

Climate Change -- The Next Frontier of Investment Selection

You may soon see a new performance metric in mutual fund and pension fund reports. It's called the carbon footprint of the fund, and its purpose is to measure how much carbon pollution is being generated by the companies in the fund's portfolio.

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By this time next year, this new metric could be built into investment reports from leading asset managers and pension plans that recently signed the [Montreal Carbon Pledge](#), a new initiative sponsored by Principles for Responsible Investment (PRI). A United Nations-supported network of international investors, PRI's goal is to contribute to the development of a more sustainable global financial system.

The PRI Initiative is inviting all investors to endorse the Pledge and thereby commit to measuring and publicly disclosing the carbon footprint of their equity portfolios on an annual basis. In the short term, PRI's goal for the Pledge is ambitious: To attract at least US \$3 trillion of portfolio commitment in time for the next United Nations Climate Change Conference in Paris in December 2015.¹

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Why the Investment Interest?

To many experts in the financial community, climate change is inevitable. "The scientific consensus on global climate change is now essentially unanimous," wrote Beth Ann Bovino, U.S. Chief Economist for Standard & Poor's. "[T]he accumulation of greenhouse gases in the atmosphere, if allowed to continue unabated, will have extensive and costly impacts on regional climates and economies throughout the world."³

Among the impacts chronicled by Standard & Poor's:

- The cost to the U.S. economy of doing nothing to lessen the impact of climate change would be between 2.2% and 5.2% of GDP by the year 2100, depending on how many super storms like Sandy and Katrina lash the region.
- Rising sea levels -- a widely noted outcome of climate change -- will disproportionately impact people living along the East Coast and West Coast. Even though flood tides may wash over only a small fraction of the country's total land area, a significant rise in the average ocean level could essentially wipe out a large chunk of Florida and the Gulf coast, swallowing entire cities from Miami to New Orleans.
- Changes in rainfall patterns have led to severe droughts that have hampered U.S. agriculture and impacted populous areas of the Southeast and

Southwest. On the other hand, rising temperatures in more northerly regions could enhance their crop-growing abilities.

Investment Considerations for Climate Change

Climate change is destined to become an increasingly critical issue for the environment, the global economy, and the global investment markets. With more data becoming readily accessible, investors now have the resources to gauge the impact that global climate change may potentially have on their investment portfolios. As a starting point, here are ways to begin conducting your own due diligence.

- **As a shareholder in a company:** Read the annual report and Form 10-K. Management statements in these publications could tell you how the company views the risks of climate change and how those risks could affect the business. Companies with significant mining and drilling activities should also disclose the impact of potential carbon emissions regulations on the value of their assets. Keep in mind that you are entitled to vote in company meetings and special elections.
- **As a shareholder in a mutual fund:** Read your fund's prospectus to determine whether fund managers give any special weight to environmental concerns. Equity funds are required to vote their shares at stockholder meetings. You can see how fund managers have addressed that requirement in past meetings.

In addition, the following specialized indexes may be useful for benchmarking purposes:

- [FTSE Developed ex Fossil Fuels Index Series](#) -- "The FTSE Developed ex Fossil Fuels Index Series is a capitalization-weighted index designed to represent the performance of constituents of the FTSE Developed Index after the exclusion of companies that have a certain revenue and/or reserve exposure to fossil fuels."
- [Solactive CK Low Carbon US Index](#) -- "The Low Carbon Indexes™ guarantee a 50% reduction in carbon intensity against the market benchmark, as verified by South Pole Carbon, and are the first in the industry to use the Sustainable Industry Classification System™ (SICS™), which categorizes industries based on resource intensity and sustainability innovation potential."

For More Information

[U.S. Forum for Sustainable and Responsible Investment](#)

[CDP](#) (formerly the Carbon Disclosure Project)

¹Principles for Responsible Investment, press release, "[Investors take Montreal Carbon Pledge to footprint portfolios](#)," September 26, 2014.

²*The Globe and Mail* (Toronto), "[Global investment funds pledge 'carbon footprint' disclosure](#)," September 25, 2014.

³Standard & Poor's Financial Services LLC, "For the U.S. Economy, Climate Change Is a Case of Pay Now--Or Pay More Later," September 18, 2014.