Ninety One 晉達

Capturing the decarbonisation growth opportunity

The low carbon transition presents a significant, long-term structural growth opportunity that is compelling for both investors who have made a pledge to net-zero emissions and investors in search of new return drivers.

The speed at which climate-related developments are occurring — across policy, technology and consumer trends — is accelerating. Many companies behind decarbonisation solutions are in renewables and transportation, where rapidly improving technology and lower costs are contributing to the long-term structural growth trend.

Decarbonisation's diversification potential

One of the compelling characteristics of decarbonisation as an investment theme is that the range of companies covered sit across multiple sectors and regions, and with a spread of market capitalisations, but generally with higher-than-average growth rates.

It comprises a hugely diverse group of businesses: from wind-power developers, to logistics firms, to software companies, to biotech businesses, and more. We saw the benefits of this diversity during the global equity sell-off in Q1 2020.

Hedge systemic carbon risk in portfolios

Investors are rightly paying attention to how climate change and the transition to a low-carbon economy may impact the risk/return profile of their portfolios. The average investor is highly exposed to fossil fuels, given the amount of carbon-intensive exposure in their underlying investments.

As climate action accelerates, these headwinds for traditional, carbon-heavy businesses will grow stronger. We believe one approach to manage this risk is through an investment process that seeks companies for which these same factors are tailwinds, and hence we would expect an opposite effect on investment performance.

Innovation and adaptation

Environmental solutions by their nature require innovation. To solve the climate challenge, we need to reinvent many aspects of the way the world produces and consumes – from transforming energy generation and transmission, to changing industrial processes, to transitioning to new ways of transporting people and goods. Electric vehicles, for instance, look similar to traditional cars on the outside, but contain very different components and technologies, and require different infrastructure. Innovation is therefore a key driver of the competitive advantages, growth potential and profitability of the companies benefiting from decarbonisation.

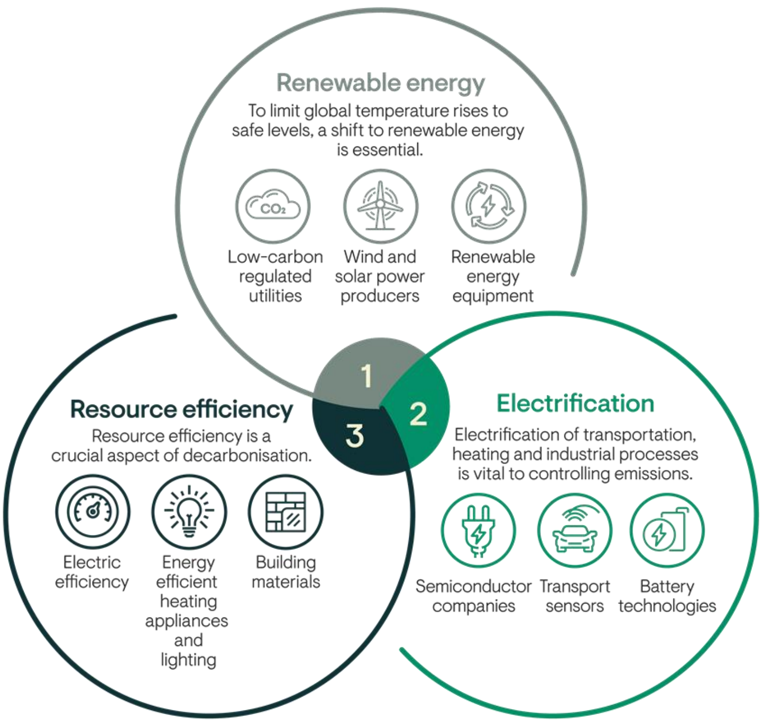
Adaptation is also key, since climate change is already occurring and likely to continue even if emissions-reduction targets are met. Alongside the decarbonisation innovators, companies that help the world adapt to an unstable climate can also be presented with significant growth opportunities.

Three pathways to a low-carbon future

The economic transformation required to limit the worst effects of climate change has only just begun. The world is currently spending only US$500 billion of the US$1.6-US$3.8 trillion of public and private investment required annually to keep temperature rises below 2 degrees. Thus the massive growth opportunity lies ahead.

We believe the three main pathways to decarbonisation include:

- **Renewable energy:** The world needs a complete change in how we generate electricity, moving away from fossil fuels towards renewable energy, mainly wind and solar.
- **Electrification:** Increased electrification is essential, including an overhaul of ground transportation, making the fleet more autonomous and efficient, and ultimately moving away from internal combustion engines to self-driving electric vehicles powered by renewable energy.
- **Resource efficiency:** More efficient use of resources is key to decarbonisation, including achieving higher standards of efficiency in many domestic and industrial processes, and in buildings and appliances



Tap into a long-term structural growth trend

Despite the pandemic, the past year suggests governments over the world are committed to decarbonisation, further fuelling the structural growth trend.

However, government policy isn't the only driver of decarbonisation. The costs of low-carbon technologies are declining, and green solutions' performance continues to catch up to, and increasingly exceed, that of traditional, high-carbon products and services. Add to this growing consumer preferences for low-carbon solutions, and decarbonisation looks hard to stop.

In our view, the growth potential of some of these businesses is significant. To get to net-zero, or close to it, the green energy and transport sectors will have to be multiple times their current sizes. Wind and solar must dominate electricity generation, and 100 million EVs must be sold every year by 2050, up from about 2 million in 2019. This implies substantial growth not only for renewable-energy utilities and EV manufacturers, but for companies in their supply chains.

We believe the shift towards a decarbonised future is accelerating and will create compelling investment opportunities for decades to come. Decarbonisation is still at an early stage, which should give investors the potential to capture meaningful alpha and diversification.

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Tel | (852) 2147 0090 Email | info@hkrsa.org.hk Website | www.hkrsa.org.hk

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