, positioning our clients, colleagues, and communities for the future.

How We Can Help

Continuously rethinking purpose and priorities drives HR transformation. Shaping the future of work requires improved strategies around investment and retirement, health and wellness benefits, talent and communications. We believe in the value of investing in the future to build resilience for your business and your employees.

Investments and retirement require sophisticated solutions. We approach these with a big picture view that prioritizes long term financial wellness. We offer research and advice on assessing risk and designing benefits programs while keeping in mind the need to optimize throughout changing times.

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