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Feature Articles

This month's focus: **Asset Management in the Carbon Neutral Era**

The role of finance in realizing a decarbonized society is not just to mobilize the necessary funds. The transition to a decarbonized society inevitably transforms the industrial structure. As a result, if employment is lost or Japan's industrial competitiveness is reduced, decarbonization may in fact be disrupted. Investors and financial institutions investing in diverse companies through the market will be asked how to draw society's future as part of their own transition strategy.

As local authorities, nations, and corporations raise their voice to commit to achieve carbon neutrality, expectations regarding the role of financial institutions have also been increasing. In order to aid asset managers embarking on their journey of climate/ESG consideration, this paper aims to clarify and understand:

- the relationship of climate change and other environmental and social factors with existing portfolio analysis models;
- the current state of disclosure standards and evaluation models needed for analysis; and
- the key characters needed to build an effective team for integrating climate/ESG factors into the fund management process, including leveraging the growing pool of training/certification programs.

This article is a condensed version of Weathering Climate Change, a Megatrends paper published by PGIM in spring 2021. The full version of the paper including all sources and references can be obtained online via
https://cdn.pficdn.com/cms/pgim-japan/sites/default/files/2021-03/E_PGIM_Megatrend_Weathering-Climate-Change_20210319.pdf

Climate change is no longer a hypothetical risk. Though policymakers, businesses, and activists may disagree on many aspects, there is one indisputable fact: the air and water on our planet are warming – and this global warming is accelerating.

While our climate destiny is largely predetermined over the next two decades, there is still massive uncertainty for long-term investors looking to navigate climate change, which is spurring a generational reallocation of resources and leading to the emergence of a new set of winners and losers by country and by sector.

No one can perfectly predict the dynamics of asset price adjustments as climate risks become internalized – or whether adjustment will be smooth or abrupt – but a repricing will occur, and investors will need to be prepared.

In this paper, we propose an actionable climate change agenda for institutional investors, encompassing both hidden portfolio vulnerabilities and potential opportunities in the transition to a lower-carbon world.

At PGIM, we believe active investors must be on the front foot, predicting and responding to the impact of climate change on the economies and our markets in which investors operate. This will create both immense uncertainty and opportunity. Only forward-looking, long-term investors will have the nimbleness and foresight to seize the opportunities and navigate the risks accompanying our changing climate.

The impact of climate change risk on a company's business and financial performance will be widespread and massive. Investors will either mitigate the risks associated with the transition to a low-carbon economy through carbon footprint reduction and integration, or capture opportunities through investing in climate solutions. In addition, a strategy to comply with the Paris Agreement, which aims to achieve the 1.5°C target, is emerging. While we see challenges such as the availability and quality of emission data, we believe that the incorporation of climate change risk into equity management will continue to progress.

36th SAAJ Annual Conference: *Role of Corporations and Securities Analysts in Heralding an Era of Post Pandemic: Now is the time for structural reform in Japan*

Prospects