

In Full Flow:
*Sovereign wealth funds
mainstream climate change*



Message from OPSWF

This year, the One Planet Sovereign Wealth Funds Network's key priorities were to further support sovereign wealth funds, asset managers, and private investment firms in the implementation of the principles of the OPSWF Framework.

These included outreach to new members to expand the adoption of the Framework, sharing best practice through peer exchanges, notably on methodologies to measure portfolio carbon footprints, improving climate-related financial disclosures and the global support for the Task Force on Climate-related Financial Disclosures (TCFD) recommendations. The Network also briefed members on climate investment strategies and solutions across sectors and regions. Network members have launched collaborative projects to support the market and the financial system in accelerating the implementation of the Paris Agreement, by identifying and assessing climate-related risks and opportunities, and developing enhanced ESG strategies, with a focus on climate, to better inform and guide sovereign wealth funds' priorities as long-term investors and universal asset owners.

The fourth Annual OPSWF CEO Summit, which was hosted by President Emmanuel Macron from the Elysée Palace on 4 October 2021, was attended by the US Special Presidential Envoy for Climate, John Kerry. The Summit provided increased momentum within a reinforced global Network of now 43 members across continents, comprising 18 sovereign wealth funds, 17 asset managers, and eight private investment firms, with over \$36 trillion in assets under management and ownership. Members announced their further support for the recommendations of the TCFD as a universal standard, with an emphasis on private investment firms increasing the climate disclosures of unlisted portfolio companies. Additionally, members committed to identifying investment enablers for private-sector financing of the energy transition in emerging markets and scaling green-hydrogen production globally. They presented a selection of over a hundred climate-related investment actions, including data points, with a demonstrated positive impact on reducing carbon emissions, chronicled in the 2021 OPSWF Framework Companion Document.

The fifth Annual OPSWF CEO Summit will take place in Abu Dhabi in 2022.

Introduction



In September 2020, the International Forum of Sovereign Wealth Funds (IFSFW) partnered with One Planet Sovereign Wealth Funds (OPSWF) to undertake the first comprehensive survey of sovereign wealth funds' attitudes towards climate change and their actions to mitigate its effects, finance the energy transition and fund technologies that will help the world adapt to a warmer climate.

We published the results of that survey in [*Mighty Oaks from Little Acorns Grow: Sovereign wealth funds' progress on climate change*](#) in February 2021. The report revealed that most sovereign wealth funds were aware of the potential impact of climate change on their portfolios. The majority of them agreed that "without action, climate change will have a material negative impact on economic growth" and that, unchecked, climate change would leave future generations worse off. However, many were only starting to implement strategies and practices that would help them adapt their portfolios to this challenge and reduce their environmental impact, hence preparing the ground for more actions to come.

Despite the many difficulties arising from the ongoing COVID-19 pandemic, climate change has remained at the top of the investment agenda. Like other asset owners, sovereign wealth funds have continued to take this issue seriously, as demonstrated by the expansion of OPSWF in 2021 to 19 members. In 2020 and 2021, OPSWF also published a [Companion Document](#)¹ to demonstrate the investments and actions which sovereign wealth have undertaken.

Twelve months after undertaking our first survey, IFSWF and OPSWF have once more collaborated to understand how sovereign wealth funds' thinking and action has progressed on climate change, in what we hope will be an annual process.

¹ The Companion Document outlines investment practices from OPSWF Network members, asset managers and private investment firms.

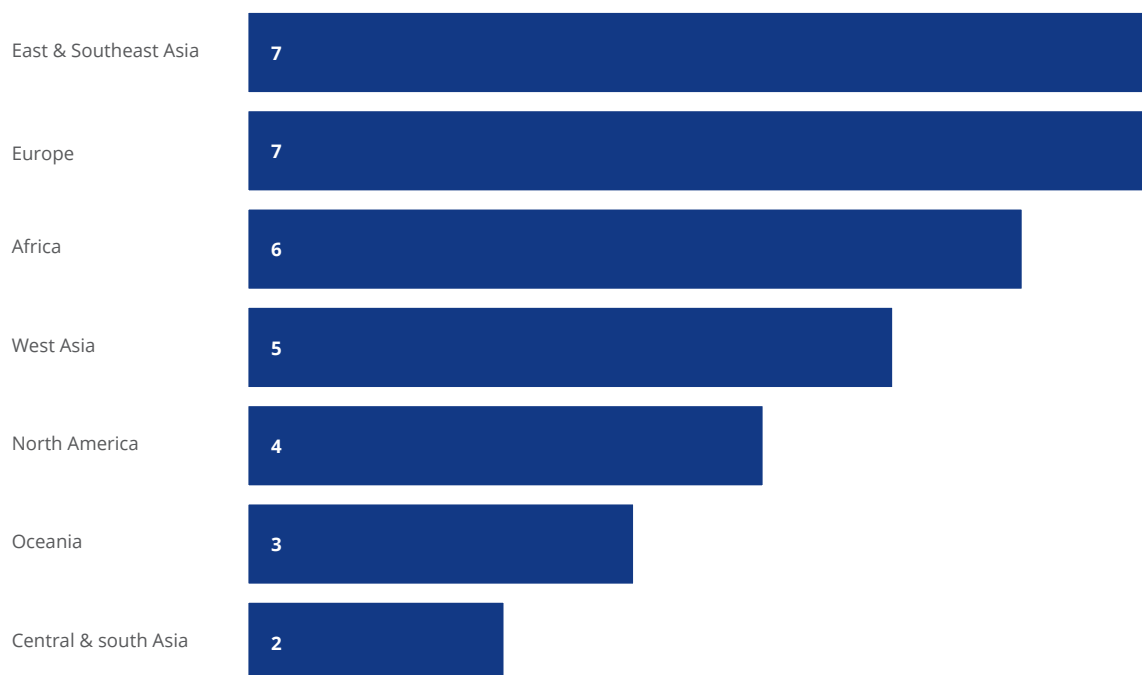
About the Survey

For this project, we distributed a survey to 46 sovereign wealth funds, primarily members of IFSWF and OPSWF. Thirty-four institutions (74%) responded.

These responses represent the views of 42% of the world's 81 sovereign wealth funds. While the survey was anonymous – so we do not know which institutions completed the survey – the distribution list included all the world's largest sovereign wealth funds with total assets under management of more than \$5.75 trillion, over 90% of sovereign wealth funds' total assets under management, according to the IFSWF's database.

It should also be noted that the survey was distributed to two more institutions than last year, and we received the same number of responses (34). As a result, we believe that the results of the two surveys are directly comparable where the same questions were asked. Moreover, respondent institutions broadly represented the total distribution of sovereign wealth funds, as shown in the chart below.²

Chart 1 Geographic distribution of respondents (2021)



Source: IFSWF-OPSWF Climate Change Survey 2021

The 2021 survey was shorter than the original questionnaire and concentrated on the practical challenges of integration and implementation of climate change into the investment process, rather than on the respondents' alignment of views on climate change. Last year's survey results showed an overwhelming agreement that human activity has accelerated climate change, that it will have a material negative impact on long-term economic growth and will leave future generations worse off. Consequently, we did not consider it necessary to revisit these questions. Instead, we wanted to focus on the practical steps sovereign wealth funds are taking and the challenges they are facing in addressing climate change, as well as the opportunities deriving from asset (re)allocation.

² Please note, we have used slightly different regions this year, so the geographical distribution is not directly comparable to that we published last year.

Streaming Ahead

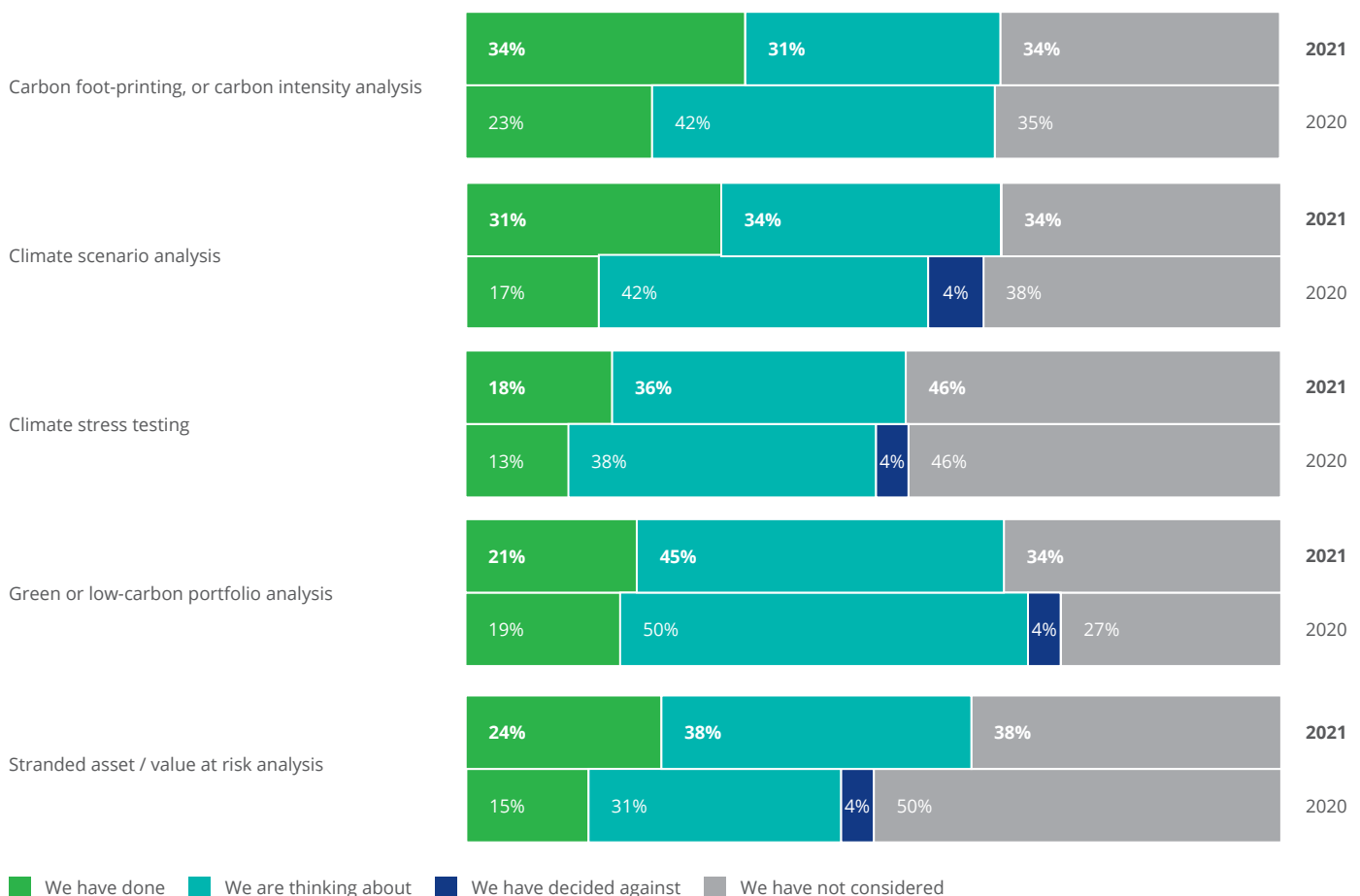


The 2021 IFSWF-OPSWF Climate Change Survey reveals that sovereign wealth funds have made substantial progress in addressing climate change and that they have become more systematic in their approach. In 2020, only 24% of respondents to our survey incorporated environmental, social and governance (ESG) considerations in their investment process and only 18% had a dedicated ESG team, while 48% told us that they did not take a systematic approach to climate change.

Twelve months later, 71% of respondents have adopted an ESG approach and less than 10% told us that they didn't consider climate change in their investment approach at all, while only 20% of the respondents considered climate change in an unsystematic manner. It is not, therefore, surprising that 60% of our respondents have adopted their ESG or climate-related strategy since 2019; 23% adopted it this year, and 37% adopted their ESG strategy in 2019 or 2020.

Over the past year, sovereign wealth funds have rapidly expanded their use of five different methods of assessing climate-related risks and opportunities to better understand their portfolio exposure to climate-change risks, manage and reduce their climate impact. For example, 34% of respondents have now carbon footprinted their portfolios, up from 23% last year. Similarly, 31% now use climate-scenario analysis versus 17% in 2020. Similar progress can be seen in climate stress-testing, green- and low-carbon portfolio analysis and stranded value/assets at risk analysis.

Chart 2 Have you assessed the climate-related risks and opportunities in your portfolio?
(comparison between 2020 and 2021)



Source: IFSWF-OPSWF Climate Change Survey 2021

The survey also revealed that while only 9% of respondents reported that they were mandated to address climate change, almost two-thirds of our respondents (65%) are proactively adopting such an investment approach, rather than waiting for it to be included in their mandate, many of which were written years, or even decades ago, and could be bureaucratic or politically challenging to update. Overall, sovereign wealth funds are doing this because they believe that it is “the right thing to do” (50%) with 23% saying they thought it would boost returns and 27% saying it would reduce risks to their portfolio.

Chart 2.1 Is addressing the effects of climate change part of your mandate? (2021)



Source: IFSWF-OPSWF Climate Change Survey 2021

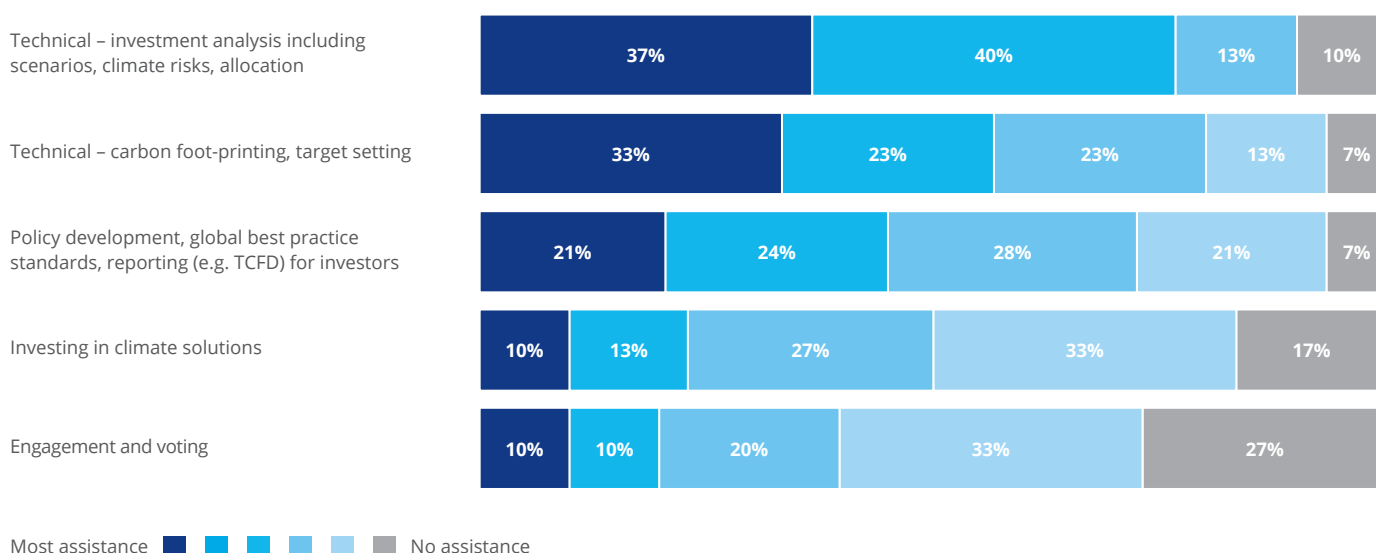
An important reason why these sovereign wealth funds have been able to adopt these strategies is that stakeholder opposition has declined over the past year. In 2020, nearly a fifth of respondents reported that a substantial obstacle to adopting an ESG or climate change investment approach was that stakeholders did not believe these issues to be important. This year this proportion had dropped to only 3%. As a sovereign wealth fund’s board is most frequently the body responsible for approving the adoption of these strategies, this transformation of opinion has removed a substantial obstacle to sovereign wealth funds adopting and implementing ESG approaches.

Tooling Up

Sovereign wealth funds are also investing in developing their climate change or ESG approach. However, as all of them have different structures, mandates and complexities, sovereign wealth funds have not all adopted the same approach to implementing their climate change approach. While 41% of respondents told us that they were planning on upskilling their investment teams, 38% said they were either expanding or establishing a dedicated ESG team. As such, it appears that sovereign wealth funds have broadly adopted two approaches, one where they are working to train their investment teams and embed ESG practices into their existing investment teams and processes, and the other where a dedicated team will be overseeing their approach to climate change. Both of these approaches are used across financial services, and one trend to watch will be whether one or other of these approaches proves to work better in the context of a sovereign wealth fund. Regardless of the approach, sovereign wealth funds are taking climate issues seriously and are expanding their capabilities in this area.

It is this aspect of adopting their climate change or ESG strategy with which sovereign wealth funds say they need the most assistance. The issues that were the most pressing for the survey respondents were technical challenges such as investment-analysis-like-scenarios, as well as carbon footprinting and target setting. On the whole, sovereign wealth funds needed less assistance with climate policy development investment practices and engagement, which were likely to have already been set.

Chart 2.2 What climate-related topics does your organisation need the most assistance with? Rate 1 to 5, where 5 is the most assistance (2021)



Source: IFSWF-OPSWF Climate Change Survey 2021

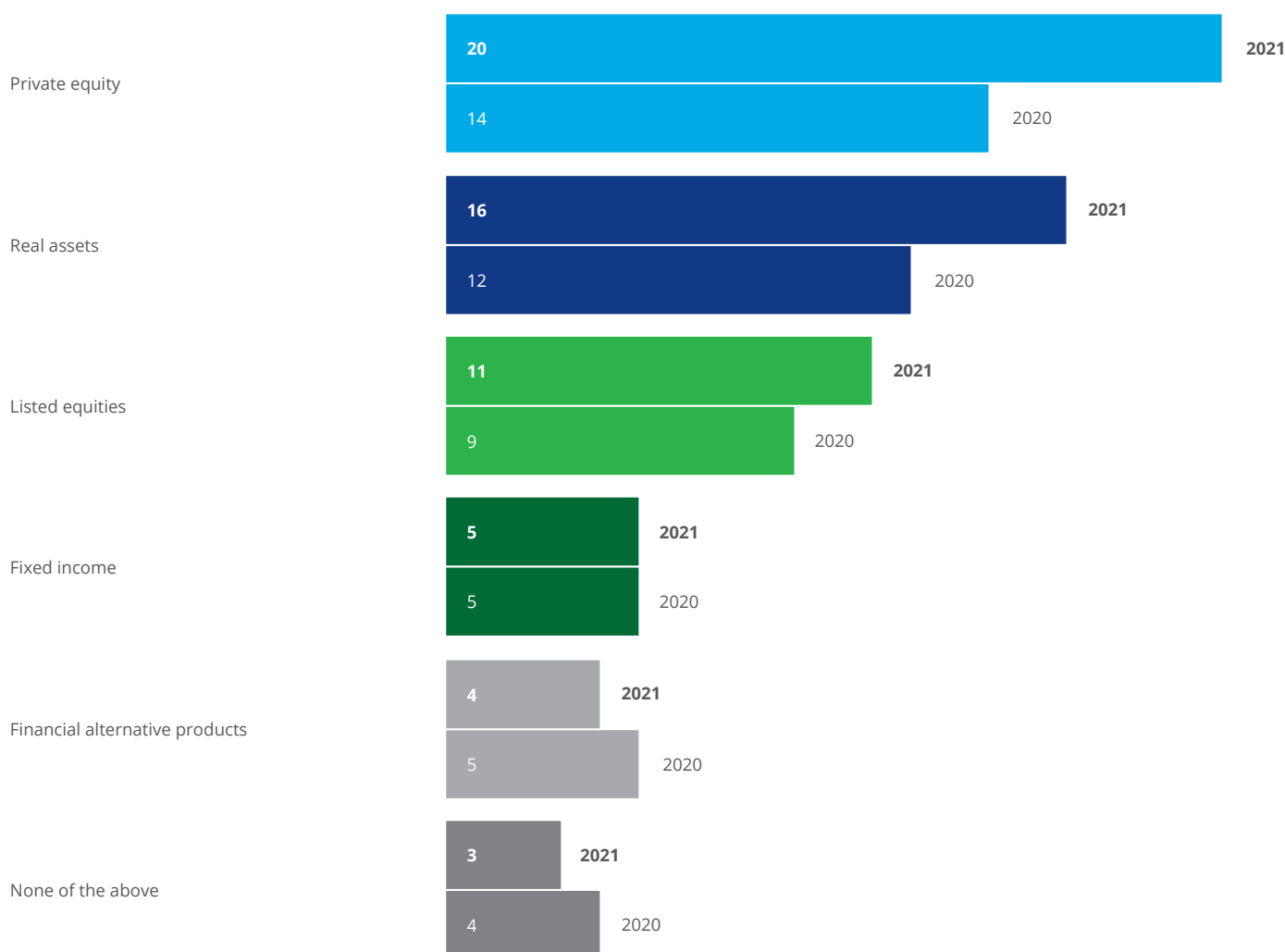
An important caveat is the length of time over which these changes will take effect. Some sovereign wealth funds have large portfolios managed by large internal teams, across a large number of asset classes and types. Undertaking this type of transformation in the way their assets are managed can be complex and take longer than either the fund or their stakeholders would like. Consequently, measuring real progress on ESG integration, cutting the carbon footprint of their portfolios and the adoption of targets and metrics for carbon reduction, rather than speed of implementation, will be key to understanding how sovereign wealth funds are performing going forward.

Expanding investment horizons for impact

So far, we have concentrated on the integration of ESG and climate-change considerations into sovereign wealth funds' investment processes. It is important to remember that not only are they managing risks, but also seeking out new opportunities to finance the energy transition and fund technologies that will help the world adapt to climate change. As large pools of long-term capital sovereign wealth funds are in a good position to put their assets to work in investments that can have an at-scale impact on carbon reduction.

Overall, sovereign wealth funds continue to favour more established opportunities in these spaces. For example, renewable energy remains the most popular investment sector, with 70% of respondents saying it was the most attractive climate-related sector, broadly in line with our findings last year.

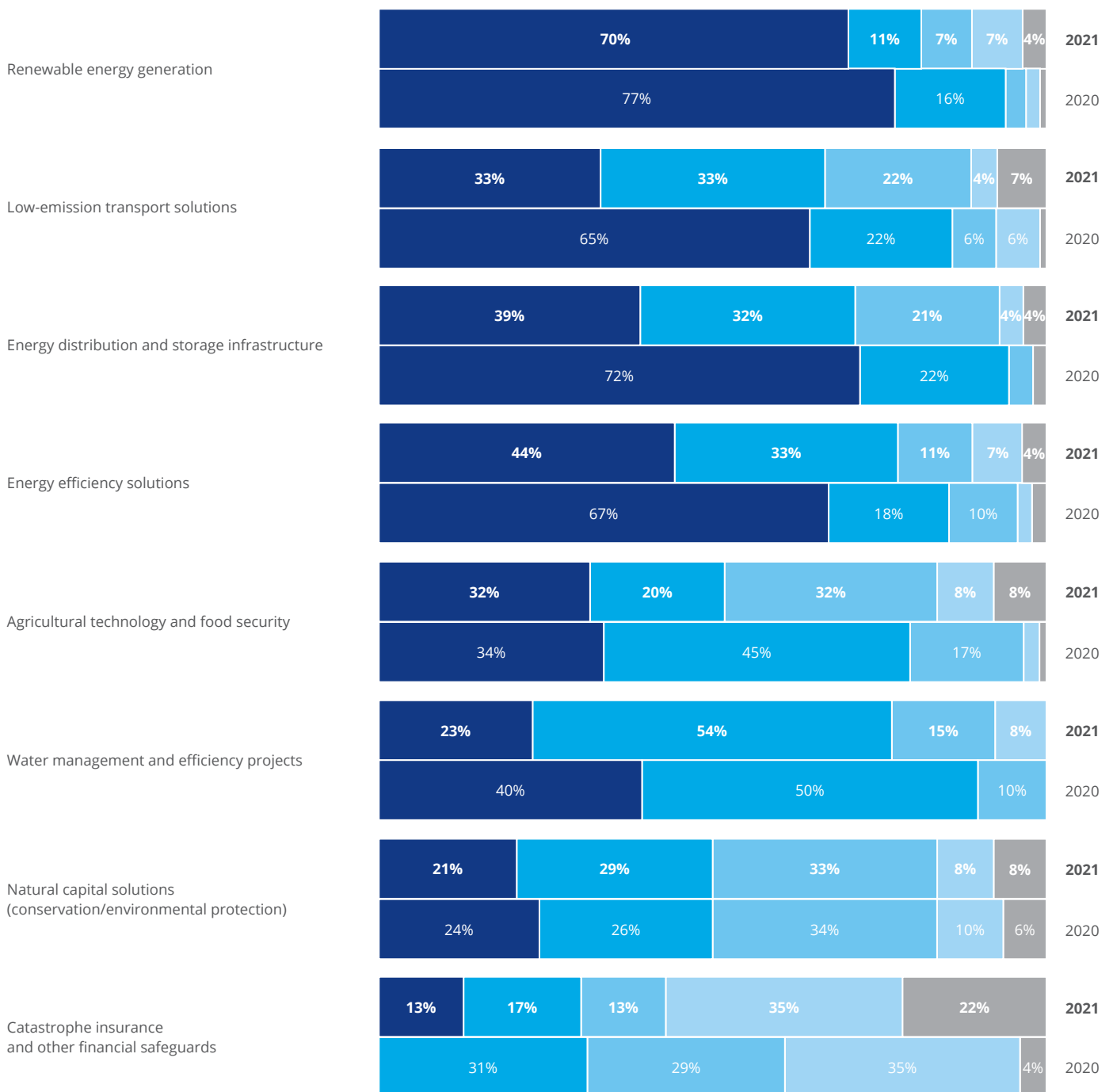
Chart 2.3 In which asset classes do you pursue targeted portfolio construction for climate change-related purposes? (comparison between 2020 and 2021)



Source: IFSWF-OPSWF Climate Change Survey 2021

Equally, as they did last year, private equity, real assets and listed equity continue to be the most usual asset classes for sovereign wealth funds to pursue targeted portfolio construction for climate-change-related purposes, and this is borne out in the OPSWF [Companion Document 2021](#). As we observed last year, these tend to be the most straightforward for investors to tackle.

Chart 2.4 In which sectors do you see the best investment opportunities?
Please rate 1 to 5, where 5 is the best (comparison between 2020 and 2021)



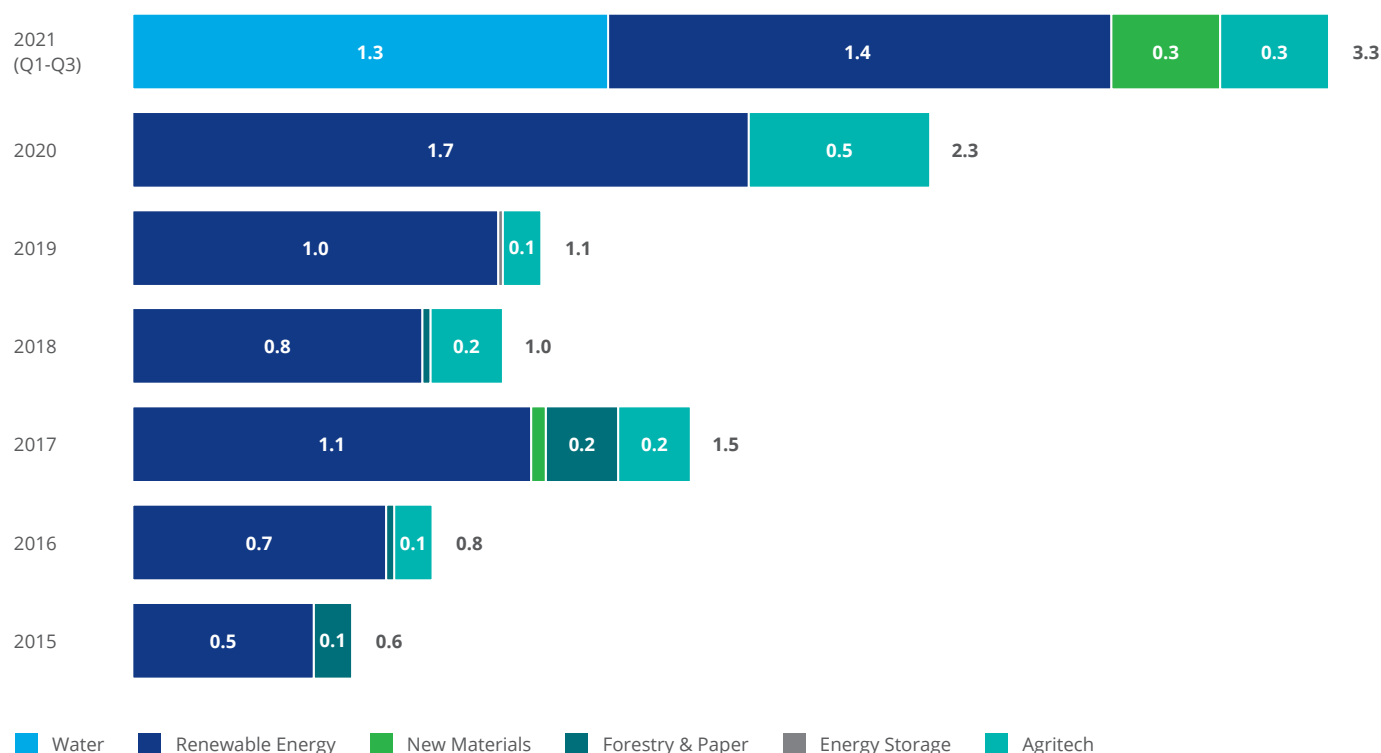
Most attractive ■ ■ ■ ■ ■ Least attractive

Source: IFSWF-OPSWF Climate Change Survey 2021

However, our survey results provide some indication that sovereign wealth funds are beginning to look at a wider range of climate-related investment opportunities. The charts show that the distribution of opinion of the attractiveness of a range of climate-related sectors has become wider at both ends of the preference spectrum as shown in chart 2.3. Putting these findings in the context of greater adoption and learning about climate change and ESG among sovereign wealth funds suggests that they have investigated a wider range of opportunities more thoroughly over the past year and have developed a more detailed and nuanced view of where attractive investments lie.

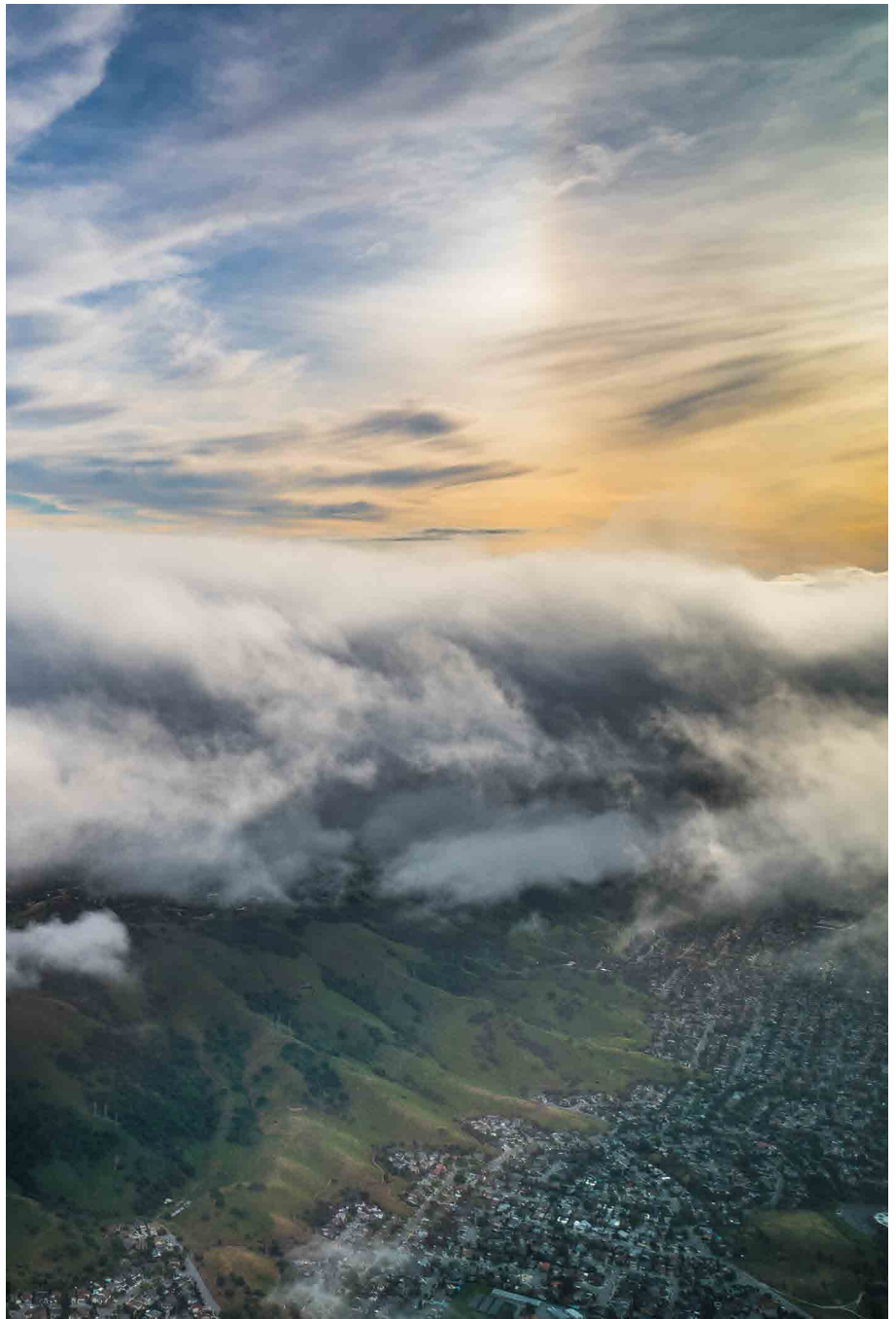
As sovereign wealth funds become more knowledgeable and create dedicated capacity, this trend suggests that they may embrace a wider range of investment opportunities including catastrophe insurance and other financial safeguards. Indeed, IFSWF data already shows that sovereign wealth funds are making a broader spread of investments in climate-related sectors, than the established route of increasing exposure to renewable energy. Interestingly, given the flurry of sovereign wealth fund investment activity in the agritech sector in the last two years, they now appear to view this sector as slightly less attractive than they did in 2020, which may be a function of increasing competition in this space and higher valuations as other investors look to gain access to these businesses.

Chart 2.5 Sovereign wealth fund investments in climate-change related sectors 2015-2021 (US\$ billions)



Source: IFSWF Database, as of 30 September 2021

As sovereign wealth funds develop greater knowledge and more understanding of climate-change-related investments, they are engaging more with the issue. Only 14% of sovereign wealth funds currently divest from companies on environmental grounds (the same proportion as last year), but we have seen a small rise in the proportion that engage with its portfolio companies on climate-related issues from 54% to 58%, the share of which has come from the funds that previously did neither. Although this is a small increase, it indicates that more sovereign wealth funds have connected with the issue of climate change. As large and often influential investors, effective and coordinated engagement by sovereign wealth funds with their peers has the potential to have a real influence on their portfolio companies' adoption of lower-carbon, climate-friendly strategies and thus a material impact on tackling climate change and its consequences.

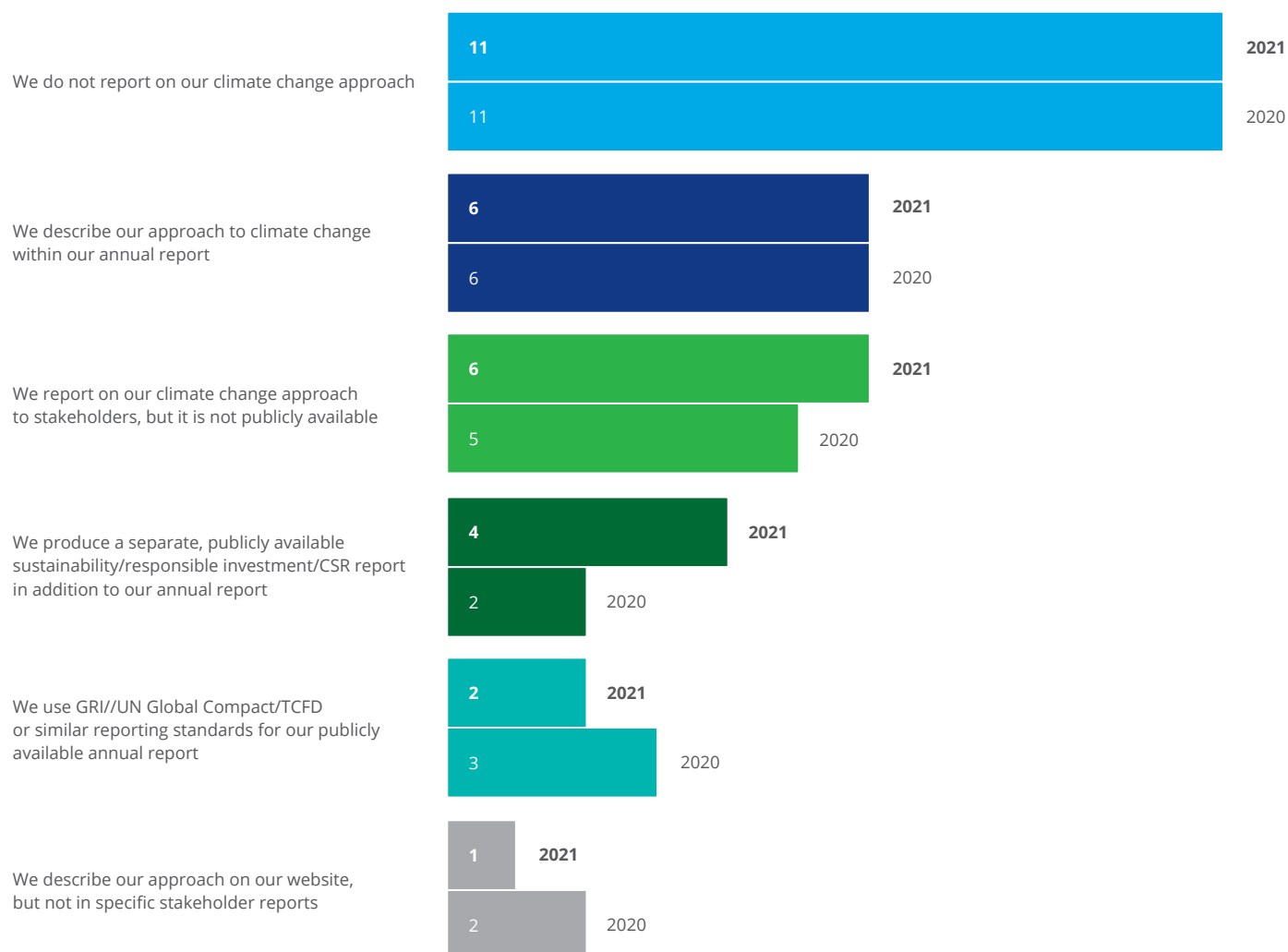


Improving measurement and reporting

As more sovereign wealth funds are now implementing an approach to climate change, more respondents (58% in 2021, up from 38% in 2020) report that they struggle to find reliable data on which to base their strategies. This is a fundamental barrier to them measuring, managing and mitigating their portfolios' climate impact. For example, sovereign wealth funds appear to struggle with defining key performance indicators and metrics on which to assess their strategy. This may partly be a result of there being a plethora of data providers and frameworks for sovereign wealth funds to navigate, but also because asset managers and banks all have different approaches and methodologies to measuring climate impact which makes it hard for sovereign wealth funds to integrate the data into a consolidated and consistent dashboard or data set. Consequently, over half of the respondents do not use metrics to assess their climate impact. Equally, there are many competing standards and frameworks on which to assess climate impact, and as relatively new adopters of ESG, the most popular method of enhancing our survey respondents' climate change approach is to improve their understanding of these tools as shown in Chart 2.2.

Potentially as a result of this lack of certainty about appropriate hard metrics, most sovereign wealth funds are yet to fully report on their climate approach: 83% of respondents that use a climate change or ESG approach don't publish their climate change strategy. Although there has been an improvement in reporting – 35% of respondents still do not report anywhere on how they are tackling climate change, down from two-thirds last year – most sovereign wealth funds are not yet disclosing much information on this topic. Twenty per cent of respondents (up from 17% last year) only report on climate change directly to their stakeholders, a further fifth describes their climate change approach in their annual reports, but less than 20% of respondents have a separate climate change report or use one of the accepted sustainability reporting standards for their publicly available annual report.



Chart 2.6 How do you report on your climate change strategy? (comparison between 2020 and 2021)

Source: IFSWF-OPSWF Climate Change Survey 2021

While the lack of public disclosure on climate change appears to be a symptom of a deeper issue – uncertainty around climate data and developing appropriate metrics – it may also reflect that, as often conservative institutions, sovereign wealth funds are concerned about ensuring their public metrics are aligned with accepted, established standards. However, as sovereign wealth funds find appropriate standards and metrics, and with the efforts of organisations like OPSWF, we anticipate increased public visibility on the measures sovereign wealth funds are taking in this regard.

Indeed, in our 2021 survey, sovereign wealth funds appear to be partnering with peers and international initiatives to increase their influence on the climate agenda and help solve some of these challenges. In 2020, 59% of respondents were not members of any climate-related initiatives, while 10 reported being OPSWF members or observers. In 2021, 15 of our survey respondents were OPSWF members and four were PRI signatories, while CDP (formerly the Carbon Disclosure Project) and Climate Action 100+ both had two signatories in our respondent base. The number of respondents that were not engaged in any grouping had halved over the year. However, 41% of respondents are still not members of any climate-related initiatives, so there is still progress to be made, but the increasing engagement of sovereign wealth funds in the global climate debate is clear.

What Next?

Last year, in *Mighty Oaks from Little Acorns Grow*, IFSWF and OPSWF put forward six recommendations for sovereign wealth funds to enhance their climate-change response:

- 1. Adopt and implement climate-related policies.**
- 2. Seek out the appropriate talent and expertise.**
- 3. Explore board member and executive education.**
- 4. Use metrics** to show not only climate impact (i.e. success in reducing carbon exposure) but also comparable returns and risk reduction.
- 5. Communicate to all stakeholders** the strategic importance of climate.
- 6. Partner with peers and international initiatives** to share experience and generate greater leadership from within the sovereign wealth fund community.

A year later, this evaluation of our survey responses has shown that sovereign wealth funds have made material progress in recommendations **one, two, three, five and six.**

- 1.** We have seen rapid adoption of climate-related policies over the past year and many more sovereign wealth funds are applying a more strategic and systematic approach to climate change in their portfolios than they did just 12 months ago.
- 2.** In terms of talent and expertise, it is clear from the survey that sovereign wealth funds are investing in upskilling their teams and, where they believe it appropriate, to hire specialist personnel. However, a larger number of sovereign wealth funds report struggling to find and attract talent and expertise.
- 3.** The rapid adoption of ESG strategies in 2021 and a decline in stakeholder disinterest in the issue of climate change, demonstrates that sovereign wealth funds' boards and executives now understand the need to consider these risks and opportunities in their investment approach.
- 5.** It is clear from this year's survey that sovereign wealth funds' stakeholders are increasingly supportive of adopting climate change and broader ESG strategies. While the survey does not explore the reasons for this shift, the role of sovereign wealth funds in engaging their stakeholders to overcome this barrier cannot be discounted.
- 6.** In 2021, more sovereign wealth funds have joined international initiatives to engage in the climate debate, learn from their peers and show leadership. While there is still some way to go, it is clear from this year's survey that sovereign wealth funds appear to understand the benefits of joining such groupings not only to enhance their organisations' reputation but also to help enhance their climate impact.

However, sovereign wealth funds do need to make more progress on recommendation four: developing and using metrics and targets for their climate exposure and reducing their carbon footprint. While, for observers, sovereign wealth funds' disclosure on climate strategies is important as a measure of progress, for them, defining their carbon reduction targets and their exposure to climate-change-related investment sectors is essential. The development of these metrics will depend on sovereign wealth funds' ongoing efforts to develop bespoke methodologies, deepen expertise and engage with their stakeholders to ensure they are comfortable with public targets and metrics that might not be achieved due to circumstances outside of their control.

That said, the challenging nature of identifying appropriate data and metrics, developing and implementing methodologies to measure and manage climate exposure and understanding the plethora of different reporting standards and frameworks, should not be underestimated, particularly for the large sovereign wealth funds with complex portfolios. However, the survey does reveal that sovereign wealth funds are not only working on this internally but also engaging with international climate change associations and their peers to engage and make an impact on reducing carbon emissions globally. As long-term pools of capital, investing for the benefit of future generations, or the sustainable development of their own economies, this is an appropriate and potentially influential development.



Acknowledgements

The International Forum of Sovereign Wealth Funds and One Planet Sovereign Wealth Funds would like to thank their members for their participation in this survey and additional interviews. Without their support we would not be able to bring this comprehensive few of their approaches to light.

IFSWF and OPSWF would also like to thank Dr Victoria Barbary, Director of Strategy and Communications at the IFSWF for designing the survey and preparing the text. They would also like to thank Enrico Soddu, Head of Data and Analytics at the IFSWF for all the analysis and data visualisation in this report.

The authors would like to thank Duncan Bonfield, IFSWF Chief Executive, and Lawrence Yanovitch, OPSWF coordinator, for their support in making this project possible.



About the International Forum of Sovereign Wealth Funds (IFSWF)

The International Forum of Sovereign Wealth Funds (IFSWF) is a voluntary organisation of global sovereign wealth funds committed to working together and strengthening the community through dialogue, research and self-assessment.

In 2008, a group of 23 leading state-owned international investors from around the world established the IFSWF's precursor, the International Working Group of Sovereign Wealth Funds, following discussions with global groups such as the G20, International Monetary Fund and the US Department of the Treasury. The Working Group created a set of Generally Accepted Principles and Practices, known as the [Santiago Principles](#), for sovereign wealth funds' institutional governance and risk-management frameworks. Following the [Kuwait Declaration](#) in 2009, the International Working Group became the IFSWF with the mandate of helping members implement the Principles.

Today, helping members implement the [Santiago Principles](#) remains the foundation of the IFSWF's activity. But the Forum now represents a group of almost 40 sovereign wealth funds from all corners of the globe, with a variety of mandates and at various stages in their development. As a result, the Forum's focus has evolved. In addition to encouraging the ongoing commitment to the Santiago Principles, the Forum also undertakes research, facilitates peer assistance exercises and holds workshops and seminars to help members enhance their existing investment capabilities. The IFSWF also undertakes to represent its members to the global financial and policy communities.

Standard Setting

The IFSWF helps foster good governance practices within the membership by enabling members to share their unique experiences of applying the Santiago Principles with each other. By sharing experiences, the Forum helps members to improve their governance and accountability structures and practices. The IFSWF also promotes transparency by encouraging members to report publicly on their experiences of implementing the Santiago Principles.

Knowledge Sharing

The IFSWF seeks to help members raise their expected risk-adjusted returns by regularly bringing our members together to share their perspectives on specific governance, investment and operational issues. We also undertake peer assistance on investment practices, asset allocation and financial risk assessment. The Forum works with academic and practitioner experts to help members fulfil their mandate in an increasingly challenging and complex investment environment.

Representation

The Forum helps represent the views of its members to the wider financial community. It provides a contact point through which members can collaborate with multilateral finance organisations and, where appropriate, engages with the media on issues of interest to the membership.

About One Planet Sovereign Wealth Funds

[One Planet Sovereign Wealth Funds](#) was established at the One Planet Summit in December 2017. The objectives of the initiative are to:

- Help mobilise the capital of sovereign wealth funds, to innovate and expand the market for investment opportunities that advance alignment with the goals of the Paris Agreement.
- Accelerate efforts to integrate financial risks and opportunities related to climate change in the management of large, long-term asset pools.
- Leverage the scale and benefits of knowledge-sharing, while preserving flexibility and agility.

On 6 July 2018, the OPSWF founding members published a voluntary framework ("[the Framework](#)") outlining principles for sovereign wealth funds to systematically integrate climate change into their decision-making, and how they can collectively support ambitious global climate action.

This Framework includes 12 recommendations based on three guiding principles:

- **Principle 1: Alignment**
 - Build climate change considerations, which are aligned with the sovereign wealth funds' investment horizons, into decision-making.
- **Principle 2: Ownership**
 - Encourage companies to address material climate change issues in their governance, business strategy and planning, risk management and public reporting to promote value creation.
- **Principle 3: Integration**
 - Integrate the consideration of climate-change-related risks and opportunities into investment management to improve the resilience of long-term investment portfolios.

Following the drafting of the Framework, members committed to continuing to work together to develop and share best practices relating to the implementation of the Framework principles. The One Planet Asset Managers (OPAM), the One Planet Private Equity Funds (OPPEF) initiatives and the One Planet Research Forum have also been established to accelerate efforts in supporting the implementation of the Framework and to support the transition towards more sustainable financial markets.

From 6 founding sovereign wealth funds, the Network has since grown to 43 members, comprising 18 sovereign wealth funds, 17 asset managers, and eight private investment firms, with over \$36 trillion in assets under management and ownership. For more information, visit oneplanetswfs.org

