

TalkingPoints

Positioning for the Green Transition: What's Your Business Opportunity?



Chris Baldock

Lead ESG Positive Impact
Trucost, part of S&P Dow Jones Indices

Trucost outlines some of the main considerations for companies seeking to capitalize on low-carbon business opportunities, estimated by the World Bank at USD 23 trillion between now and 2030.¹

1. What steps are companies taking to position for the green transition?

Companies are trying to make sense of fast-moving policy, market, and technology changes related to carbon and climate risk. Whether it's about their own operations or the greener products and services they sell, corporate executives want to understand the financial implications and their competitive profile.

Corporate leaders realize it's not about if a green transition will occur, and it's not even about when—it's about how fast the green transition will happen. Over 60% of the world's largest companies have already set carbon reduction targets. More than 100 have set a target that is science based, defining a pathway to future-proof growth by specifying how much and how quickly they need to reduce their greenhouse gas emissions to align with global energy transition commitments. A further 400 are en route.²

The challenge for companies lies in identifying the smartest strategies to achieve their green transition goals. For most, this will mean optimizing an array of capital investments and weighing their options using robust data on financial and environmental returns.

2. What are the challenges with existing approaches to capital expenditure decisions?

Capital expenditure (capex) decisions, such as constructing manufacturing facilities, introducing new technology, or evolving product lines, are some of the biggest a company makes.

1. International Finance Corporation (2016), *Climate Investment Opportunities in Emerging Markets An IFC Analysis*, available at https://www.ifc.org/wps/wcm/connect/news_ext_content/ifc_external_corporate_site/news+and+events/news/new+ifc+report+points+to+%2423+trillion+of+climate-smart+investment+opportunities+in+emerging+markets+by+2030
2. The Science Based Target Initiative, available at <http://sciencebasedtargets.org>

Investments like these are vital to future growth, but financing long-term, multi-million dollar projects can carry significant risk. Carbon trading schemes, taxes, and fuel duties aimed at meeting the Paris Agreement—limiting global warming to less than 2 degrees Celsius—could affect the financial viability of investments. Trucost estimates that average carbon prices could increase more than sevenfold to USD 120 per metric ton by 2030.

Governments and financial regulators are increasingly demanding that companies be more transparent about how they are managing climate-related risks in capex decisions, which can have significant implications for shareholder value. The Financial Stability Board's Task Force on Climate-related Financial Disclosures (TCFD) recommends that companies use scenario analysis to weigh the business implications of climate change, including investment projects, so risks can be priced into the market.

The problem is that many companies make capex decisions based largely on financial considerations. For companies that want to maintain their carbon competitiveness and license to grow, failing to integrate green transition metrics into the business case creates significant blind spots.

3. What needs to change?

Trucost calculates the net financial and environmental costs and benefits of a company's capex program. Investments in a range of potential or existing projects can be assessed in this way to inform decisions over which projects should go forward. A Green Transition Score for each project shows its contribution toward achieving a corporate goal, such as a science-based carbon reduction target. A company can therefore optimize its project portfolio to achieve its goal.

Companies can further prioritize their investment plans under a range of different scenarios compared to business as usual—addressing regional issues such as the carbon intensity of grid electricity, planned changes to national infrastructure, or even the impact of local carbon pricing.

4. What's the key to engaging stakeholders in low-carbon business?

Quantifying the green transition return alongside the financial return of low-carbon strategies provides a business lens on low-carbon investment. One of the major benefits is being able to credibly demonstrate to investors that the company is minimizing exposure to climate risks by considering future scenarios in which there are much higher costs for carbon emissions in line with the TCFD recommendations.

It also creates opportunities for companies to gain access to new streams of finance for their capex programs, for example through issuing green bonds. According to the Climate Bonds Initiative, global green bond issuance hit a record USD 155.5 billion in 2017, with investment in low-carbon buildings and energy efficiency on the up.³ To be robust and credible, companies issuing green bonds must be able to provide quantified evidence of the environmental benefits of the projects that they are seeking to finance. The Green Transition Tool provides this evidence by quantifying the actual avoided emissions from projects, alongside a measure of the progress toward meeting a 2 degree scenario.

5. What does the future look like?

Above all, it will be critical for sustainability teams to meet the information needs of a senior business audience, including the Chief Financial Officer and Chief Risk Officer, when seeking investment in low-carbon strategies. It takes a wide range of data to inform complex decisions, but developing a holistic business case that factors green transition return alongside financial return is a critical step toward making the transformational investment decisions many companies will need to align with the global energy transition.

Exhibit 1: Revealing 'Green Transition' Business Case Blind Spots

Project Name	ROI Before Future Carbon Pricing (%)	ROI After Future Carbon Pricing (%)	Difference (%)
Solar	-90	-82	+8
Anaerobic Digestion Plant	-61	-70	-15
LEDs	159	224	+41
Coal Storage	464	-86	-118

Source: Trucost. Data as of May 2018. Table is provided for illustrative purposes.

3. Climate Bonds Initiative (2017), Green Bond Highlights, available at <https://www.climatebonds.net/resources/reports/green-bond-highlights-2017>

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