



Thinking Ahead Institute

INNOVATION CONVERSATION

Date: 30 November 2023

Topic: The focused small-group discussion revolved around climate-related matters, encompassing significant topics including climate transition, net-zero scenarios, tools for scrutinising climate scenarios, the examination of climate issues from both macro and micro perspectives, challenges associated with managing climate risks, and the pivotal role of asset owners and managers in fulfilling net-zero commitments, among other pertinent subjects.

Participants:

Caro Herrera Augusto – Santander Asset Management
Edward Evers – Ninety One UK Limited
George Beesley – MFS Investment Management
Herschel Pant – AXA Investment Managers UK Limited
Paul Brain – Newton Investment Management Limited
Peter Scaturro – S&P Dow Jones Indices LLC
Piers Lowson – Baillie Gifford & Co
Rowan Stone – Atomos Wealth
Sigrid Smith – Newton Investment Management Limited
Tim Hodgson – Thinking Ahead Institute

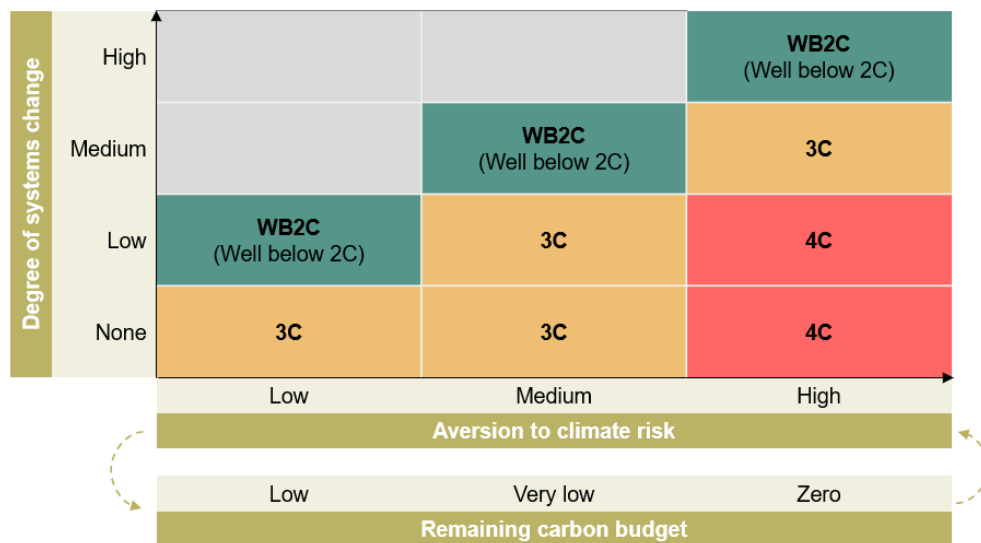
Introduction

- In TAI's paper titled [Pay Now or Pay Later?](#) we distilled various climate scenarios into a binary choice: a 1.8°C transition ('pay now') or a 2.7°C status quo ('pay later'). The Investing for Tomorrow (IFT) Macro Working Group, TAI ran this year, extensively examined this framework, addressing issues such as the economic transition under the current rules of the game and the accuracy of incentives.
- Current net-zero scenarios | the net-zero scenarios from organisations like IEA and NGFS are 'priced to perfection' (everything needs to proceed in an orderly manner, with no mistakes), but only offer a 50/50 chance of successfully limiting global warming to 1.5°C.

Climate matrix and scenario exploration

- Climate matrix | TAI has introduced a two-dimensional matrix that includes dimensions for the degree of systems change and climate risk. The matrix advocates for considering a broader range of scenarios due to uncertainties in predicting future conditions. It also underscores the significance of considering potential shifts in society's tolerance for climate change and organisations' aversion to climate risk.

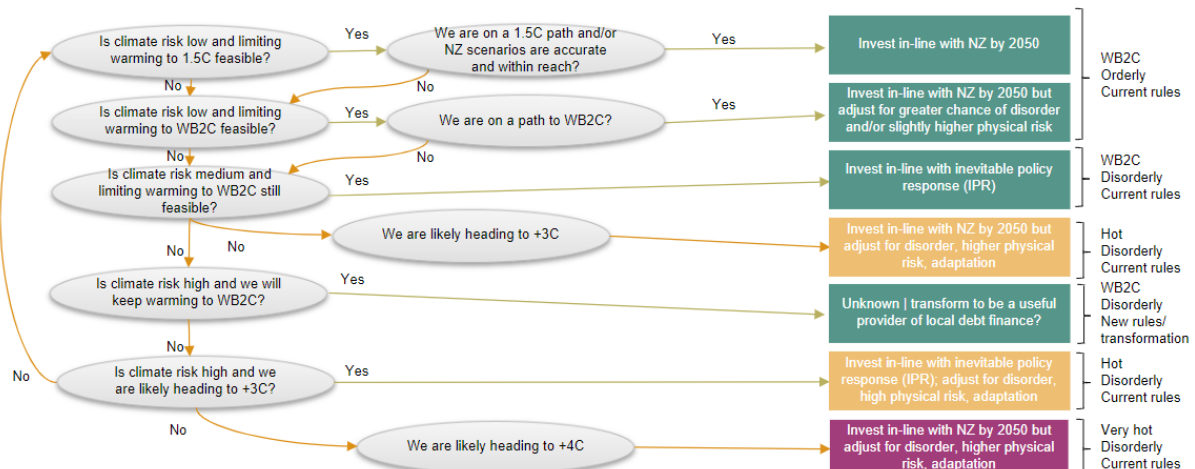
Long-term scenarios reconstruction



- Other tools for scenario exploration | TAI has also developed other decision-making tools, including a decision tree and hypothesis testing process. These tools are designed to help explore various scenarios, connect long-term projections with short-term decision-making, and provide insight into future changes that could impact investment portfolios.
 - The decision tree poses a series of 'yes/no' questions leading to different end points.

Scenario decision tree

Answer twice – for the market and for you



- Macro vs micro perspective | the micro-level approach is helpful for organisations to deal with their micro-level emissions and contributions. While, the macro-level work is crucial for improving our understanding of the big picture, emphasising the urgency of the climate issue and the need for immediate action. It is also instrumental in guiding decisions related to asset allocation and addressing the pressing nature of the climate crisis.

Discussion around the climate challenges

- View on macroeconomic situation | it is important to consider the macroeconomic situation and geopolitical events, and revise targets accordingly. Especially, people should take the energy cost, efficiency and scalability of carbon capture and storage into consideration.

- Responsibility of asset managers | several effective approaches have been implemented to attain the net-zero target and address climate risks. Nevertheless, challenges arise in acquiring accurate data, particularly within developing regions. Hence, active participation in collaborative initiatives, pinpointing companies for focused attention, and employing engagement as a pivotal strategy are crucial steps toward achieving net-zero commitments.
- Climate investment solutions | providing clients with climate investment solutions is an important focus for investment organisations. Hence a lot of effort is put into developing capabilities, both internally and in collaboration with third-party funds, to create a diverse range of strategies. This approach aims to provide customers access to portfolios and investment strategies prioritising transition. Engagement in climate initiatives is also important for strengthening collaboration through joint actions and interactions with regulatory bodies.
- Misalignment between universal owners and corporate boards | there is a misalignment between the fiduciary duty of corporate boards, which is exclusive to the corporation, and the broader interests of universal owners who seek sustainable and long-term value across a diverse portfolio of companies. The universal owner might identify certain actions that could compromise a corporation's long-term financial prospects but would yield advantages to other holdings in their portfolio. In such cases, getting corporate boards to prioritise broader concerns such as social and environmental impacts become challenging for universal owners.
- Fiduciary duty and climate objectives | it would help to expand the intersection between fiduciary duty and climate objectives, with an emphasis on balancing financial returns and societal impact.
- Potential gaps | potential gaps between net-zero pledges and the evolving global reality underscore the importance of rapidly and effectively decarbonising. This urgency is crucial to prevent a widening gulf between commitments and tangible progress. It necessitates active participation from governments, the financial system, and asset managers.

Science-Based Targets Initiative (SBTi)

- Concerns about SBTi | while acknowledging the importance of science-based targets (SBTs), concerns arise regarding their effectiveness. There is a question about the application of SBTs and their adequacy in addressing uncertainties in climate science, particularly concerning the wide range of potential warming values of equilibrium climate sensitivity (ECS).
- Risk management perspective | advocates for a risk management perspective, suggesting a need to assume that warming could be higher than officially documented.
- Assumptions in climate scenario analysis | the discussion delves into the macro-level assumptions essential for science-based targets (SBTs), encompassing elements like orderliness, coordination between sectors, and perfect foresight. However, there is expressed uncertainty regarding the extent to which SBTs incorporate these macro-level assumptions into their frameworks.

About the Thinking Ahead Institute

The [Thinking Ahead Institute](#) is a global not-for-profit member organisation whose aim is to mobilise capital for a sustainable future. The Institute's members comprise asset owners, investment managers and other groups that are motivated to influence the industry for the good of savers worldwide. It has around 60 members with combined responsibility for over US\$16 trillion and is an outgrowth of WTW's Investments' Thinking Ahead Group.