

## Linda at the G20 International Conference on Climate in Venice

*Featuring:*

**Linda Eling-Lee**, Managing Director and Head Of ESG Research, MSCI

Mike Disabato:

Hey everyone, we are back from our short summer holiday with a special bonus ESG Now episode. Last week, the world's top economic leaders convened in Venice, Italy to discuss and negotiate crucial details of our global monetary and political systems as part of the G20 Conference. As you can imagine, one of the major challenges the G20 discussed was climate change. And on July 11th, it held what's called the International Conference on Climate in Venice. At the event, leaders convened to promote better global cooperation on climate risks and to lay out their strategies to support the transition towards a low carbon economy and society.

Mike Disabato:

The day of talks can be found on YouTube. It's about a three-hour long video. And if you're interested, it is a comprehensive look into how the transition to a net-zero world and the financial sector intertwine. Today however, we're going to focus on one speech because it was given by our very own Linda-Eling Lee, who is our global head of ESG research. In her speech, Linda focused on the dwindling pool of companies that are able to meet the goals set in the Paris Climate Agreement and what should be done to address that in the future. She began her speech by posing a question to the audience on the oddity of time and the impermanence of our economy. I hope you enjoy listening, and we will be back with our regular ESG Now program this Thursday.

Linda-Eling Lee:

What will be the largest companies in the world in 2015? So 30 years from now? Well, obviously we don't know that. What we do know is that today, Apple, Amazon, Facebook, and Taiwan Semiconductor, these are among the largest public companies in the world. These are the giants that we know from the digital revolution that has really changed all of our lives in the last 30 years. But we should really recall that of the 10 largest companies today, seven of them didn't actually even exist 30 years ago. So we meet here today at the dawn of another revolution. We think that investors are asking which companies will thrive or are going to die

in the next 30 years? So as we drive emissions to zero, assets are going to be repriced and industries will be unrecognizable. And so this is the Net-Zero Revolution.

Linda-Eling Lee:

With more than \$14.5 trillion that are benchmark to MSCI's indexes plus our market leadership and ESG data, ESG ratings and analytics, we are asked by investors every day how to navigate a low carbon economy. Equally, we're asked by thousands of companies why investors are evaluating their climate strategies. So I'd like to share three things with you today that we see at the nexus between companies and investors.

Linda-Eling Lee:

First is that what investors are holding in their portfolios today isn't going to work for 2050. There are over 9,000 companies in 50 countries in MSCI's broadest market index. This represents the global equity universe. Now, these companies are putting carbon into the atmosphere at a rate that takes the world to more than three degrees warmer by the end of the century. By our calculation, over 90% of all public companies today are not on track to reduce their emissions for keeping global warming to one and a half degrees.

Linda-Eling Lee:

Now, how can an investor actually reduce their carbon intensity of their portfolio if the companies in those portfolios aren't actually doing so? Investors really have two choices, influence or reallocate. So as share owners, investors must influence and put pressure on company boards and management to transform their business models. Investors however, they do need every company on average to reduce carbon intensity by about 10% every year until 2050 just to keep us under one and a half degrees. That's not going to be easy because we have found of course, that historically, fewer than one in four companies has actually managed to reduce their emissions by quite this much. This is just a lot to ask. Or investors can reallocate. Investors can move more of their capital to the decarbonizing companies and away from those that are moving too slowly or maybe not even acting at all.

Linda-Eling Lee:

But here too there's a hard limit. Remember, 90% of companies are running too hot, meaning that their emissions trajectory would actually take us beyond a one and a half to two degree rise in temperature. Now, these too hot companies, they're really no longer investible options for a growing number of institutional investors. But these institutional investors have very large pools of capital and they can't just invest in a smaller and smaller set of companies. So what the world actually really needs are new companies. They need new businesses to invest in. We really need the tech companies of the future, really the innovators of the Net-Zero Revolution.

Linda-Eling Lee:

Second, the Net-Zero Revolution is going to produce not just losers that are holding carbon stranded assets, but some spectacular winners. So a moment ago, I told you some of the largest companies in the world today. In 1995 at the dawn of the internet, the largest companies included General Electric, ExxonMobil, Royal Dutch Petroleum, Philip Morris. Not one was a technology company. Back then, the market value of the tech sector was about 6% of the global equity universe. Today it's roughly about 20%.

Linda-Eling Lee:

Now, at the dawn of the Net-Zero Revolution, we're estimating that fewer than 3% of the companies in the MSCI index actually earn a majority of their revenues from clean energy or low carbon technologies. So this revolution begins with these companies helping to transform how we produce and how we consume energy. But in time, this revolution won't just be about displacing traditional fossil fuel companies with renewable energy businesses. It's going to be much bigger than that. Just as a digital revolution has reached far beyond the tech sector to really reach every part of our economy, the Net-Zero Revolution is not limited to the energy sector. It's going to touch every company in the world sooner than they imagine.

Linda-Eling Lee:

Experience has shown us though that identifying the winners of the future is not very straightforward. For every Amazon, dozens if not hundreds of e-commerce companies have fallen by the wayside. And we tend to forget all the social media sites that died off in the wake of Facebook. This push that we have now for sustainability will likewise see its share of failures. Green startups, which remember, are still startups. Many companies that are competing to event low carbon solutions are not going to succeed. Yeah, some, including ones that may not even exist today, could actually emerge as the titans of a net-zero world.

Linda-Eling Lee:

So third, how can investors then investigate this future that we've been talking about from the present? Well, in part they're using indexes. So think of a basket of companies. An index measures the performance of that basket. So if the basket actually has every company in the world in it, then you can weigh the emissions of the world's companies. And then when we embed forward-looking climate metrics, you can get a temperature reading, which tells you that the world's companies would take us to over three degrees warmer.

Linda-Eling Lee:

Now, I'd like you to imagine that you're at the supermarket. You can choose which companies to actually put into your shopping basket. Next to the prices you see emissions, or you see a conversion of emissions to a temperature. You can see how every company you put into your shopping basket actually adds to the basket's emissions and changes the basket's temperature. Over the next three decades, if the companies of the world actually succeed in decarbonizing, an index like MSCI's index that measures the basket that contains all of the

world's public companies, so really the whole supermarket, if you will, the MSCI All Country World will become a low carbon index, one that indicates a lower and lower temperature.

Linda-Eling Lee:

But we're not there yet, right? So between now and then, investors are using different indexes that integrate their climate concerns. They're creating alternative shopping baskets of what they consider to be healthier choices to take their investments on a faster glide path towards that convergence.

Linda-Eling Lee:

So then what do investors actually need to take them into this revolution? Our current market infrastructure has evolved to facilitate capital flows that support a carbon-intensive economy. What we really need is a market infrastructure that's oriented differently. One that actually supports sustainability. A critical component are new types of measurements that show how vulnerable or how resilient every asset is to climate change. These are measurements that can be used as a common language among market participants so that we can value the emerging risks and opportunities in the new economy.

Linda-Eling Lee:

These new types of measurements, they require data that we don't have today. And as we look forward to what COP26 could achieve, we urge policy makers and financial regulators of the G20 and the rest of the world to introduce mandatory climate-related disclosures and agree on international standards of disclosure. But we caution regulators and standard setters not to confuse what should be disclosed by companies with what can and should be measured by analysts, by investors and regulators.

Linda-Eling Lee:

So instead of asking companies to each report on their own assessment of climate risk, which will inevitably produce a lot of inconsistent data, and ask them for the basic ingredients which they can all disclose immediately. Right now we lack data on companies' full emissions throughout their entire value chain. And we critically lack disclosures of where their operations are located. These are actually the absolute minimum inputs into any climate risk analysis. So in other words, ask companies for the inputs and the market will converge on the most decision-useful outputs. And this is how we will collectively construct the pipes for a new market infrastructure.

Linda-Eling Lee:

So MSCI will play its part. I'm very pleased today to announce that MSCI will join with the Glasgow Financial Alliance for Net Zero as part of the race to zero campaign to spearhead a net-zero financial service providers alliance. This new alliance will galvanize the world's index and data providers, credit rating agencies, and accounting firms to really lay the tracks that can take investors and companies to a net-zero world. It will be great if when we look back on

2021 decades from now, we can actually say that this is the moment when the world leaned into its low carbon future when we entered an era of enterprise and collaboration to make the Net-Zero Revolution a reality. Thank you.

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