Developing tools for climate-conscious investment

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Professor Sir John Beddington of the Oxford Martin School explains the Oxford Martin Principles for Climate-Conscious Investment:

The 2015 Paris Agreement was the culmination of 21 years of negotiations about how the world could deal with climate change. The outcome is a challenge for the world's countries to limit temperature rise to below 1.5°C, if at all possible, and below 2°C, if absolutely necessary. But, nearly 3 years on, how we get from here to there remains unclear, and the private sector in particular is woefully far behind.

The effective mitigation of greenhouse gas emissions on a global scale will involve the reshaping of an economic system that in many respects, and for many generations, has been an efficient creator of human wealth and capital. For the commercial and investment communities, taking action on climate change will often be painful, particularly for short-term returns. And faced with uncertainty, inaction often feels like the natural choice. Inaction will, however, without a doubt, be more painful. This is most acutely the case for corporations who do not react nimbly and pre-emptively to the low carbon transition. If those corporations fail to thrive, their shareholders, suppliers and customers are equally implicated: shareholders via falling returns, suppliers by falling revenues and margins, and customers via diminishing choices.

The risk from inaction on the part of corporations comes both in the form of ill-preparedness for new policy and regulation, and in the longer-term, from physical risks from climate change on a company's core activity and its supply chains. Listed corporations have fiduciary duties to their shareholders to anticipate and adapt to these risks. Yet companies are not alone in feeling unable to react to the current tangled skeins of guidance over assessing, disclosing and acting on climate-change related business risk.

The Oxford Martin School has funded a group of researchers, Dr. Richard Millar, Professor Cameron Hepburn, and Professor Myles Allen, to develop a simple, scientifically-grounded set of principles that provide clarity for investors and for company strategists in analysing a business in the light of what we know about climate change and the likely path of mitigation. We have named them the Oxford Martin

Principles for Climate-Conscious Investment.

The Oxford Martin School funded this work with the Sullivan Principles in mind. These were used in the 1970s by investors, customers and suppliers of corporations doing business under the South African apartheid regime. The challenge of doing business under climate change presents a similar moral conundrum. Like the Sullivan Principles, the Oxford Martin Principles are designed to have a material impact on corporate decision-making. Like the Sullivan Principles they provide a more sophisticated alternative to simple divestment for the investment community to use. And like the Sullivan Principles, they help, by setting out clear guidelines of what is expected of companies as they navigate a contemporary moral maze.

The principles, published last week in *Nature Climate Change*, are as follows:

1. Commit to reaching net zero emissions from their business activities
2. Develop a plausible and profitable net zero business model
3. Set out quantitative mid-term targets compatible with their net zero goals

The Oxford Martin Principles should be seen both as a code of conduct and a set of tools for existing and potential investors. They prompt three deceptively simple questions: first, is this company committed to moving to net zero emissions for its own activities? Second, under current plans, will this business be profitable in a net zero economy? And third, can the company provide quantitative mid-term targets that are consistent with its net zero goal? In the paper, these questions are applied to three companies with very different business models: BHP Billiton, Unilever and Statkraft. The case studies reflect that whilst most companies would not be able to claim compliance with all three principles today, to do so is not unachievable in the future.

Simply put, these Principles are a call for companies to commit to net zero; to remain profitable; and to be verifiable. Deceptively minimal, they provide a framework through which to interrogate a company's future plans, on timeframes that are relevant to both investment horizons and to climate change mitigation.

More information: Richard J. Millar et al. Principles to guide investment towards a stable climate, *Nature Climate Change* (2017). DOI: 10.1038/s41558-017-0042-4

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