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THE GREEN FINANCE PARADOX: WHY ASSET MANAGERS SEE POTENTIAL IN HIGH EMITTERS

From clean power generation capabilities to carbon capture technologies, impact investing allows investors to build a sustainable portfolio and a cleaner future



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Instead of divesting from high carbon-emitting businesses, investors can drive meaningful change by financing transitions to low-carbon operations.



Transition finance

THE global race to achieve net-zero goals demands more than just investing in new green assets.

Existing carbon-heavy industries have to be transformed at the same time in order for the global economy to successfully transition to net zero.

Industries such as steel, cement, transportation and chemicals account for approximately one-quarter of the world's energy consumption and around one-fifth of overall carbon dioxide emissions, the International Renewable Energy Agency (IRENA) has estimated.

These hard-to-abate sectors, while integral to the global economy, pose some of the

greatest decarbonisation challenges. Therein lies a significant opportunity for impactful investment.

Rather than avoiding or divesting from high carbon-emitting businesses, investors can finance their transition into low-carbon operations. Such investments not only allow investors to tap into a wider spectrum of transition opportunities, but also position their portfolios for long-term growth and resilience while contributing to global climate goals.

Alternative investment firm Brookfield Asset Management terms such a strategy "going where the emissions are". By focusing on heavy emitters, investors can help utility companies develop clean power generation capabilities, and support industries such as cement and steel to reduce emissions in their

manufacturing processes.

Says Connor Teskey, chief executive of Brookfield Renewable and president of Brookfield Asset Management: "Without doubt, for many of the most attractive and most impactful decarbonisation investments globally, decarbonisation and value creation are complementary. We feel these represent some of the largest and most attractive risk-adjusted return opportunities in the transition investing space."

Challenges to decarbonisation

Decarbonisation is an immense challenge that requires an average annual investment of US\$7 trillion (S\$ 9.45 trillion) over the next 25 years, more than triple the investment levels of 2021, according to energy research firm BloombergNEF.

To date, much of the investment has flowed into sectors with proven and financially viable technology, such as solar and wind. Despite this advancement, more than 60 per cent of the world's power sources still run on fossil fuels as of 2023, according to the International Energy Agency (IEA).

This dependence must fall to 30 per cent by 2030 for the world to stay on track to achieve net-zero emissions by 2050, the IEA estimates. Complicating matters, energy demand continues to surge due to the electrification of vehicles, heating systems and other sectors.

This dual challenge places tremendous pressure on utility companies, which must not only transition their operations to clean energy but also expand capacity to meet growing demand.

Brookfield estimates that utilities will have to increase their total clean energy capacity

by around 19 times to achieve both these goals. Crucially, these cannot be achieved by building new clean energy capacity alone.

Existing fossil fuel infrastructure must also transform.

At the same time, other carbon-intensive industries such as steel, cement, and chemicals remain in the early stages of adopting sustainable practices.

The cement industry, for instance, is piloting carbon capture technologies, while steel manufacturers are transitioning to cleaner production methods using hydrogen instead of coal.

While these innovations represent promising steps forward, they remain prohibitively expensive compared to traditional methods, underscoring the need for more investment and technological advancement.

Importance of private capital

Achieving net-zero emissions therefore requires a comprehensive strategy that combines ongoing investment in clean energy and technology with the active decarbonisation and replacement of existing carbon-intensive infrastructure.

This dual approach is essential because, if left unchanged, the emissions from current fossil fuel infrastructure would exceed the world's carbon budget by 2030.

Carbon budget refers to the maximum amount of permissible carbon dioxide emissions while still limiting global temperature rise to a specific target, such as 1.5 deg C above pre-industrial levels as outlined in the Paris Agreement. Staying within this limit requires sustained financial support to accelerate the transition.

Private capital plays a pivotal role in this process because it can commit to long-term investments without the constraints of short-term shareholder pressures. This makes it uniquely positioned to fund the transformation of utilities and heavy-emitting industries, which require both substantial capital and time to adopt sustainable practices.

Brookfield exemplifies this patient approach by partnering with industrial companies and innovators in areas with high emissions through long-term contracts. For example, it has committed to a funding partnership of up to US\$1 billion in LanzaTech, a US-based company that has developed a technology that captures carbon emissions and converts



them into ethanol, a type of alcohol that can be used as fuel. This technology is already being used at major industrial sites, such as ArcelorMittal's steel plant in Ghent, Belgium, where it is helping to reduce emissions from steel production.

Brookfield's strategy extends to transforming existing high-emission industries. By supporting companies like ArcelorMittal in their adoption of new green methods of production, the asset manager is driving significant reductions in carbon emissions while demonstrating how established industries can evolve towards net-zero goals.

This approach enables Brookfield to identify and support innovative technologies that might otherwise be overlooked.

“Investors who are unwilling to take on initial carbon emissions can risk missing out on a transformational opportunity from both an economic and an environmental standpoint,” says Teskey.

“Going where the emissions are enables investors to target a wider spectrum of transition opportunities, finding more situations to invest for more. It also allows investors to tie their decarbonisation objectives to appropriate risk-adjusted economic returns that will make a meaningful contribution to our collective climate goals.”



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