# Effective implementation strategies to achieve net zero portfolios

The net zero blueprint is clear. Now investors must urgently action their commitments. But how? What are the most effective implementation strategies?

By *Bastiaan Pluijmers*

Investors who have set net zero targets understand that the buck does not stop there. To fulfil their commitments, they must align their actions with IPCC science recommendations. They must track and report on Scope 1, 2 and 3 emissions, prioritise the achievement of real economy emissions reductions, adhere to rules to only use offsets where there are no technologically and/or financially viable alternatives, create investment products aligned with net zero emissions by 2050 and facilitate increased investment in climate solutions.

## The net zero blueprint

It is a necessary and daunting task. Not only must investors achieve net zero in line with these requirements, but they must also continue generating consistent and competitive financial returns to fulfil their fiduciary duty. Within the current macroeconomic environment, this is anything but simple.

There are choices to be made. Either investors can focus on generating returns and push net zero commitments further out, risking reputational, climate and financial risk. Or, they can double down on their efforts to strengthen alignment between financial performance and achieving net zero.

For the past few years, my work has found meaning in the latter and here I share some of the implementation strategies that are suitable and available for investors to take action today.

## Understanding double materiality

When designing an investment approach that strives for net zero, the following guiding principles apply. First, design an approach that recognises where the actual levers of influence lie. Second, follow the best advice and developments from the industry and regulations. And third, design a pragmatic and realistic approach that asset-owner stakeholders can grasp, and to which investment managers can be held accountable. If it is too complicated and 'misses the point', then communicating progress becomes too difficult.

This is where the concept of double materiality is widely adopted and very useful. It speaks to the fact that risks and opportunities can be material from both a financial and a non-financial perspective. Many disclosures, such as the SFDR and the EU Taxonomy, confirm double materiality as the basis for comprehensive non-financial information disclosure.

Investors who adopt double materiality as a concept have a better idea of the initiatives that could help build an understanding of the non-financial impacts of investments. An example is partnering with the Impact Management Project (IMP) and using their 'ABC' framework to further categorise the sort of non-financial impact of any investment.

Investors also need to identify specific decarbonisation measures and targets. To this end, the TCFD, Partnership for Carbon Accounting Financials (PCAF), the Institutional Investor's Group on Climate Change (IIGCC), the Dutch Climate Agreement and the science-based targets initiative (SBTi) provide guidance.

Within our firm, we decided on two approaches to calculate and measure targets. The first assesses the picture now and the second looks at how we progress forward:

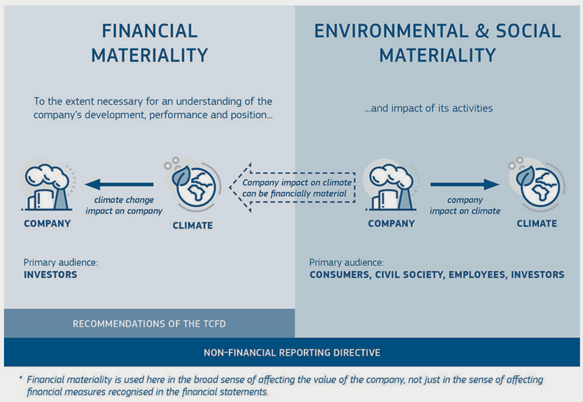
1. Measure historical and current actual carbon footprints.
2. Gauge how companies' carbon footprints and affect on the climate are likely to develop over time.

Once investors decide on the specific metrics, they can define the actions to influence change.

## Influence and implement

To be effective, it's necessary to map out where the investor's actual point of influence lies. Following industry guidance, we designed the below 'levers of influence' from a fund-of-funds perspective, managing equities, fixed income, absolute

**FIGURE 1: SEEING DOUBLE – REPORTING CLIMATE-RELATED INFORMATION**




Source: European Commission.

return strategies, private equity, dedicated impact portfolios, real estate and multi-asset portfolios. The principles apply for direct investors as well.

### (1) Engagement on emissions with external managers

- Engage and encourage engagement on the highest emitters.
- Promote and ask for science-based climate targets.
- Improve environmental data quality.

The first lever concentrates on engaging with investment managers and companies. Given that the concentration of emissions worldwide typically is held within just a few companies, an analysis of carbon emissions data shows where investors should focus engagement efforts. Namely, on this small group of heavy emitters.

For example, if a manager finds out that just 5 companies out of a total of 25 make up 80% of total carbon emissions within a single portfolio, then they only need to engage with those 5 companies to adopt the science-based targets in order to achieve the majority of emissions reductions. It is the pareto principle in practice.

### (2) Allocate to impact investments

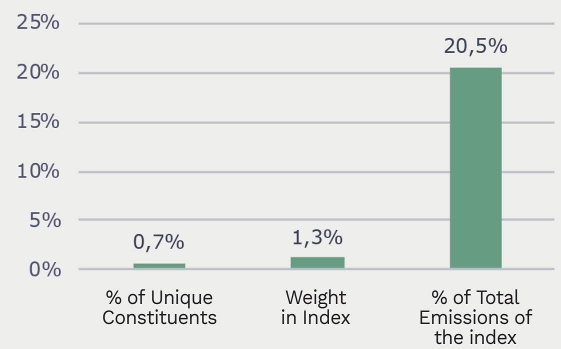
- Solutions-focused investments.
- Strategies with explicit climate strategies of science-based targets.

The second lever focuses on increasing investments in strategies and managers that are the winners of the green energy transition. These are actors that do not simply reduce emissions, but that contribute to the solutions in meaningful and measurable ways (again, the IMP's ABC framework helps here).

In this context you can think of companies that through their products and services contribute to solutions to the climate challenge. These could be renewable energy companies, but also extends to smart grid solutions, food security, regenerative farming, or new business models to create value and conserve the blue economy.

The key is to identify and assess these future winners effectively. Institutional investors could consider signing up to the Global Impact Investing Network (GIIN) to stay at the forefront of impact investing – which is a maturing and sophisticated investment practice that has surpassed well over $ 1 trillion in 'assets under impact'.

**FIGURE 2: TOP 10 COMPANIES CONTRIBUTORS TO TOTAL EMISSIONS OF ANTHOS CUSTOM GLOBAL EQUITY INDEX**




Carbon estimates are subject to delays in reported data.

Source: Anthos Fund & Asset Management, as at 30 June 2022.

### (3) Avoid exposure to heavy polluters

- Companies with revenue from thermal coal, oil sands, Arctic oil & gas exploration.

The third lever addresses investments in the heaviest polluting sectors. This should be considered a lever of last resort, given that emissions need to be reduced from the real economy, not just from portfolios. The key thing is not to assume that exposure to heavy emissions at an absolute level means exclusion should be the best approach. Instead, investors should ask these companies and funds what their 'theory of change' is and encourage them to set science-based targets and action plans.

In accordance with the latest and best industry and regulatory developments, these are the implementation strategies suitable for most investors to help them fulfil their net zero targets. If implemented early and systematically, there is no reason why this strategy is inconsistent with generating competitive financial returns.

Given the net zero blueprint is already well defined, and many investors are currently misaligned with these targets, implementing strategies like these will no doubt unlock significant rewards for those opportunistic and active investors keen to lead the way to a net zero economy. ■

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## SUMMARY

To fulfil net zero targets, investors must align their actions with IPCC science recommendations.

Risks and opportunities can be material from both a financial and non-financial perspective.

Investors who adopt this 'double materiality' have a better idea of the initiatives that could help build understanding of the non-financial impacts.

Three actions to influence change are suitable for most investors to help them fulfil their net zero targets: engagement on emissions with external managers, allocation to impact investments and avoidance of exposure to heavy polluters.