What Copenhagen Means for Investors

Abyd Karmali
Managing Director and Global Head of Carbon Markets at Bank of America Merrill Lynch and President of the Carbon Markets & Investors Association

Prior to the UN climate change negotiations in Copenhagen, consensus estimates were that the private sector would need to provide more than 85% of the roughly $200 billion annual investment required to help meet global carbon emission reduction needs by 2020. Post-Copenhagen, has anything changed and what were the key implications for investors? I have always argued that the litmus test for Copenhagen was whether the resulting political accords or agreements succeed in mobilizing flows of private capital. After all, the core *financial* challenge for climate change is one of capital reallocation and timing, or, put another way, how to steer capital away from high-carbon investments and channel it quickly and with scale towards lower-carbon technology. So what are the main conclusions to be drawn from Copenhagen?

On the positive side of the ledger, Copenhagen affirmed the direction of travel. Investors received confirmation that we are heading, albeit at a pace yet to be agreed upon, towards a low-carbon trajectory. The largest-ever gathering of heads of state outside the UN annual assembly in New York did at least succeed in producing a coalition of the willing—most crucially, representing the 17 countries responsible for more than 80% of global greenhouse gas emissions. These leaders have now committed their nations to implementing new measures that should accelerate the uptake of low-carbon energy, products, and processes.

Those who viewed the outcome from Copenhagen in a strongly negative light have, however, been quick to highlight that the summit failed to provide any deadlines for, or guarantees about, the enactment of each country's suite of low-carbon policies and measures. Moreover, no clear roadmap to a legally binding international treaty emerged. This provides some uncertainty for investors in cleaner energy, unless, of course, such investors are using conservative assumptions and attributing zero value to the environmental externalities (such as carbon emissions) their investments are helping to address. Without clear policy frameworks setting out targets and timetables that allow a sustained price signal for carbon to emerge, there is a risk that capital will not flow towards low-carbon technology. Unfortunately, one scenario that investors must now contemplate is that the climate negotiations might emulate the endless loop of the World Trade Organization talks.

There are several metrics that investors should use to monitor investment trends post-Copenhagen. First, will 2010 bring an increase in the total investment flowing towards cleaner energy? In 2009, we saw the first year-on-year decline in the past decade. It will be important for this to tick back up again. The overhanging government stimulus funds will likely play a materially positive role here. Second, will 2010 bring an increase in funds raised specifically for carbon emission reduction projects in developing countries? As one proxy for this, 2009 saw a year-on-year decline in the issuance rates in the volumes of carbon credits registered by the Clean Development Mechanism. Third, will there be an increase in assets-under-management of funds characterized as low-carbon? It is conceivable that climate change is already a mega-trend for investment and continuing momentum in the allocation towards green products from institutional investors would provide more support for the theory that the direction of travel has already been internalized by investors.

What is crucially important for all investors to keep in mind is that one material macro-risk remains unchanged following Copenhagen. If credible pricing for carbon remains absent, some investors will continue to deploy capital in the high-carbon economy. The overarching and systemic risk for all investors could then be a scenario where a future financial crisis is caused by the premature and forced retirement of highly carbon-intensive assets.

Biography

Abyd Karmali is managing director and Global Head of Carbon Markets at Bank of America Merrill Lynch. He is the company's point person for carbon business opportunities and serves on Bank of America's Environmental Council. Karmali has provided strategic advice on the commercial risks and opportunities posed by carbon emissions constraints to scores of European, US, and Asian companies. In 2008, his team won *Environmental Finance* magazine's Carbon Finance Transaction of the Year and *The Banker* Award for Most Innovative in Sustainability.

Karmali has worked for two decades on climate change and the carbon markets and is serving as elected President of the Carbon Markets and Investors Association from 2008 to 2010. Additional appointments include: member of Her Majesty's Treasury Carbon Market Expert Group, member of the World Economic Forum (Davos) Steering Committee for Advancing Low-Carbon Finance, advisor to the Carbon Disclosure Project, and advisor to the Commission to establish Britain's first Green Investment Bank. Karmali was previously employed with ICF International in Washington DC, Toronto, and London. In 1996-97 he was Climate Change Officer at the United Nations Environment Programme's Industry office in Paris and participated in the Kyoto Protocol negotiations.

He is frequently called upon by the media and has been interviewed for TV/radio by BBC, CNN, NPR and CNBC as well as cited in print media such as the *Financial Times*, *The New York Times*, *The Australian*, *Financial Post* and *The Economist*. Karmali has also provided expert testimony on emissions trading and on forestry carbon – reduced emissions from deforestation and degradation (REDD) – to parliamentary hearings held by the British House of Commons' Environmental Audit Committee.

Karmali's voluntary sector activity includes serving as Chairman of Just Energy, a not-for-profit social enterprise recently set up by Oxfam, which works with low-income communities in developing countries to maximize revenues from medium-sized renewable energy businesses and to increase the supply of clean energy. He has also undertaken volunteer work with the agencies of the Aga Khan Development Network and a three-year stint on the Board of Trustees of Focus Humanitarian Assistance Europe Foundation. He holds an M.S. in Technology and Policy from the Massachusetts Institute of Technology.