Fossil Fuel-Free Investing: Process and Perspective

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Key Takeaways

- Many investors restrict or limit investments in companies with fossil fuel reserves or municipal utilities with carbon intensive generation assets.
- Reasons may include aligning with a fossil fuel-free mission, easing climate change's impact, or mitigating transitions risks to a low-carbon economy.
- Breckinridge manages strategies that emphasize securities of issuers that our research judges to be better managers of carbon emissions and other ESG criteria.

Over the years, many investors have decided to restrict or limit their investments in companies with fossil fuel reserves or municipal utilities with carbon intensive generation assets. Their reasons may include wanting to align with a fossil fuel-free mission, to ease the impact of climate change, or to mitigate the risks surrounding companies' transitions to a low-carbon economy.

Breckinridge manages a wide array of strategies that emphasize securities of issuers that our research judges to be better when it comes to management of carbon emissions, workplace safety, investment in renewable energy and other environmental, social, and governance (ESG) criteria. For investors wishing to be more restrictive and proactively divest holdings based on carbon-related criteria, Breckinridge also manages strategies with customizable carbon screens. The carbon screens utilize our portfolio customization capabilities and data from third-party research providers. Figure 1 illustrates the screening process.

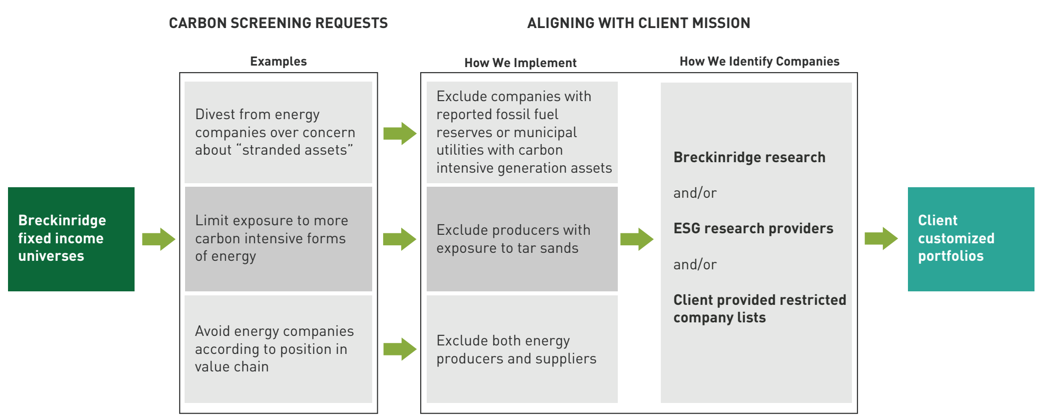
Fossil fuel concerns

The persistent rise in global temperatures, approximately 1.0 degree Celsius since pre-industrial levels, has been attributed to the steady increase in greenhouse gas (GHG) emissions. The primary contributor to the GHG emission trend is the human extraction and combustion of fossil fuels (coal, oil, and gas) for energy.[1]

Scientists have determined, with high confidence, that the rise in global temperatures and its effect on the climate is already impacting natural and human systems.[2] Recognizing the risks inherent from a rise in global temperatures, 195 countries came together in late 2015 to establish the Paris Agreement. The countries agreed to be accountable to keeping the increase in the global average temperature to well below 2 degrees Celsius (or about 3.6 degrees Fahrenheit) from pre-industrial levels.

They also decided to pursue the more ambitious goal of limiting the increase to 1.5 degrees Celsius.

FIGURE 1: CARBON SCREENING PROCESS



Breckinridge and many of our clients have grown increasingly concerned about the changing climate and its effects on investments. A way to mitigate climate risks, and support the Paris Agreement, is to limit exposure to GHG emissions.

Breckinridge's standard fossil fuel-free mandate excludes investment in companies with significant proven fossil fuel reserves and municipal utilities with carbon intensive generation assets. Through this mandate and with our ability to offer further customizations, we have helped many clients reduce their investments in securities with elevated emissions levels. The reduced investment exposure also helps to manage the risk that more stringent climate policies will negatively impact their investments.

One way to reduce this carbon transition risk is to limit investments in companies with oil, gas, or coal reserves or municipalities with carbon intensive generation assets.

For example, if future progress is made under the terms of Paris Agreement, the demand for fossil fuels will likely fall. As result, companies with reserves may be forced to leave them in the ground rather than mine or pump, leaving behind what is known as "stranded assets."[3] These companies may need to write down these assets, hurting profitability and impeding long-term planning. Restricting these companies from investment would therefore mitigate climate as well as credit risks and reduce the overall carbon footprint of the portfolio.

Awareness of transition risks, mission alignment, and greater disclosures of emission data are prompting a growing trend toward investors evaluating their exposure to the energy sector.

As of February 28, 2022, Breckinridge has applied a fossil fuel-free lens across approximately 250 accounts, with assets of about $1.7 billion in assets.[4] We look forward to continuing to work with investors on strategies and portfolio level customizations that consider their exposure to fossil fuel-reserves.

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FOOTNOTES:
1. *IPCC, 2018: Summary for Policy Makers*.
2. *IBID*.
3. Stranded assets are oil, gas and coal reserves that are left unburnable without expensive carbon capture technology, which itself alters fossil fuel economics, per speech from Mark Carney, governor of the Bank of England, September 2015.
4. Based on multi-sector and tax-efficient assets.