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## INVESTMENT OPPORTUNITIES IN THE CLIMATE CHANGE ECONOMY

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In a market embattled by low confidence, widespread employment loss and possible lingering deflation, investors are beginning to see that a new economic philosophy will be necessary to regain stability and eventually achieve positive momentum. And as many of the popular yet high risk investments of the past decade (i.e., financial services, emerging markets and real estate) teeter on the edge of insolvency, opportunities prompted by initiatives to contain global climate change are showing signs of strength.

The evidence of climate change impact and the need to rethink energy deployment is indisputable. Polar bears are officially a threatened species, dramatic weather events are leaving their mark around the world, and the U.S. has been pinned down by three foreign oil crises in 40 years.

These growing issues combined with the difficult market of 2009 could serve as a catalyst to pass comprehensive climate legislation designed to boost near-term investments in clean energy and thereby help ensure economic recovery. As the Obama administration moves toward stimulus that will include energy efficiency incentives, renewables funding and subsequent climate legislation, the current generation of investors will see a window of opportunity to capitalize and support the urgent call for change.

### *Capturing the economic opportunity*

In the face of the credit crisis and economic headwinds, investment in all energy infrastructure will slow until the market's tolerance for moderate risk improves. But once the immediate credit crisis eases, those who have already been exposed to the perils of fast and easy money will have the opportunity to get back to fundamentals and invest for the long term. Legislation will open doors to make environmentally-oriented business sustainable, and the durability of these enterprises will present stable growth opportunities.

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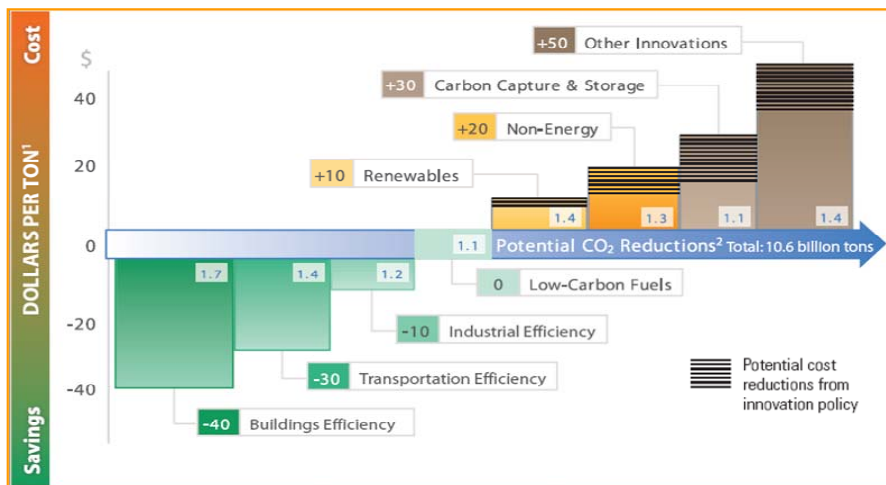
To understand the potential upside, it is important to first see the consequences of failing to address climate change. As noted in a recent Foreign Affairs report, “The economic costs of unchecked global warming will be severe...In 2007, the IPCC estimated that global warming could lead to continuing global GDP losses of one to five percent and even greater losses at the regional and local levels.”<sup>i</sup>

On a macro level, then, growth in climate-oriented sectors is critical. And on a micro level, investors that are proactive and intelligently diversify their portfolios within the right industries will benefit from extensive momentum. By unearthing companies that maintain strong corporate fundamentals and are built to thrive on a green playing field that will include a price on carbon emissions, investors can collect positive long term returns while funding progressive ventures that will shape the new economy.

There is a spectrum of eight industries that focus on decreasing carbon emissions. Efforts in areas that promote buildings efficiency, transportation efficiency, and industrial efficiency are often top of mind, but all eight (see graphic) will be contributing factors.

### NRDC Cap 2.0 - Smart climate legislation solves three problems at once

NRDC strategy to cut U.S. global warming pollution 80% by 2050 at no net cost to the economy



- 2 Invest CO<sub>2</sub> allowance funds and adopt other policies to overcome non-price market barriers to **energy efficiency**
- 1 Define federal **cap and trade legislation** that drives investment in all clean technologies by pricing pollution
- 3 Invest CO<sub>2</sub> allowance funds to overcome innovation spillovers and encourage **clean technology innovation**

<sup>1</sup> Dollars per ton of cuts in emissions of CO<sub>2</sub>e (CO<sub>2</sub> plus other greenhouse gases)  
<sup>2</sup> Billions of tons CO<sub>2</sub>e per year, in 2050  
 Source NRDC analysis, including extrapolations from the 2030 cost estimates by McKinsey & Company

The EU has already launched a cap and trade system to drive down its emissions; the U.S. is likely to pass its own major legislation designed to motivate qualifying companies in these sectors in 2009. The immediate impact will be long-term clarity for energy sector investors plus aggressive federal incentives for efficiency and renewables starting in 2010. That will likely be followed by the implementation of a full cap and trade system to control carbon emissions as early as 2012.<sup>ii</sup> Such a sustained and fiscally responsible stimulus can be a major

piece of economic recovery, fighting off current fears from Paul Krugman and others that we face the real risk of a Japan-style lost decade.

Once this combination of incentives and penalties are enforced, low carbon players will gain a 10 to 50 percent cost advantage, with complex interactions across all eight solution sectors opening up clear growth opportunities for prescient investors. Consider that the interest in renewable energy has spiked since the turn of the century and should ratchet up significantly with relevant legislation. According to a report by the Natural Resources Defense Council (NRDC), “Global investment in new renewable energy installations totaled \$100 billion in 2007, up from \$15 billion in 2000 [and] renewable energy resources are spread across the United States.”<sup>iii</sup>

Building development has also been a forward-thinking industry. Gold standards in LEED (Leadership in Energy and Environmental Design) Certifications are viewed as almost quaint by now. Indeed, in many cases design and construction projects have become races to see who can create the “greenest” building possible.

Across the economy, forward thinking entrepreneurs and industrialists recognize the opportunity for current improvement for their future’s sake, and the path to progress is to embrace climate change containment as a catalyst for economic transformation.

### *The movement underway*

Energy sector transformations are not unprecedented, although the scope of investment required in the coming decade will far exceed previous initiatives. Looking to Europe, the move to alternative energy began in the late 1970s and brought about profound change. France, for instance, uses 20 percent less oil today than it did in 1979.

The crucial missing piece in the U.S. has been follow-through. Particularly in light of recent fossil fuel price volatility, emerging energy technology leaders will demand federal leadership to establish a clear playing field that inspires sustained change.

In the meantime, states and municipalities are taking the charge up on their own. 17 states representing 45 percent of the U.S. population have committed to greenhouse gas emission reduction targets, and more than 700 cities have pledged to cut emissions and called for federal legislation to do the same.<sup>iv</sup>

From a city by city perspective, that translates into 700 interpretations of current needs and 700 different levels of commitment. There are standouts, however, that are setting the pace. In New York City, PlaNYC was launched in 2007 to gather information and pursue aggressive goals for the reduction of greenhouse gases. While there are a number of distinct initiatives, PlaNYC’s website details an aggressive energy strategy: “New York City’s government spends nearly \$800 million a year on electricity, natural gas, and heating oil and consumes roughly 6.5% of the city’s energy...We will propose an amendment to the City Charter requiring that New York City invest, each year, an amount equal to 10% of its energy expenses in energy-saving measures...the City will achieve a 30 percent reduction in

municipal greenhouse gas emissions by 2017. While it will cost \$2.3 million, the City will begin to break even in fiscal year 2013 due to energy cost savings.”<sup>v</sup>

Across the country, California also provides a leading example, as the state seeks to locally reinvest a portion of the \$30 billion it spends annually on imported fossil fuel. Redirecting those funds to clean technology development could bring billions of dollars and more than 80,000 jobs to the state.

There are other, broader consortiums dedicated to similar goals, including the Regional Greenhouse Gas Initiative, the Western Climate Initiative, and the Midwestern Regional Greenhouse Gas Reduction Accord. They all seek solutions that yield economic benefits for environmental commitments – perhaps establishing a mantra for investors adapting to the new paradigm.

### ***Urgent beginnings, patient rewards***

Thinking broadly, the U.S. is witnessing an overlap of the credit-based cornerstone of the current economy with a rising emphasis on energy-focused investments. Near-term action on climate legislation will help to ensure economic recovery and launch entirely new clean energy industries; it will unlock new projects, provide federally incentivized funding streams, and go a long way towards resolving fundamental investor uncertainty.

Such an environment will serve as a vast improvement over the highly leveraged financial engineering that sparked the downturn, and going forward there will be a greater emphasis on investing for the long haul. At a philosophical level, this provides an opportunity for investors to reset their expectations for rate of return, as the source of value will be found in less risk and more realistic gains.

Investors seek to stabilize their portfolios while the business world evolves to a new set of climate-sensitive standards. The symbiotic nature of those tasks is self evident; as legislation is formed, debated, and eventually passed, intelligent investors will recognize the appeal of sustainable investments that are built to thrive in the future.

## *About the Authors*

**Charlton Reynders, III**, is Chairman and Chief Executive Officer of Reynders, McVeigh Capital Management, a rapidly growing investment management firm with a strong emphasis on building portfolios around ethically managed, sustainable investments. Chat has compiled more than fifteen years of experience in investment management and social venture investing. He has structured and funded public/private partnerships that have brought more than \$150 million in revenues to leading cultural institutions around the world, projects that have won numerous awards. The IMAX film, *Dolphins*, produced in conjunction with the National Wildlife Federation, garnered an Academy Award nomination in 2000; another IMAX film, *Coral Reef Adventure*, received the largest grant in the history of the Informal Science Division of the National Science Foundation.

**Rick Duke** is the director of NRDC's Center for Market Innovation. Rick works with government and corporate leaders to accelerate market adoption of clean technologies and practices. Prior to joining NRDC, Rick was an engagement manager at McKinsey, where his projects included developing a hedging strategy for a leading CO2 credits originator and managing a global assessment of greenhouse gas reduction opportunities, published by McKinsey and the European Union utility Vattenfall. Rick has also worked for the Federal Reserve Bank of New York, managed a small renewable energy company in Honduras and consulted for the International Finance Corporation. He holds a Ph.D. from Princeton University, where his doctoral work focused on the economics of public investment in clean energy.

## *Endnotes*

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<sup>i</sup> *Containing Climate Change: An Opportunity for U.S. Leadership*, Carter F. Bales and Richard D. Duke, Foreign Affairs, Sept/October 2008

<sup>ii</sup> <http://www.nrdc.org/globalWarming/cap2.0/files/invest.pdf>

<sup>iii</sup> *The New Energy Economy: Putting America on the Path to Solving Global Warming*, Rick Duke, Dan Lashof, NRDC Issue Paper June 2008

<sup>iv</sup> Ibid

<sup>v</sup> [http://www.nyc.gov/html/planyc2030/html/plan/energy\\_reduce-consumption.shtml](http://www.nyc.gov/html/planyc2030/html/plan/energy_reduce-consumption.shtml)