



Building a climate focused portfolio

Thursday 27 January

The asset management industry continues to evolve dramatically in the environmental, social and governance space. In this session Rt Hon Amber Rudd, former Secretary of State for Work and Pensions, Jihan Diolosa, Head of Responsible Investing at Russell Investments, Emily Steinbarth, Senior Quantitative Research Analyst at Russell Investments, and Debbie Fisher, Deputy Head Clwyd Pension Fund at Flintshire County Council Deeside, look at the objectives that schemes should consider when building a climate response focused portfolio.

The politics of climate change and where its headed

A political consensus on climate change has emerged in Europe. In the U.K., most of the key moves to put in legislation on the environment have had bipartisan support - as far back as 2008, the Climate Change Act was supported by both Labour and the Conservatives. Investors can be assured therefore that the direction of travel on the environment is fixed. The same cannot be said, unfortunately, about the U.S., with President Trump's decision to pull back from the Paris Climate Accords casting doubt on the country's commitment to combating climate change.

The challenge for political leaders in introducing radical green policies is in bringing public opinion with them, especially against the backdrop of rising energy prices. With mounting pressure to reduce bills for households, the temptation is to pull back on the climate agenda. This would be a mistake in the long term, as it will be renewable alternatives which provide reliability, consistency, and help to keep costs down into the future.

Did COP26 make a difference?

The Paris Climate Accords in 2015 was the first agreement of its kind, signaling a clear course for world leaders and businesses alike. Last's year's COP26 in Glasgow built on that success. While critics say that it did not go far enough, important progress was made. One significant difference between Paris and Glasgow was the motivation of the broader public. The language of climate change has entered the public vernacular. Ordinary people aren't just seeing the effects of global warming in the science, but they are seeing it in the world around them, with droughts, fires, and the mass movement of people.

Boardrooms have taken notice. Big business was present in Glasgow, from bankers to pension fund managers. There is an understanding now of the need for the private and public sectors to collaborate and realise the opportunities presented by the move towards green energy. By leveraging the expertise and resources of corporations alongside the initiatives of world governments, investors can take confidence that practical solutions are forthcoming.

Race to Net Zero: the role of pension funds

The growing public interest in climate issues puts pressure on fund managers. Increasingly, scheme members and the wider community will make contact and encourage divestment from companies and industries which do not align well with environmental or social causes. The difficulty for asset managers is how best the effect change in the companies they invest in and ease uncertainty at the corporate level. Another hurdle is assessing the volume of options on the table when it comes to sustainable equities and defining exactly what we mean by 'sustainable'. The challenge - translating broad global targets into discrete portfolio decisions - is significant. Much of the complexity stems from the inconsistent use of metrics, and decisions around how much leeway to allow in a given portfolio (e.g. do you allow for geographical or sectoral differences?).

Nevertheless, the need for pensions funds to play their part in achieving Net Zero is unambiguous. There is an abundance of resources available to help educate managers on best practice, while frameworks like the Institutional Investors Group on Climate Change (IIGCC) and the Science Based Targets initiative (SBTi) can provide additional guidance.

The journey towards investing more responsibly

Not every company in a portfolio will be aligned on ESG issues. Engagement with business leaders is key in shifting their thinking. Divestment for bad practice may not work, but an approach that favours dialogue and education is likely to build consensus and get results. In addition to engaging with existing companies within a portfolio, fund managers should seek out opportunities with new technologies that will help to take carbon out of the atmosphere.

While the scope of the challenge is enormous, there is no need to go it alone. Investors starting on their ESG journey should consider working closely with like-minded consultants and take professional advice. Setting a suitable roadmap is a great first step. But then comes the really hard, and exciting, part: implementation of the strategy.

Important information

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