KPMG

The rise of climate capitalism

Authored by:

Mike Hayes
Head of Global Renewables, KPMG International

Thekla von Bülow
Manager, KPMG in Germany

Minh Dao
Partner, Deal Advisory, KPMG Australia

The dawning

ESG is not the appetizer on an investor's menu anymore—it is now part of the main course.

With the urgency of climate change becoming indisputable in the wake of a staggering increase of extreme weather conditions around the globe, dealing with climate change has moved well beyond being a philanthropic pastime of the well-intentioned. Investors—be it corporate players, institutional investors, or other type of asset manager—have come to realize that the physical threat, policy change, and shifting market dynamics will likely have a significant impact on a wide array of assets in the years to come. The risk of stranded assets is just one prominent but worrying example. Climate and capitalism are becoming inextricably linked.

Getting real—Walk the talk

Finally, the climate change and ESG agendas have collided, and investors are voting with their wallets by publicly stating that they will not invest unless there is a real, detailed, and committed underlying ESG strategy. For many investors, this requirement is now embedded in their investment committee approval processes. It has become very clear that employees, customers, shareholders, and the general public are putting companies under pressure to act.

We are talking about nothing less than the transition of entire economies to a low carbon future, with very little time at hand. With all that comes with it, investors are worried about the financial implications of their investment policy in such uncertain times.

As an investor, fundamentally changing the way you do business and the way in which investment decisions are made will require guts, determination, hard work, creativity, and the willingness to move into unchartered territory.

Getting started—Roll up your sleeves

In reality, there is a lot of insecurity around the actual timing and extent of climate change and its effect on individual investment decisions. The bankability of individual projects remains the uppermost priority of investors, despite the appreciation and awareness of the climate urgency.

However, the game changer is that there is now a real business case for ESG. For example, renewables, specifically wind and solar, have become fully commercial and offer real competitive business opportunities. Other clean technologies are on their way to commercialization as well; the key here is scale and collaboration. We see a lot of potential in investors being bold and addressing unserved markets.

With all the emotionality of climate enthusiasts and scaremongering, getting down to the real investment decision can turn out to be a relieving task. In other words, ESG is now starting to become the output of rational investment decisions rather than being the mold investment decisions are pressed into in order to comply with ESG targets of "I'm the good guy" PR campaigns. And investors will be surprised by how much of their "smart investing" already is ESG. They are effectively joining the group of "impact investors," perhaps even without realizing it.

Managing risk

Besides looking at the arising low-carbon opportunities, investors have to reassess how they look at risk. And the key to doing that is to focus on the core issues of climate change and key KPIs. Data collection and data transparency thereby play central roles. Companies may have to move away from looking at their business in an isolated way but rather take on an integrated approach to reflect the risk of the entire value chain.

Frameworks such as the Taskforce for Climate-Related Financial Disclosures offer increased transparency and comparability. However, as long as these are of voluntary nature, they will not achieve the required group pressure.

A new paradigm—Climate capitalism

At this point, nobody can deny the effects of greenhouse gas emissions on our planet. There is wide consensus on the triggers and effects. Supported by effective policy decisions, such as the EU Sustainable Finance Taxonomy, investors are increasingly shaping the agenda and are becoming a force for real change. Investors are getting clearly focused on what is a sustainable business opportunity and what is not. With funding flowing from high- to low-carbon businesses based on rational investment evaluation, the transitional power of the financial systems may be the driving engine for decarbonization. This should give rise to a new economic era, where climate action and inclusive growth are reconciled—"climate capitalism." In reality, investors can appreciate that, while there is a lot of risk, this transition to a low-carbon global economy also brings unprecedented economic opportunity.