Breckinridge CAPITAL ADVISORS

2021 Climate Summit Brings Pledges to Combat Climate Risk

Author

ROB FERNANDEZ
DIRECTOR, ESG RESEARCH

Key Takeaways

- In commitments at once ambitious and daunting, countries are accelerating decarbonization.
- At an April summit, the U.S. nearly doubled prior carbon emission reductions targets.
- Progress and implications for corporate and municipal bond credit quality will be monitored.

At the Biden Administration's virtual Climate Summit in April, world leaders from 40 countries gathered and several announced accelerated long-term targets to decarbonize their economies.

The new commitments are ambitious and the challenges to achieving them are daunting.

The Biden administration's focus on climate as a policy driver continues to be reflected in its actions at the Climate Summit and subsequent policy and legislation. Those initiatives include expansive infrastructure (the proposed American Jobs Plan) and economic support (the already enacted American Rescue Plan and the proposed American Family Plan). The White House's May executive order "to advance consistent, clear, intelligible, comparable, and accurate disclosure of climate-related financial risk" is another example.

April Climate Summit Featured a Recommitment to Paris Agreement

At the April climate summit, the U.S. pledged to lower its carbon emissions by 50 percent to 52 percent by 2030 from 2005 levels, nearly doubling prior targets. Canada pledged to lower by 40 to 45 percent by 2030, up from a prior target of 30 percent. Japan pledged a 46 percent reduction by 2030 from 2013 levels, compared with a prior target of 26 percent. China reiterated plans to reach peak carbon emissions by 2030 and reach net-zero by 2060.

With its new target, the U.S. is catching up to the UK and European Union (EU). According to the BBC,[1] the UK is committed to reducing carbon emissions by 78 percent by 2035 while the EU's commitment is 55 percent by 2030.

On April 21, 2021, the U.S. submitted its new target as a Nationally Determined Contribution (NDC) under the Paris Agreement. President Biden recommitted the country to the 2015 global climate accord upon taking office in January 2021, after the prior U.S. administration had withdrawn from participation.

NDCs are the core requirement of the Paris Agreement, representing each country's commitment to reduce national CO2 emissions and adapt to the impacts of climate change. The Paris Agreement's goal is to achieve net zero emissions by 2050, keeping the average temperature rise in this century to well below 2 degrees Celsius versus pre-industrial levels, while pursuing efforts to limit the temperature rise to 1.5 degrees.

Essentially, net zero means that the amount of greenhouse gases (GHG) produced is offset by emissions removed or sequestered from the atmosphere over a specified time period, so the net amount emitted is zero.

Reaching the climate goals entails quick and significant changes to everyday life from the types of cars we drive, to how we heat our homes, to how we power manufacturing plants and office buildings. As recently as the end of the June 11 to 13 G7 Summit in the UK, supporters and skeptics alike pointed to the session's final joint G7 communique, as being notable for weaving climate throughout its many goals, while leaving out key details of the process of reaching the goals.

In April, *The New York Times* cited studies that estimate by 2030: half of all new cars sold would need to be electric; nearly all coal fired plants would have to be retired, and the number of wind turbines and solar panels could quadruple. Several Breckinridge analysts discussed the subject in Breckinridge's spring *ESG Newsletter*.

What Comes Next?

To help achieve its 2030 GHG reduction goal and the Paris Agreement more generally, the U.S. is creating several initiatives, including 1) a Global Climate Ambition Initiative to support developing countries in establishing net-zero strategies and setting and achieving their NDCs; 2) the first U.S. International Climate Finance Plan; and 3) international efforts to develop strategies and technologies to enable the global energy and economic transition.

At home, the Biden administration released an Executive Order on Climate-Related Financial Risk on May 20. The goals of the order include to:

- "Advance consistent, clear, intelligible, comparable, and accurate disclosure of climate-related financial risk, including both physical and transition risks
- "Act to mitigate that risk and its drivers, while accounting for and addressing disparate impacts on disadvantaged communities and communities of color and
- Spur "the creation of well-paying jobs; and achieve our target of a net-zero emissions economy by no later than 2050."

As a next step, the order directs establishment of a Climate-Related Financial Risk Strategy. Members of the President's economic and climate teams in coordination with the Secretary of the Treasury and the Director of the Office of Management and Budget are to develop within four months of the date of the order, a comprehensive, government-wide strategy regarding:

- Measurement, assessment, mitigation, and disclosure of climate-related financial risk to programs, assets, and liabilities in order to increase the long-term stability of Federal operations.
- Financing needs associated with achieving net-zero greenhouse gas emissions for the U.S. economy by no later than 2050, limiting global average temperature rise to 1.5 degrees Celsius, and adapting to the acute and chronic impacts of climate change: and
- Areas in which private and public investments can play complementary roles in meeting these financing needs.

Further, the order charges to other branches of the government to development of plans to address of climate-related financial risk by financial regulators (Treasury, Financial Stability Oversight Council); resilience of life savings and pensions (Labor); federal lending, underwriting, and procurement (OMB and the National Economic Council, in consultation Treasury); and a long-term budget outlook (OMB, in consultation with Treasury, the Council of Economic Advisers, the National Economic Council, and the National Climate Advisor).

Through the order, the President formalized his whole-government approach to analyze and mitigate the risk that climate change poses to homeowners and consumers, businesses and workers, and the financial system and federal government Itself.

While the U.S. return to the Paris Agreement and the NDC announced at the April 2021 Climate Summit are formidable, the President's subsequent actions and executive order in May seek to establish the process for the federal government to achieve net zero emissions by 2050. Progress from here, and its implications for credit quality in the corporate and municipal bond markets will be monitored carefully going forward.

FOOTNOTES:
1. *https://www.bbc.com/news/world-europe-56828383#:~:text=Under%20a%20new%20law%20agreed,target%20of%20a%2060%25%20reduction.*

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