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Ninety One

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Tapping into the decarbonisation investment opportunities

Climate change is one of the world's greatest risks and the global pandemic has accelerated many efforts to address it. Deirdre Cooper, Co-Head of Thematic Equity at Ninety One, explores how investors may achieve long-term structural growth while contributing to a low-carbon world.

Deirdre Cooper
Co-Head of Thematic Equity

Q1

Why does decarbonisation matter?

Decarbonisation is the process of reducing carbon emissions to limit the impacts of climate change. It is crucial because the world is currently on track for average temperature rises that will have severe environmental, social and economic consequences.

For investors, decarbonisation matters because transitioning to a low-carbon economy requires a radical overhaul of the energy system, transport system and many other aspects of the global economy. This is changing the risk and return potential of industries and individual companies.

Q2

How is decarbonisation creating investment opportunities?

Global efforts to cut carbon emissions are driving vast flows of capital, fuelling innovation and creating a multi-year tailwind for select companies. A portfolio focused on decarbonisation therefore offers investors the potential to gain exposure to an area of long-term structural growth, offset carbon risk in other investments, and make a positive impact by financing businesses tackling one of the planet's biggest challenges.

Excitingly for investors, the structural growth trend being driven by decarbonisation is just beginning. The world is investing only US$500 billion of the US$2.4 trillion that needs to be spent every year to 2035 to limit temperature rises to 1.5°C[1].

Q3

Which sectors will benefit most?

Decarbonisation is creating opportunities in many sectors because it is changing the way the world produces and consumes. The companies most likely to benefit tend to be in the industrials, utilities, energy, technology, materials, chemicals and automotive industries. Within each of them, potential beneficiaries of decarbonisation exist across the value chain, from makers of components, to service providers, to end-product distributors.

One way to identify them is to think about all the companies involved in the key pathways to a low-carbon economy, which include:

- Renewable energy: The world needs a complete change in how we generate electricity.
- Electrification: Increased electrification is essential, including an overhaul of ground transportation.
- Resource efficiency: We need higher efficiency standards in industrial processes, buildings and appliances.

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[1]Source: Climate Policy Initiative – Global Landscape of Climate Finance UN IPCC. November 2019.

Q4

What impact has COVID-19 had on the decarbonisation trend?

Many people thought climate targets would be shelved when the pandemic struck. In fact, the opposite happened as governments ramped up their environmental plans, partly to stimulate their economies. China, Japan and South Korea committed to 'net-zero' in 2020, while the European Union focused its COVID-recovery strategy on green sectors. In addition, Joe Biden's US election win has brought to the White House a president with a much more ambitious climate agenda. Coupled with a heightened sense of responsibility for the planet's health among consumers and businesses, these policy developments have accelerated the low-carbon transition.

Q5

Is there any proof of alpha generation from decarbonisation?

The ability to generate alpha depends very much on the investment approach used to gain exposure to decarbonisation. The beneficiaries of this powerful trend are often not obvious – they don't come with a convenient label! That's why we believe decarbonisation requires a research-focused investment approach specifically designed to identify the potential outperformers as the low-carbon transition progresses.

We also believe strongly that investors should be highly selective. While we expect decarbonisation to drive above-market growth, it is a very disruptive process. We favour an investment approach that concentrates on leading companies with competitive advantages, because we think they have the best chance of emerging as the winners from this economic transformation.

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