ESG Viewpoint

The road to net zero

April 2021

BMO GAM’s net zero commitment

In December 2020, BMO Global Asset Management announced an ambition to reach net zero emissions by 2050 or sooner across all assets under management, as a founder signatory to the Net Zero Asset Managers initiative.

This commitment builds on our existing actions on climate change, which include:

- An **active engagement approach**, asking our investee companies to adopt net zero targets;
- The incorporation of climate change into our **voting policy**, where we will vote against management at companies that fall short of our standards; and
- **Carbon neutrality** and **100% renewable electricity** in our operations, as part of a wider commitment by BMO Financial Group

It also forms a key part of our parent company BMO Financial Group’s climate ambition, to be our clients’ lead partner in the transition to a net zero world.
2021 will see us working on implementing our approach to managing our assets in line with our new net zero commitment. We will set an interim assets under management (AUM) target for assets to be managed according to net-zero principles ahead of this year’s critical COP26 climate negotiations in Glasgow, UK in November.

Why net zero?
The 2018 report of the Intergovernmental Panel on Climate Change (IPCC) made two things crystal clear. First, the risks to people and the planet from climate change become far more serious as the global temperature rise tips over the 1.5°C threshold. And second, keeping temperatures below that threshold means we must transition to a net zero global economy by 2050 at the latest – with any remaining greenhouse gas emissions from human activities at that time balanced by the removal of CO2 from the atmosphere.

Governments are responding – and with President Biden intent on setting a net zero goal for the US, we can expect that by the time of the COP26 negotiations, countries responsible for almost 80% of global GDP will have pledged net-zero emissions by 2050 (or 2060, for China and Brazil). Corporates are shifting too, with almost 1,400 now having net zero targets, according to the UN Race to Zero campaign.

It’s time for financial institutions to match that ambition – and more than that, to use our influence to support the wider economy through a rapid and just low-carbon transition.

“Asset managers have a unique and critical role to play in the transition to global net zero emissions. We look forward to building partnerships both with our asset owner clients, and with the companies we invest in, to move together on the journey to making this a long-term shared goal.”

Kristi Mitchem, CEO, BMO Global Asset Management

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Principles for action

As we work on putting our commitment into practice, we have established some principles that will govern our approach.

**Principle 1: Focus on real-world emissions reductions**

We know that we can cut a portfolio’s carbon intensity dramatically, just by selling companies in highly energy-intensive sectors like electric utilities and industrials, and replacing these with companies in lower-emissions industries. But such portfolio changes alone make little difference in the real world. Our ambition is to use the power of our engagement, working in collaboration with other investors, to influence companies to take action – and as their emissions fall, so then will the carbon content of our investment portfolios. However, engagement can’t be open-ended. If companies fail to respond, and remain fundamentally misaligned with a low-carbon future, we will need to re-consider our investments in them.

**Principle 2: Work in partnership with clients**

As asset managers, our fundamental responsibility is to meet our clients’ current and future investment needs. We believe that net-zero investing is supportive of the responsibility – but we also understand that many of our clients still have many questions about what this means, and we need to be mindful of the existing mandates we have with them. Our aim is to work in partnership with our clients, providing education on what the low-carbon transition means when applied to portfolios. In practice, this means we may be able to move some of our assets to a net zero-aligned pathway earlier than others – which is why we will set an interim AUM target, with the intention that this will ratchet up over time.

**Principle 3: Transparency**

The risks of ‘net zero-washing’ are real. Methodologies on net zero investing are still emerging, and disclosure by corporates is patchy, despite the progress made since the publication of the Task Force on Climate-related Financial Disclosures. However, the urgency of the issue is too great to wait until we have all the building blocks fully in place. In this context, it is important that we are straight with our clients and wider stakeholders about limitations in our approach, including gaps in data or methodology. We will seek to avoid ‘black box’ approaches, or simple metrics which could obscure a more complex reality.
Defining a ‘net zero aligned’ investment portfolio is no straightforward task. To guide our implementation, we are looking to the Net Zero Investment Framework, developed by the Paris Aligned Investment Initiative, with input from BMO GAM. This is a comprehensive framework, covering governance, target-setting, methodologies for specific asset classes, and policy and stakeholder engagement.

Methodological framework

BMO GAM is currently co-chairing the Implementation Working Group, aimed at sharing experiences between asset owners and managers working with the Framework, and producing further guidance on its application.

The Framework sets out detailed guidance on:

- **Portfolio-level targets** for emissions reductions, consistent with a fair share of a 50% cut in global emissions by 2030, and net zero by 2050
- **Analysis of underlying assets** (companies, countries or other assets) on a forward-looking basis, to understand whether these are on a trajectory consistent with the net zero transition
- **Investment in solutions** – recognising that as we decarbonise the emissions-intensive economy, we need a huge scaling up in finance for green activities

An important evolution embedded in this approach is the shift in emphasis from a historical, backward-looking metric – portfolio carbon emissions – towards a greater focus on analysis of the likely future trajectory of these emissions.

To take listed debt or equity issuers as an example, we will aim to assess the extent to which companies in our portfolios are aligned to a 1.5°C future. In doing so, we will seek to understand how these companies compare with decarbonisation pathways for their own sector, rather than take the same approach for all – recognising that decarbonisation challenges, and the availability of technological solutions, vary significantly by industry. We also believe it is important to look not just the ambition of company targets, but also the credibility of plans to implement these – taking into account factors such as their governance approach, whether there are shorter-term interim targets in place, and whether capital expenditure plans are tilting towards a greener approach.

Such analysis is complex, and the data challenges are considerable. But the work of organisations such as the Transition Pathway Initiative, the Science-based Targets Initiative, and the Climate Action 100+ initiative in its recent benchmark report are all examples of this more nuanced approach.

BMO Financial Group is also focusing on enhancing the availability of high-quality data on climate risks and opportunities, through the creation of the BMO Climate Institute, which will partner with industry, governments, academia and investors.
COP26 and beyond

2021 is a crucial landmark year in the fight to tackle the climate crisis, and every part of society needs to play its part. We will continue our engagement with companies and our efforts to decarbonise portfolios, supporting the low-carbon transition in the real economy – and will also be part of the collective investor voice calling on governments to be visionary and ambitious in the way they approach the Glasgow COP26 negotiations. Strong action now is essential to set the world on a trajectory to a more stable climate and a healthier planet.

“Our collective responsibility is to ensure that a better future is not only possible but probable, and then not only probable but foreseeable.”

Christiana Figueres and Tom Rivett-Carnac,
The Future we Choose: Surviving the Climate Crisis, 2020
Responsible Investment – a glossary of terms

Its wide-ranging nature means that responsible investment involves a host of associated language and jargon. Here we explain some of the most commonly used terms.

Get to know the author

Vicki Bakhshi, Director, Responsible Investment

Vicki Bakhshi has worked at BMO GAM since 2006, focusing on climate change engagement and strategy. Prior to BMO, Vicki worked as advisor to the UK Prime Minister on international climate policy from 2003-2005. Outside of work she enjoys trail running, and spending time with her two boys.

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