Markets missing fossil fuel exposure to climate risk: analysis

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The energy sector is thought to be exposed to between $1-4 trillion in transition risks alone as nations work towards the Paris goals

Investors are overlooking the long-term risks climate change poses to oil and gas infrastructure firms, which face tens of billion of dollars worth of stranded assets as the world transitions to greener energy, according to new analysis seen by AFP.

As the use of fossil fuels—the main source of planet warming greenhouse gases—comes under growing scrutiny, a number of funds are choosing to divest themselves of energy projects that may end up cancelled or mothballed as efforts grow to limit emissions.

The 2015 Paris deal on climate change enjoins nations to limit the rise in global temperature to "well below" two degrees Celsius (3.6 Fahrenheit), something experts say is impossible without a rapid drawdown in fossil fuel use.

ATLAS, an investment fund specialising in long-term infrastructure projects, examined how the assets of five oil and gas infrastructure companies would fare as countries switch to renewables in line with the Paris targets.

The analysis, seen exclusively by AFP, shows that the firms—who together hold a roughly 10 percent share of the energy infrastructure market—risk losing more than $100 billion of their valuation.

"There's a very significant unspoken risk to the valuation of these companies," said executive chairman Charles Kirwan-Taylor.

"That's something we take account of in our investment selections and we think other people should too."

ATLAS said that the market was improperly valuing oil and gas infrastructure projects by not discounting the risks of declining hydrocarbon use.

Although companies involved often have no direct exposure to market fluctuations due to fixed-price contracts, the assets they own are exposed in the long term to changes in energy policy, fuel costs and shrinking demand.

Ben Caldecott, director of the Sustainable Finance Programme at Oxford University, said the analysis "brings to the fore the contrast between the market's short-term approach to valuation and the longer-term actions we need to implement to limit climate change."

Carbon capture?

The energy sector is thought to be exposed to between $1-4 trillion in "transition risks" as nations work towards the Paris goals.

Last week an international team of financial experts said fossil fuel companies were of "principal concern" to investors due to their long-term risk exposure.

Carbon Tracker accused the sector of failing to disclose to shareholders the full extent of the liability posed by future climate change legislation.

"The change in policy around fossil fuels is one very big variable which will effect demand very considerably," Kirwan-Taylor told AFP.

In October, the UN's climate change panel (IPCC) issued a landmark report saying that the more ambitious 1.5C Paris target could only be hit with deep and rapid cuts in production and consumption of oil, gas and coal.

Yet oil and gas giants plan to invest nearly $5 trillion in exploring and developing new fields in the coming decades.

To do so and still comply with the Paris deal, the companies envisage a major role for carbon capture and storage (CCS)—a technology that syphons off CO_2 as fossil fuels are burned and stores it underground.

Despite decades of pilot projects and billions invested, markets have so far shunned CCS due to prohibitively high costs.

The ATLAS analysis found that the infrastructure companies faced significantly greater risk if projected CCS development was removed from transition scenarios.

Kirwan-Taylor said the fund would not factor in potential carbon capture impacts "because the technologies for that are not yet apparent".

"Even people who are supportive of CCS acknowledge that we haven't found the answer yet," he told AFP.

"From the point of view of a factually based investor, the 'something will turn up' approach to risk doesn't fit with rigorous analysis."

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