Debunking Six Myths About Climate Investing

By painting climate change with a broad brush, institutional investors are overlooking opportunities to potentially generate compelling market returns and make a meaningful impact on the most pressing issue facing our planet today.

Investors have come to terms with the reality that climate change is no longer a theoretical threat. The effects of extreme weather, rising sea levels, resource scarcity and pollution are rippling across every continent with dire consequences for individuals, governments and businesses.

Yet, for many investors, climate investing is still an abstract concept that is often lumped in with discussions of risk management, consumer preferences, the conflation of Environmental, Social and Governance (ESG) with impact investing. In fact, the implications of climate change are nuanced—and so are the potential solutions. By looking at the issue of climate change through a broader lens, we believe investors can be better positioned to identify opportunities that meaningfully address a range of climate issues and potentially deliver compelling risk-adjusted returns.

Here are six of the most common myths percolating around climate investing.

**Myth #1**
The climate problem is all about global warming.

**REALITY:** Problems are manifold.

For many people, the term “global warming” evokes images of melting icebergs in the Arctic Circle. This is indeed a major
and daunting consequence of climate change. Still, there are many aspects of the climate issue that are more tangible and potentially more manageable. They include, but are not limited to:

- **POLLUTION:** From visible air quality issues in smog-choked Beijing and Delhi to leafy London where nitrogen oxide levels routinely exceed safe norms—pollution is present in our daily lives.
- **RESOURCE SCARCITY:** Drought is a growing problem that affects communities and farmers around the world. Last year, Cape Town nearly ran out of water and introduced the concept of Day Zero which effectively triggered the start of drastic water rationing. California also is dealing with the acute effects of drought and, now, flooding. Lakes in many parts of Africa are shrinking, thus leading to social strife, conflict, migration and refugee crises.
- **WASTE MANAGEMENT:** Many of our cities are running out of landfill and other solutions to dispose waste. Plastics are making their way into the oceans, marine life and our food chain at alarming levels. At the current pace there could be more plastic than fish in the oceans by 2050.¹
- **ECO-DIVERSITY:** Sections of pristine rainforest in Indonesia are routinely razed for agriculture and timber. This is also true in Brazil where the Amazonian rain forests produce 20% of our planet’s oxygen. In 2016 alone, 30% of the coral in the Great Barrier Reef was destroyed.²

**Myth #2**

An ESG strategy addresses climate solutions.

**REALITY:** ESG is necessary, but not a sufficient condition, for addressing climate change.

ESG, or the incorporation of environmental, social and governance risk factors, is an increasingly core part of any investment strategy. It seeks to limit the operational, financial or reputational risk that could arise from something going wrong in one of these dimensions.

We believe that creating positive climate impact, however, requires more than ESG hygiene. It requires actively investing in businesses, typically putting primary capital to work in a private equity context, whose core activities create new positive effects on the environment, be it a reduction in CO2 emission, pollution or resource consumption.

**Myth #3**

Renewable energy is the main solution.

**REALITY:** The investable opportunity set goes far beyond power generation.

Renewables have historically been a cornerstone of climate change investing—but there is a world of opportunity besides windmills and solar panels. A comprehensive climate strategy will look beyond power generation to energy efficiency, housing, transportation, food and recycling.

Here again, some of the most distinctive investment ideas, both from the perspective of returns and impact, focus on solving specific problems, improving existing technology or making broader adoption more feasible.

Minimizing the carbon impact of transportation, for instance, isn’t just about funding electric cars and makers of lithium-ion batteries. There are myriad companies in this space that are contributing to more eco-friendly transportation in seemingly small but immensely impactful ways.

One example is a battery-exchange kiosk company in Asia, which makes electric two-wheelers a more viable alternative with a creative answer to charging. Rather than plugging in their vehicles and waiting for them to charge, drivers use the kiosks to swap batteries. The kiosks are technology-agnostic; as new batteries come onto the market, the company simply adds them to its catalog.

Similarly, green chemistry is a category that doesn’t get the same attention as alternative energy but offers ample room for reducing the use of fossil fuel derivatives in items of everyday consumption, from packaging materials to paints and furniture polish. The same is true of new business models around recycling, compostable packaging materials, waste-to-energy generation and waste water processing.

There is also a plethora of investment ideas related to food. Demand for meat protein is growing along with the world’s population and income levels. Yet, livestock is a major source of emission of the greenhouse gas methane—which is approximately 30 times worse than CO2.³ As such, sustainable seafood, which has a much smaller carbon footprint, presents a blue ocean of opportunity.

**Myth #4**

Renewables need subsidies to offer compelling returns.

**REALITY:** Cost has declined massively since the advent of renewables and pricing is now competitive with traditional energy in many markets.

It was once the case that renewables thrived and died on subsidies, but three major changes make this idea an antiquated one.

---

¹ Source: https://www.morganstanley.com/ideas/peak-plastic, May 2018
³ https://www.sciencedaily.com/releases/2014/03/140327111724.htm
First, costs have come down substantially while technology has improved; it is now feasible to deploy renewable energy in very small spaces or across remote geographies. Blades on windmills now approach aeroplane wings in terms of size and sophistication, while solar panel prices have declined by more than 60% in the last decade. As this technology reaches critical mass, installation and servicing are also becoming more cost effective and convenient.

Secondly, investors can now target specific projects thus making sure the solution aligns with the problem. Markets are not monoliths, and energy prices, along with solar and wind resources, vary within regions. This makes renewables very competitive in some places and less so in others. It also puts the onus on investors to look at the specific context in which renewable projects operate.

Finally, demand for distributed solutions is on the rise, driven by ageing grid infrastructure in developed markets and, in the case of many emerging markets, because of the absence of grids. A company that focuses on making and selling solar-powered home systems in Southern Africa, for example, is opening doors for environmental and social change. In switching out kerosene or diesel for solar power, consumers are saving money, helping improve air quality in their communities and tapping into a more reliable and sustainable source of power.

**Myth #5**

Early stage clean-tech investing is a wild goose chase.

**REALITY:** Savvy investors target low-key solutions rather than moon shots.

Clean-tech investing has been through a few bubble-bust cycles and, like other areas in early-stage investing, there have been some high-profile successes and failures. While a lot of early attention in clean tech investing has been on grand, over-arching solutions, there is a growing and rich universe of companies working behind the scenes to tackle specific causes or effects of climate change.

Indeed, the sector has evolved, as have investors. Instead of looking for a silver bullet for desalination at scale, savvy investors are looking at software that regulates water systems pumps. Rather than banking on the next big thing in electric cars or batteries, smart early-stage investors are backing things like hardware to facilitate data collection and power optimization at charging stations.

These ideas may not make headlines—and that is often a good thing—but they are collectively creating the fabric for meaningful and incremental gains in their respective areas.

**Myth #6**

Climate investing is highly dependent on political and regulatory changes.

**REALITY:** Individuals, businesses and local governments can wield as much power.

Media reports focus a lot of government level pronouncements on climate policy, however the underlying trend of climate investing is a steadfast one that, increasingly, transcends politics. Collectively, individuals, corporations and local governments can wield more power.

Consider the United States. While the federal government has taken a different direction on climate initiatives, individual states and cities are rolling out ambitious plans of their own. In March, New Mexico joined California, Hawaii and the District of Columbia in setting a goal for all renewable and carbon-free electricity by 2045, and governors for a dozen other U.S. states are reportedly planning to unveil similar goals. Meanwhile, some of the world’s largest companies are taking meaningful steps to reduce their environmental footprints. Not to be underestimated, individuals are taking a stand, as citizens and as consumers.

This is all to say that a comprehensive climate strategy encompasses ideas big and small. It looks to address the broader threat of global warming, as well as to support grassroots initiatives to seek to solve problems related to pollution, resource scarcity, waste management and eco-diversity. Innovation does involve technology and business risk. However, a globally-diversified, active approach across asset classes—from early-stage to infrastructure to agriculture—can offer investors a means by which to achieve meaningful returns and make a real impact in addressing the most pressing issue facing our planet today.

---

* Source: https://news.energysage.com/solar-panel-efficiency-cost-over-time/
IMPORTANT INFORMATION
The statements above reflect the opinions and views of AIP Private Markets as of the date hereof and not as of any future date and will not be updated or supplemented. All forecasts are speculative, subject to change at any time and may not come to pass due to economic and market conditions. The information contained herein refers to research, but does not constitute an equity research report and is not from Morgan Stanley Equity Research. The views expressed herein are those of AIP Private Markets as of March 2020 and are subject to change at any time due to changes in market and economic conditions. The views and opinions expressed herein may differ from those of other Morgan Stanley affiliates or businesses. These comments are not necessarily representative of the opinions and views of any other Morgan Stanley portfolio manager or of Morgan Stanley as a whole. While the information contained herein is believed to be reliable, we cannot guarantee its accuracy or completeness. The recipient should bear in mind that past performance is not indicative of future results. Keep in mind that forecasts are inherently limited and should not be relied upon as an indicator of future performance. The views expressed are subject to change based on market, economic and other conditions. They should not be construed as recommendations, but as an illustration of broader economic themes.

Information regarding expected market returns and market outlooks is based on the research, analysis, and opinions of the investment team of AIP Private Markets. These conclusions are speculative in nature, may not come to pass, and are not intended to predict the future of any specific Morgan Stanley investment. Certain information contained herein constitutes forward-looking statements, which can be identified by the use of forward-looking terminology such as “may,” “will,” “should,” “expect,” “anticipate,” “project,” “estimate,” “intend,” “continue” or “believe” or the negatives thereof or other variations thereon or other comparable terminology. Due to various risks and uncertainties, actual events or results may differ materially from those reflected or contemplated in such forward-looking statements. No representation or warranty is made as to future performance or such forward-looking statements. There is no guarantee that any investment strategy will work under all market conditions, and each investor should evaluate their ability to invest for the long-term, especially during periods of downturn in the market. There are important differences in how the strategy is carried out in each of the investment vehicles. Your financial professional will be happy to discuss with you the vehicle most appropriate for you given your investment objectives, risk tolerance and investment time horizon. This piece has been prepared solely for informational purposes and is not an offer, or a solicitation of an offer, to buy or sell any security or instrument or to participate in any trading strategy. The material contained herein has not been based on any individual recipient circumstances and is not investment advice, nor should it be construed in any way as tax, accounting, legal or regulatory advice. To that end, the recipient should seek independent legal and financial advice, including advice as to tax consequences, before making any investment decision. Any index referred to herein is the intellectual property (including registered trademarks) of the applicable licensor. Any product based on an index is in no way sponsored, endorsed, sold or respect thereto. By accepting this document, you agree that such document (including any data, analysis, conclusions or other information contained herein provided by the AIP Private Markets Team in connection herewith) may not be reproduced or otherwise shared or distributed to any other persons, in whole or in part, without the prior consent of an AIP Private Markets Team representative. Persons considering an alternative investment should refer to the specific investment’s offering documentation, which will fully describe the specific risks and considerations associated with such investment. This communication is only intended for and will only be distributed to persons resident in jurisdictions where such distribution or availability would not be contrary to local laws or regulations. Alternative investments typically have higher fees and expenses than other investment vehicles, and such fees and expenses will lower returns achieved by investors. Alternative investment funds are often unregulated, are not subject to the same regulatory requirements as mutual funds, and are not required to provide periodic pricing or valuation information to investors. The investment strategies described in the preceding pages may not be suitable for the recipient’s specific circumstances; accordingly, you should consult your own tax, legal or other advisors, both at the outset of any transaction and on an ongoing basis, to determine such suitability. This is prepared for sophisticated investors who are capable of understanding the risks associated with the investments described herein and may not be appropriate for the recipient. No investment should be made without proper consideration of the risks and advice from your tax, accounting, legal or other advisors as you deem appropriate. Morgan Stanley does not render tax advice on tax accounting matters to clients. This material was not intended or written to be used, and it cannot be used with any taxpayer, for the purpose of avoiding penalties which may be imposed on the taxpayer under U.S. federal tax laws. Federal and state tax laws are complex and constantly changing. Clients should always consult with a legal or tax advisor for information concerning their individual situation. This communication is intended to describe an investment strategy. It is not an offer, solicitation or sale in respect of any particular fund or other investment vehicle. Access to this investment strategy may be restricted for certain investors depending on factors such as their location and sophistication. Morgan Stanley is not responsible for the information contained on any third party website or your use or inability to use such site, nor do we guarantee its accuracy or completeness. The terms, conditions, and privacy policy on any third party website may be different from those applicable to your use of any Morgan Stanley website. The opinions expressed by the author of an article written by a third party are solely his/her own and do not necessarily reflect those of Morgan Stanley. The information and data provided by any third party website of publication is as of the date of the material which it was written and is subject to change without notice.

RISK CONSIDERATIONS
Many countries have experienced outbreaks of infectious illnesses in recent decades, including swine flu, avian influenza, SARS and the 2019-nCoV (the "Coronavirus"). In December 2019, an initial outbreak of the Coronavirus was reported in Hubei, China. Since then, a large and growing number of cases have been confirmed around the world. The Coronavirus outbreak has resulted in numerous deaths and the imposition of both local and more widespread "work from home" and other quarantine measures, border closures and other travel restrictions, causing social unrest and commercial disruption on a global scale and significant volatility in financial markets. In March 2020, the World Health Organization declared the Coronavirus outbreak a pandemic. The ongoing spread of the Coronavirus has had, and will continue to have, a material adverse impact on local economies in the affected jurisdictions and also on the global economy, as cross border commercial activity and market sentiment are increasingly impacted by the outbreak and government and other measures seeking to contain its spread. The global impact of the outbreak has been rapidly evolving, and many countries have reacted by instituting quarantines and restrictions on travel. These actions are creating disruption in supply chains, and adversely impacting a number of industries, including but not limited to retail, transportation, hospitality, and entertainment. Alternative investments are speculative and include a high degree of risk. Investors could lose all, or a substantial amount, of their investment. Alternative investments are speculative and include a high degree of risk. Investors could lose all, or a substantial amount, of their investment. Alternative investments are speculative and include a high degree of risk. Investors could lose all, or a substantial amount, of their investment. Alternative investments are speculative and include a high degree of risk. Investors could lose all, or a substantial amount, of their investment. Alternative investments are speculative and include a high degree of risk. Investors could lose all, or a substantial amount, of their investment. Alternative investments are speculative and include a high degree of risk. Investors could lose all, or a substantial amount, of their investment. Alternative investments are speculative and include a high degree of risk. Investors could lose all, or a substantial amount, of their investment. Alternative investments are speculative and include a high degree of risk. Investors could lose all, or a substantial amount, of their investment. Alternative investments are speculative and include a high degree of risk. Investors could lose all, or a substantial amount, of their investment. Alternative investments are speculative and include a high degree of risk. Investors could lose all, or a substantial amount, of their investment. Alternative investments are speculative and include a high degree of risk. Investors could lose all, or a substantial amount, of their investment. Alternative investments are speculative and include a high degree of risk. Investors could lose all, or a substantial amount, of their investment. Alternative investments are speculative and include a high degree of risk. Investors could lose all, or a substantial amount, of their investment. Alternative investments are speculative and include a high degree of risk. Investors could lose all, or a substantial amount, of their investment. Alternative investments are speculative and include a high degree of risk. Investors could lose all, or a substantial amount, of their investment. Alternative investments are speculative and include a high degree of risk. Investors could lose all, or a substantial amount, of their investment. Alternative investments are speculative and include a high degree of risk. Investors could lose all, or a substantial amount, of their investment. Alternative investments are speculative and include a high degree of risk. Investors could lose all, or a substantial amount, of their investment. Alternative investments are speculative and include a high degree of risk. Investors could lose all, or a substantial amount, of their investment. Alternative investments are speculative and include a high degree of risk. Investors could lose all, or a substantial amount, of their investment. Alternative investments are speculative and include a high degree of risk. Investors could lose all, or a substantial amount, of their investment. Alternative investments are speculative and include a high degree of risk. Investors could lose all, or a substantial amount, of their investment. Alternative investments are speculative and include a high degree of risk. Investors could lose all, or a substantial amount, of their investment. Alternative investments are speculative and include a high degree of risk. Investors could lose all, or a substantial amount, of their investment. Alternative investments are speculative and include a high degree of risk. Investors could lose all, or a substantial amount, of their investment. Alternative investments are speculative and include a high degree of risk. Investors could lose all, or a substantial amount, of their investment. Alternative investments are speculative and include a high degree of risk. Investors could lose all, or a substantial amount, of their investment. Alternative investments are speculative and include a high degree of risk. Investors could lose all, or a substantial amount, of their investment. Alternative investments are speculative and include a high degree of risk. Investors could lose all, or a substantial amount, of their investment. Alternative investments are speculative and include a high degree of risk. Investors could lose all, or a substantial amount, of their investment. Alternative investments are speculative and include a high degree of risk. Investors could lose all, or a substantial amount, of their investment. Alternative investments are speculative and include a high degree of risk. Investors could lose all, or a substantial amount, of their investment. Alternative investments are speculative and include a high degree of risk. Investors could lose all, or a substantial amount, of their investment. Alternative investments are speculative and include a high degree of risk. Investors could lose all, or a substantial amount, of their investment. Alternative investments are speculative and include a high degree of risk. Investors could lose all, or a substantial amount, of their investment. Alternative investments are speculative and include a high degree of risk. Investors could lose all, or a substantial amount, of their investment. Alternative investments are speculative and include a high degree of risk. Investors could lose all, or a substantial amount, of their investment.
Risks Relating to Private Equity Investments. Certain funds will typically invest in securities, instruments and assets that are not, and are not expected to become, publicly traded and therefore may require a substantial length of time to realize a return or fully liquidate. The respective general partners cannot provide assurance that they will be able to identify, choose, make or realize investments of the type targeted for their fund, or that such fund will be able to invest fully its committed capital. There can be no assurance that a fund will be able to generate returns for its investors or that returns will be commensurate with the risks of the investments within such fund’s investment objectives. The business of identifying and structuring investments of the types contemplated by these funds is competitive and involves a high degree of uncertainty. In addition to competition from other investors, the availability of investment opportunities generally will be subject to market conditions as well as, in many cases, the prevailing regulatory or political climate. In addition, investments in infrastructure may be subject to a variety of legal risks, including environmental issues, land expropriation and other property-related claims, industrial action and legal action from special interest groups.

DISTRIBUTION
This communication is only intended for and will only be distributed to persons resident in jurisdictions where such distribution or availability would not be contrary to local laws or regulations.

United Kingdom: Morgan Stanley Investment Management Limited is authorised and regulated by the Financial Conduct Authority. Registered in England. Registered No. 1981121. Registered Office: 25 Cabot Square, Canary Wharf, London E14 4QA. Morgan Stanley Investment Management Limited is authorised and regulated by the Financial Conduct Authority in the United Kingdom. Switzerland: Morgan Stanley & Co. International plc, London, Zurich Branch Authorised and regulated by the Eidgenössische Finanzmarktaufsicht (“FINMA”). Registered with the Register of Commerce Zurich CHE-115 415.7/70. Registered Office: Beethovenstrasse 33, 8002 Zurich, Switzerland, Telephone +41 (0) 44 588 1000. Facsimile Fax: +41(0) 44 588 1074. Hong Kong: This document has been issued by Morgan Stanley Asia Limited for use in Hong Kong and shall only be made available to “professional investors” as defined under the Securities and Futures Ordinance of Hong Kong (Cap 571). The contents of this document have not been reviewed nor approved by any regulatory authority including the Securities and Futures Commission in Hong Kong. Accordingly, save where an exemption is available under the relevant law, this document shall not be issued, circulated, distributed, directed at, or made available to, the public in Hong Kong. Singapore: This document should not be considered to be the subject of an invitation for subscription or purchase, whether directly or indirectly, to the public or any member of the public in Singapore other than (i) to an institutional investor under section 304 of the Securities and Futures Act, Chapter 289 of Singapore (“SFA”), (ii) to a "relevant person" (which includes an accredited investor) pursuant to section 305 of the SFA, and such distribution is in accordance with the conditions specified in section 305 of the SFA; or (iii) otherwise pursuant to, and in accordance with the conditions of, any other applicable provision of the SFA. In particular, for investment funds that are not authorized or recognized by the MAS, units in such funds are not allowed to be offered to the retail public; any written material issued to persons as aforementioned in connection with an offer is not a prospectus as defined in the SFA and, accordingly, statutory liability under the SFA in relation to the content of prospectuses does not apply, and investors should consider carefully whether the investment is suitable for them. Australia: This publication is disseminated in Australia by Morgan Stanley Investment Management (Australia) Pty Limited ACN: 12204 0037, AFSL No. 314182, which accept responsibility for its contents. This publication, and any access to it, is intended only for “wholesale clients” within the meaning of the Australian Corporations Act.

For illustrative purposes only. All forecasts are speculative, subject to change at any time and may not come to pass due to economic and market conditions. Past performance is not indicative of future results.