TOWARDS TRANSITION INTELLIGENCE: NAVIGATING A MULTI-SPEED TRANSITION THROUGH INVESTOR TRANSITION PLANNING

A forward-looking approach to transition planning can give institutional investors a strategic edge in navigating the uneven economic transition to net zero. Making the distinction between transition plans—a formal output—and transition planning—an ongoing process—there are five ways through which professionals in sustainability, risk and investment teams can deepen their organisation's transition intelligence and enhance their transition planning.

A GLOBAL ECONOMIC TRANSITION TO NET ZERO IS UNDERWAY

Global capital reallocation is transforming the energy system. In 2024, investment in the energy transition hit US$ 2.1tn, up 11% from the previous year, double the investments in oil, gas and coal at US$1.1trn. Wind and solar are the fastest growing electricity sources in recent history, outpacing growth in conventional fossil fuels.

Government policy in the real economy is a critical driver of market confidence. The transition is playing out at multiple speeds across countries and sectors. Globally, climate policy activity remains high. In some major jurisdictions, policy delays or reversals could slow decarbonisation, but so far, there has been limited spillover effect across markets.

TRANSITION PLANNING IS A STRATEGIC TOOL FOR NAVIGATING UNCERTAINTY

Transition planning can serve as a tool for responding to, participating in, and contributing to the transition to a net zero economy. There has been continued momentum in the uptake of transition planning in major markets and sectors over recent years. While disclosures of transition plans have grown across sectors, a strategic approach to investor transition planning is still emerging.

For investors, transition planning has highest potential as a strategic tool, not only as a compliance exercise.

This means integrating transition considerations in wider strategic processes, wherein investors and investees assess the drivers of risk and opportunity in a changing global economy and determine approaches for maximising value across a range of time horizons.

Defining Transition Planning

Transition Planning:
A dynamic, iterative process through which an entity develops an organisation-wide approach to the broader economic transition to net-zero.

Transition Plans:
The formal output – often a public disclosure – which details how the entity plans to achieve its stated goals.

PRINCIPLES FOR RESPONSIBLE INVESTMENT

TOWARDS TRANSITION INTELLIGENCE: 5 KEY CONSIDERATIONS FOR A STRATEGIC APPROACH

1. DEVELOP A HIGH-CONVICTION VIEW OF HOW THE TRANSITION MAY UNFOLD

A high conviction view on how the transition may unfold in the real economy allows investors to allocate capital with confidence amidst change and complexity. This view can be informed by forecasts of key trends such as sectoral supply and demand shifts, as well as anticipated changes in sector policy direction and implementation.

Recent evidence reveals that having a well-defined base case is good practice that can lead to improved risk management, capital allocation and long-term investment performance.

2. INTEGRATE SCENARIO ANALYSIS INTO INVESTMENT DECISION-MAKING

Long-term investors can benefit from integrating climate scenario analysis into the investment process to build agile, informed strategies to better navigate the uncertainty of the transition.
Following several years of experience in doing, or using, climate scenario analysis, a growing number of investors are working to more fully integrate insights from scenario analysis in their investment processes.

3. CONSIDER IMPLEMENTATION STRATEGIES THAT SUPPORT EMISSIONS REDUCTIONS IN THE REAL ECONOMY

System-level climate risks are managed where the real economy is decarbonised. Investors can benefit from tracking where decarbonisation is happening, to shape competitiveness and long-term value.

Stewardship tools can be central in supporting real economy decarbonisation. In designing implementation strategies, it is useful to consider companies' capital expenditure (CapEx), operational expenditure (OpEx) and research and design (R&D) budgets, in addition to forward-looking targets and plans.

4. FOCUS ON VALUE CREATION AND OPPORTUNITIES IN THE TRANSITION

Transition planning does more than mitigate transition risk—it is a lens that identifies where economic value is shifting. Transition planning can support investors in capturing new growth opportunities, including through climate solutions, transition and adaptation finance, and opportunities in emerging markets and developing economies (EMDEs). These opportunities span a range of asset classes and a growing universe of transition-critical technologies and adaptation solutions.

5. ENGAGE WITH POLICY MAKERS ON DELIVERING NDCs AND A WHOLE OF ECONOMY TRANSITION

Investors can support an orderly transition to net zero by engaging with policy makers to deliver ambitious policy frameworks. National transition plans should provide information about whether governments are prepared for – and enabling – the transition to net zero. Investors can use national transition plans to identify where engagement can support ambition and implementation. Engagement between policy makers and investors is key for both in financial and real economy reforms.

Policy that accelerates the transition is vital to close implementation gaps, stabilise global temperatures, and avoid potentially catastrophic levels of climate disruption.