Breckinridge CAPITAL ADVISORS

Through their transitions, higher education E&Fs lend to net zero trend

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Key Takeaways

- It is logical to manage endowment assets through the same sustainability lens as capital assets.
- Qualitative and quantitative assessments of issuers' net zero approaches may become an integral part of the security selection process.
- A net zero approach also may seek to identify issuers that may benefit during a global transition to a low- or no-carbon economic future.

As colleges and universities announce commitments to carbon neutrality, how should we consider the connection between capital assets and financial assets? Simply put, if managing capital assets, such as building and equipment, through a sustainability lens is considered prudent investing, why wouldn't managing endowment and foundation (E&F) investment assets be viewed the same way. Assets are assets, and sustainability seems particularly material to endowments managed for the long term.

Higher education E&F transitions to environmental, social and governance (ESG) approaches often started with divestment of fossil fuel investments (See *College and University E&Fs incorporate ESG approached in Response to Stakeholders*), and many of those decisions were grounded in mission alignment rather than an investment thesis.

On the other hand, there is a clear investment case for setting E&F emissions reduction targets that align with an institution's broader carbon neutral commitments. Over the long-term, climate risk and how it is priced in securities valuation models will become more meaningful, particularly among the large-emitting sectors. Absolute greenhouse gas (GHG) reduction requirements will likely transform economies and sectors over the longer-term and have credit implications for various sectors and asset classes. Companies and issuers that are unwilling or unable to transition may face difficulties.

What is the net zero trend?

A net zero commitment means transitioning investment portfolios to net-zero GHG emissions over time. That level considers findings of the International Panel on Climate Change (IPCC) consistent with limiting global temperature rise to 1.5°C above pre-industrial temperatures by 2050. Net zero requires establishing intermediate emissions reduction targets every five years in line with Paris Agreement and regular progress reports.

GHG emissions are gases in the atmosphere that absorb and re-emit heat, helping to keep the planet's atmosphere warmer than it otherwise would be. *The New York Times* reported[1] that the IPCC report finds that, "The dangers of climate change are mounting so rapidly that they could soon overwhelm the ability of both nature and humanity to adapt, creating a harrowing future in which floods, fires and famine displace millions, species disappear, and the planet is irreversibly damaged."

The pursuit of net zero by higher education E&Fs may be a logical parallel to efforts on other fronts. Across Industry sectors, businesses are addressing GHG emissions associated with their own operations and those of suppliers and customers; often in response to regulations or self-imposed ESG commitments. At the same time, the asset management industry launched its own net zero campaign through the Net Zero Asset Management initiative (NZAMi). NZAMi signatories commit to transition investment portfolios to net zero emissions by 2050. Breckinridge Capital Advisors is a NZAMi signatory and has offered a fossil-fuel free investment strategy since 2014.

The trend to net zero among E&Fs is particularly strong. According to a May 6, 2021, *Businesswire* report,[2] a group of 17 leaders from higher education E&Fs, investment consultants, asset managers, and nonprofit partners joined together as a steering committee to guide a new Net Zero Endowments initiative hosted by the Intentional Endowments Network (IEN). Groundbreaking commitments from institutions like Harvard, Stanford, Michigan, and the University of Pennsylvania, led IEN's initiative.

In October 2021, the Times Higher Education (THE) Climate Impact Forum, reported[3] 1,050 universities from 68 countries made commitments to reach net-zero emissions by 2050 and transform their impact on nature, including a new initiative on nature-positive universities. The UN's Race to Zero campaign, the Environmental Association for Universities and Colleges, and Second Nature with support from the UN Environment Programme (UNEP) are supporting the effort.

The why is clear. What about the how?

A net zero approach typically employs frameworks for identifying and assessing the plans of security issuers to pursue pathways to net zero GHG emissions, and monitors progress. Qualitative and quantitative assessments of issuers on this basis and more become an integral part of the security selection process for portfolios following a net zero pathway.

Jane Dietze, chief investment officer of Brown University's $4.7 billion portfolio told *CIO magazine*[4] in March 2021, "The reality is that, collectively, we need to achieve substantial improvements in measurement and disclosure of a wide array of climate-related data. Companies, managers, institutions all need to demonstrate strides in the production and sharing of uniform data related to climate impact and sharing of uniform data related to climate impact."

Tom Joy, CIO of the Church Commissioners of England's $11.87 billion portfolio, told *CIO magazine*[4] that the commissioner's own analysis revealed, "that it is crucial to have a better line-by-line understanding of climate risks within the portfolio." He noted that his team increased engagement efforts with issuers to better understand their decarbonization approaches and targets.

In addition to identifying the strongest issuers on a net zero basis and winnowing out those that still have progress to achieve, a net zero approach seeks to identify issuers that may benefit during a global transition to a low- or no-carbon economic future.

Opportunities emerging from efforts to confront and reduce global warming may reveal new investment opportunities. "Climate solution investments have a key role in providing both investment returns and contributing to our climate targets," Tom Joy told *CIO*.

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FOOTNOTES:
1. "*Time Is Running Out to Avert a Harrowing Future, Climate Panel Warns*," *The New York Times*, February 28, 2022.
2. "*Leading Higher-Education Institutional Investors to Guide New Initiative for Net Zero Endowments, Targeting 50 Endowments Over Two Years*," *Businesswire*, May 6, 2021.
3. "*Over 1,000 universities and colleges make net-zero pledges as new nature initiative is unveiled*," UN Environmente Programme, October 28, 2021.
4. "*Endowments Embrace Net-Zero Portfolios: Is It the Future of Investment Management?*" *CIO Magazine*, March 11, 2021.