Turning the Tide

The urgent need to shift capital flows to climate solutions:
a case study of ten fund management companies.

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Executive Summary

The finance sector risks undermining the goals and ambitions of the Paris Agreement on Climate Change. If practices are not addressed, the sector may contribute towards a 4–6°C increase in global temperatures by the end of this century, far above the 2°C goal set as the absolute maximum in order to avert disastrous climate change impacts on people and planet. Although Swedish stakeholders are the focus of this study, the findings should be seen as an indication of a challenges that likely exists globally.

This study presents the results from a climate survey and a portfolio analysis of Sweden's ten largest fund management companies, that invest retail and institutional clients' assets in global stock markets. It investigates what actions are taken to bridge the global gap in green investments and fulfil the goals of the Paris Agreement. Climate change is one of the greatest human rights challenges of our time. Still, the study shows that coal power companies, which remain in the fund management companies' investment portfolios, are planning to expand their capacity. At the same time, renewable power companies' capacities are, based on projections, expected to level out over coming years.

To avoid some of the worst effects of climate change, 195 states committed in 2015 under the Paris Agreement to keep the rise in global temperatures this century well below 2°C and pursue efforts for 1.5°C. The agreement clearly designates an important role to the finance sector. There is a need for investors to direct capital flows to zero-carbon investments, innovation and climate solutions, and to pressure fossil fuel and deforestation industries to transform their business models.

This report compares results from a similar survey conducted by Swedwatch in 2015. Principal findings show that:

• Many investors have increased their climate efforts. There is some progress in the form of increased investments in green bonds from earlier low levels, and some of the investors are preparing to carry out scenario analysis in line with voluntary G20 recommendations. In one instance, climate-induced human rights impacts are being translated into business risk. However, given the urgent need for concrete climate transition results, the ambitions and actions of the fund management companies are not sufficient.

• The investors included in the study have not set any targets for reallocation of capital from investments in fossil production to investments in green finance and climate solutions for mitigation and adaptation. Across the board, climate solutions are almost exclusively found in niche funds, which make up only a fraction of the total investments. Some investors deferred responsibility for choosing to invest in climate solution to clients.

• A majority of the fund management companies state that they are actively engaging with companies, policy-makers and large financial actors in order to, for example, decrease greenhouse gas emissions and encourage better climate reporting as well as transition to low carbon business models. However, only a handful report concrete targets, timeframes or results from these efforts.

• The fund management companies explain that the reasons for not reallocating substantial capital is that they are protecting the value of their clients' investments, and that climate risks are not considered in today's short-term financial markets. Further, they refer to a current lack of green projects and climate solutions to invest in. Regarding the lack of targets and disclosure on their investments' impacts on climate, forests and human rights, they describe that the challenge is that companies are not measuring and reporting on this.

However, in order to contribute effectively to a swift climate transition by 2020, it is not an option for investors to wait for improved company reporting and substantially increased client demand for green, climate focused fund products. Also, investors are key agents in the Paris Agreement and should take lead in identifying new investment opportunities in green finance and climate-solution focused savings products. If the finance sector awaits public funding initiatives to materialise, there is a risk that the window of opportunity to ensure a stable future is missed.

Swedish and international decision-makers and regulators should redefine climate risk models for the financial sector. Financial stability is a minimum requirement for a sustainable future. However, fund management companies in this study are committed both to international conventions on environment and human rights, and to the fulfillment of the UN Sustainable Development Goals. Consequently, the portfolios' current and future impacts on the climate, forest integrity, and community rights should be addressed and communicated.

New financial risk models need to underline the false sense of security in not acting, which is already leading to devastating consequences for the future of the planet. Ultimately, extreme weather events, deforestation, human suffering and loss of life from climate change impacts are already affecting business activities and economic growth. The study clearly illustrates that the finance sector needs risk models, which reflect this reality.

Already today, the effects of climate change are impacting poor households and vulnerable groups such as children, women and indigenous people. They are being hit the hardest by for example hurricanes, floods, and food insecurity. Even with current temperature increases, climate change is acting as a threat-multiplier to conflict, thereby undermining international efforts for peace and sustainable development.

Two years after the Paris Agreement, rapid progress on its implementation is critical. In order to reach the long-term goal of net zero emissions in the second half of this century, investors need to act now and contribute to a clear global decline in carbon emissions by 2020.