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LA FRANÇAISE FIXED INCOME insights

CLIMATE CHANGE AND ITS EFFECTS ON THE BOND MARKET

Climate change is a reality that affects us all. We are both the victims and the perpetrators of this environmental phenomenon. As a committed investor with strong convictions, we seek to actively participate in the energy and ecology transition essential to the preservation of our planet as we know it. We aim to direct assets under management towards opportunities presented by this transformation, while protecting them from related risks.

- **In 2015, the average temperature on Earth had increased by around + 1 °C from the 20th century average [1].**
- **The frequency of extreme climate events has multiplied by more than 7 since 1960[2].**
- **This resulted in more than 1.7 million deaths and 4.4 billion injuries from 1998-2017.**
- **Over the same period, the economic impact amounted to $2,900 billion, 251% higher than in the previous 20 years[3].**

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(1) GIEC AR5 report, 2014
(2) EM DAT database
(3) https://www.unisdr.org/2016/iddr/IDDR2018_Economic%20Losses.pdf

Maximum increase in the global temperature by 2100, set by the Paris Accords in 2015.

+2°C

The bond risk premium does not currently integrate climate risk. This risk is explained differently for each industry. For the oil industry, for example, “stranded assets” represent a major risk. A Carbon Tracker study that analyses the CAPEX of 72 oil exploration and production companies shows that in a world aligned with the demand for a +1.75°C scenario, $1.6 trillion in assets[(4)] could be economised. This would cancel out their value in the balance sheets of the companies that hold them.

Faced with the necessity to accelerate the financing of the transition, we have seen the green bond market emerge. This market has grown exponentially over the past four years following the adoption of the concept by industrial and financial issuers. These bonds are issued in relation with projects to invest in renewable energy, high-quality environmental real estate and the financing of “green” projects by banks.

However, not all industry sectors have issued bonds on this market. When an industry's main activity is structurally a high consumer of fossil fuels, access to this market is more difficult. Nevertheless, we should not exclude these sectors from the transition, as they form the cornerstone of a profound revolution in energy and the economy. They are actors in the transition and we seek to identify the companies that are investing in their transformation to finance them via the bond market.

This graphic illustrates the carbon emissions emitted by a company for a single production unit. As you can see, successive investments in new, cleaner technologies and production assets will help to lower their consumption and improve their energy efficiency.

Thanks to climatologists, we know that we have a carbon emissions budget that cannot be surpassed if we want to limit the temperature increase to 2 degrees by the end of the century. We can therefore use companies' detailed analyses to evaluate how their strategy and their investments might impact their trajectories.

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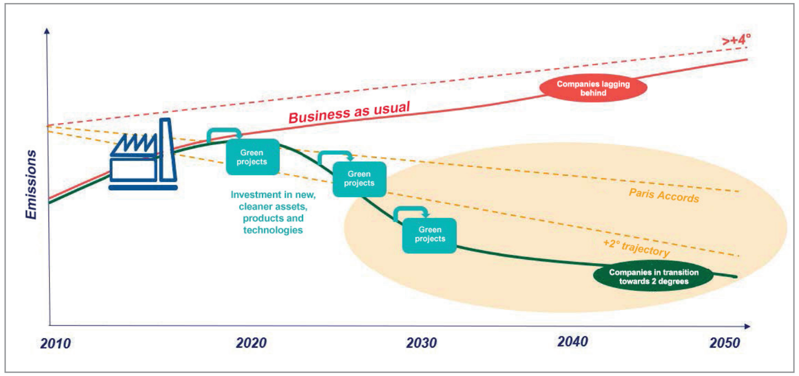
(4) Carbon tracker, “2 Degrees of Separation: Company-level transition risk”, July 2018 Update

TRAJECTORY OF COMPANIES IN THE ENERGY TRANSITION



CONCLUSION

We are addressing the need to take action at the heart of our management, as we firmly believe that each actor in our economy has a role to play in the transition. This means going beyond surface statements to make a broad commitment on the climate change front: with our clients, with the companies that we finance and with our peers.

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