GAM Investments

GAM EXPLAINS:

THE IPCC MITIGATION OF CLIMATE CHANGE REPORT

MARKETING MATERIAL FOR PROFESSIONAL INVESTORS ONLY

THE IPCC MITIGATION OF CLIMATE CHANGE REPORT

With the global spotlight focused on the Russia-Ukraine war, the latest report from the UN's International Panel on Climate Change (IPCC), published in April 2022, did not make many headlines, yet its findings are momentous. The report offers an alarming depiction of the scale and scope of the action still needed to tackle the climate crisis.

WHAT IS IT?

The United Nation's International Panel on Climate Change published its Working Group III Sixth Assessment report (AR6) in April 2022. At almost 3000 pages, it brought together a significant amount of research from world-leading climate scientists across 195 countries, tasked with assessing the efforts made in mitigating climate change; assessing the implications the world will face on its current warming trajectory; and conveying what is needed to meet long-term climate goals.

The report is the third in a three-part assessment. Its predecessors were 'The physical science basis' (Working Group I), published in August 2021, which concluded that Earth's warming is unequivocally human-induced. The second part, 'Impacts, adaptation and vulnerability', was issued in February 2022 and found that no place on Earth would escape the impacts of global warming.

WHY IT MATTERS TO INVESTORS

Climate change is a systemic risk affecting all sectors and markets. The mitigation report demonstrates both the extent and speed with which investments that seem sound now can become much riskier. This is not limited to obvious sectors such as energy or transport, but rather affects all parts of the global economy.

The report outlines how far behind the financial sector is in reaching the funding levels needed to meet the targets set out in the Paris Agreement, and the need for investors to substantially increase investment in renewable energy and other low-carbon solutions.

This transition will be the biggest economic transformation since the Industrial Revolution and the findings of the report suggest that capital markets must be innovative and bold in their support for low carbon activities.

How investors choose to invest in the coming years and whether they can encourage the companies they invest in to adopt robust Paris-aligned strategies are likely to be definitive for the future of the planet, as well as for their own portfolio returns.

At GAM Investments, we are already investing in opportunities from green hydrogen to green housing, and engaging with companies to actively manage their climate risk. Last year, we exited our investment in a large German utility company in large part due to its inadequate plan to reduce its carbon footprint.

Our Sustainable Climate Bond strategy is one of the first to focus on green bonds of European financial issuers. European banks dominate the European corporate financing landscape and therefore have a pivotal role in driving sustainable growth. In its first year, the projects financed by the green bonds the strategy holds helped avoid 1,580 tons of carbon dioxide equivalent (CO2e) – equal to driving a car more than 200 times around the Earth. They also helped install 2.8MW of renewable energy capacity and to finance around 1500m2 of green buildings [1].

THREE TOP TAKEAWAYS

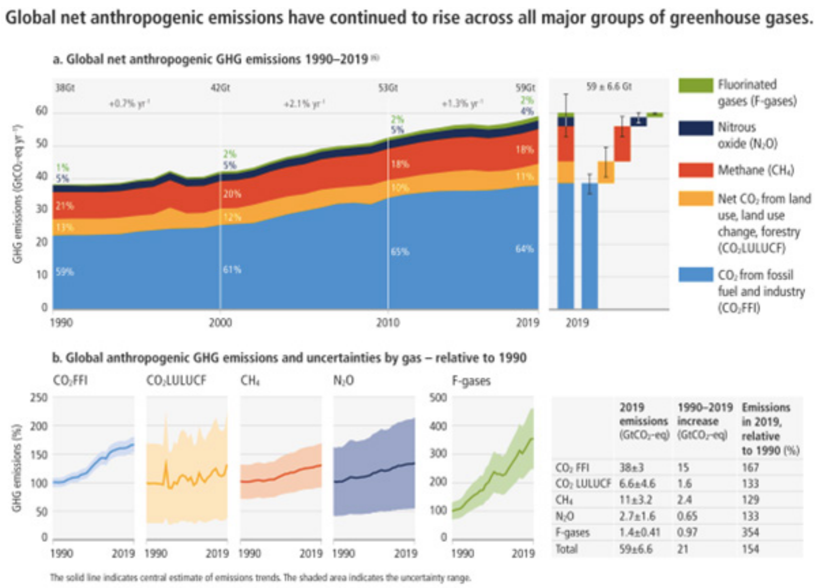
1- We are on track for 3˚C without immediate and deep emission cuts that peak by 2025

The IPCC research demonstrates that during the period from 2010 to 2019, annual emissions continued to grow, though at a lower rate than in the previous decade, with 59 billion tonnes of C02e added to the atmosphere in 2019. To put this into perspective, globally we emitted the equivalent weight of 121 million jumbo jets in 2019 alone.

The IPCC findings show that the climate crisis is about much more than just fossil fuels. The report assesses activities across the whole economy, from construction to cattle, retail to real estate and fashion to forestry. To take the livestock sector as an example, if cattle were a country they would be the world's third highest emitter of greenhouse gases.

Furthermore, the IPCC finds that nations and non-state actors are falling short on net zero targets. Even with current climate pledges, the world is on track to reach a 3˚C [2] irreversible warming scenario. The authors of the research found that in order to limit temperature rises to 1.5˚C, emissions need to peak before 2025 and reduce by 43% by 2030, reaching net zero by 2050.

Figure 1: Global net anthropogenic GHG emissions (GtCO2-eq yr-1) 1990–2019



Source: IPCC (2022) Figure SPM.1

2- Incentivise action through market and regulatory instruments

The report points to the power of economic and political tools in driving action. Decision makers can generate a reduction in fossil fuels by, for example, policies that introduce carbon pricing mechanisms or those that remove fossil fuel subsidies. Financial incentives can also be used to stimulate positive action, such as boosting carbon-cutting technological innovation. Evidence has shown that mitigation policies have led to a

[1] As calculated by Carbone 4 based on the portfolio as of year-end 2021. More information available here: https://www.gam.com/-/media/content/featured-funds/gam-climate-bond-impact_report_202205_en_online.pdf.

[2] IPCC, AR6, WGIII, Full Report, 2403

[3] IPCC, AR6, WGIII, Full Report, 60

reduction in greenhouse gas emissions , yet more regulation and financial opportunities are needed for a sustainable transition.

In the financial sector, regulation is taking place in the form of risk management and disclosure, such as the rollout of the Task Force on Climate-Related Financial Disclosures and the recently proposed US SEC rules, which form the basis for how markets can better manage climate risk. These developments help to hold companies and financial markets to account, encouraging positive action among corporates.

It is clear from the report, however, that commitments from financial institutions must rapidly turn into action at portfolio level.

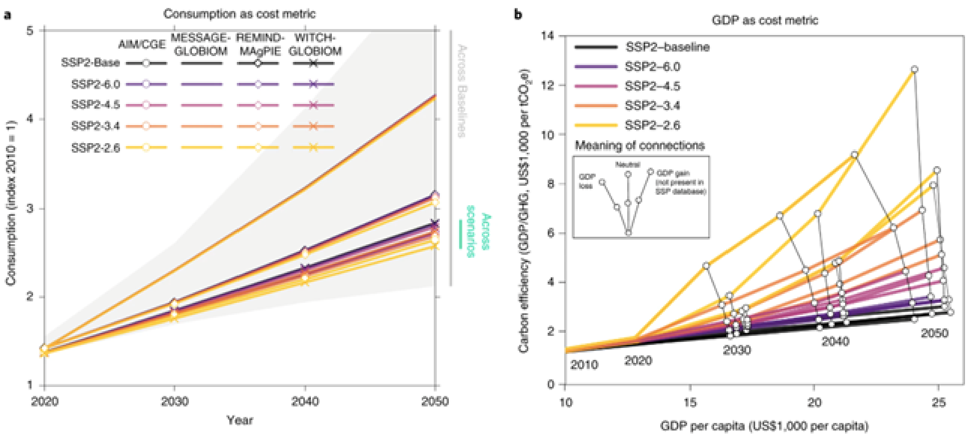
3- Much more finance is needed to curb global warming

In short, acting now is critical but this action requires funding, with IPCC warning that climate finance is currently three to six times lower[4] than what is needed to keep warming below 2˚C.

Total climate finance for mitigation and adaptation is estimated at up to USD 385 billion per year, the equivalent of delivering the US Covid-19 rescue plan every year.

The costs of inaction will, however, be greater still. A study by consultancy firm Deloitte estimated that the cost of inaction on the US economy would be USD 14 trillion over 50 years. Moreover, research shows that capital expenditure on climate mitigation leads to growth across many sectors of the economy. Investors must scale up funding to support deep emission cuts and spark innovation for clean technologies.

Figure 2: Mitigation costs in a growing economy



a, Consumption growth variation across baselines, models and mitigation scenarios. The green bar indicates the results range of the WITCH-GLOBIOM model. The grey wedge is the range of consumption growth across all SSP baselines from the SSP database. **b**, Producing more (GDP) with less (GHG emissions). Model results from four IAMs with endogenous GDP estimation for scenarios that combine middle-of-the-road socioeconomic assumptions (SSP2) with five different levels of climate change mitigation stringency. Thin black lines in **b** indicate GDP per capita mitigation frontiers for milestone years for each model. Perfectly vertical lines would indicate no reduction in GDP per capita. Negative slopes indicate decreasing GDP per capita with growing mitigation effort. See Supplementary Section 4 for variations of **b** using other SSP scenarios. Data source: SSP database[135].

Source: Köberle et al. (2021)

[4] IPCC, AR6, WGIII, Full Report, 185

WHAT'S NEXT?

A Synthesis Report is due to be published in September later this year. This will integrate the three latest Working Group reports, as well as the most recent IPCC Special Reports on Global Warming of 1.5°C, Climate Change and Land, and The Ocean and Cryosphere in a Changing Climate.

COP delegates recently convened to consider the impacts of the IPCC's findings from the Working Group II paper and how to ensure science is at the forefront of the global response at the climate conference in Egypt later this year. We will be closely watching to see how these discussions evolve and incorporate the findings of the latest crucial mitigation report.

To learn more about the findings of the WGIII IPCC, the full report is available to download here.

For more information about sustainability at GAM Investments, please click here.

For more insights from GAM, please visit 'Our Thinking' page here.

GAM's purpose is to protect and enhance our clients' financial future. By attracting and empowering the brightest minds to think beyond the obvious, we strive to provide investment leadership, innovation and a positive impact on society and the environment.

STEPHANIE MAIER

Global Head of Sustainable and Impact Investment

Stephanie Maier is Global Head of Sustainable and Impact Investment, responsible for leading GAM's sustainable and ESG (environmental, social and governance) strategy.

Stephanie joined GAM Investments in January 2021 from HSBC Global Asset Management, where she was Director for Responsible Investment. Prior to that, she spent seven years at Aviva Investors, latterly as Head of Responsible Investment Strategy and Research, and was formerly Head of Research for EIRIS, an ESG research and consultancy firm.

Stephanie holds an MSc in Environmental Technology from Imperial College London, a BA in Biological Sciences from Oxford University and the Investment Management Certificate (IMC). She is based in London.

For more information, please visit GAM.com

2008 01/08/2022