Global economy threatened by 'sustainable' investments

Governments are pressuring portfolio managers to invest their clients' funds in sustainables. Martin Hutchinson critically examines the arguments made in favour of investing in sustainables

Recent decades have seen the substantial growth of the so-called 'sustainable' investments movement, which would have portfolio managers invest their clients' funds in assets that are perceived to promote social benefits, especially benefits to the environment. In fact, such investments undermine the global economy and contribute to the political corruption that undermines civil order as well.

The aims and claims of sustainable investments

Calls for sustainable investments are often related to Environmental, Social and Governance (ESG) criteria, which were defined in a 2005 report by the firm Freshfields Bruckhaus Deringer on behalf of the United Nations[1]. Today, sustainable investments made in accordance with these criteria total about $12 trillion, up from $639 billion in 1995. Of that total, nearly $2 trillion are invested primarily with environmental goals in mind[2].

One might think environmental criteria had to do mainly with, for example, avoiding investing in projects that would pump dangerous pollutants in rivers. That sounds sensible. However, the primary environmental focus today is on whether a company's operations contribute adversely to the perceived problem of global warming. Climate alarmists who define environmental criteria allege that increased amounts of atmospheric CO_2 produced by using fossil fuels to generate energy is creating runaway warming that will seriously harm humans. But on closer examination, the argument for making investments based on this criterion collapses.

Fiduciary duties

To begin with, the environmental element of sustainable investment guidelines runs counter to the goals of fiduciaries and other investors whose primary duty or goal is to maximize returns on an investment portfolio.

Professional investors managing institutional portfolios for others, especially large retirement funds, have a legal and moral obligation to look first and foremost to their fiduciary duties to their clients. They are 'playing with other peoples' money,' not engaging in an exercise to promote their personal values. When it comes to sustainable investments, professional investors' duties often come into conflict with the environmental element of the ESG principles.

Institutional biases

To fulfill their fiduciary duties properly, portfolio managers are obliged to do their research and to understand that materials supporting sustainable investments are often biased. Many reports are produced by organizations with a vested financial interest in the topic, including large banks, utilities, renewable energy producers, and insurers. In other cases, political ideology taints sustainable investment reports.

It's better to protect prosperity and portfolios by engaging in responsible investment practices that properly balance the real risks and rewards of investing than to depend on the fantasies of 'green' extremists

A primary source of much of the climate alarmist bias surrounding sustainable investments is the reports of the UN Intergovernmental Panel on Climate Change[3]. That organization systematically excludes and even refuses to acknowledge a mountain of materials that question the climate change orthodoxy.

For example, the Nongovernmental International Panel on Climate Change has produced four volume of its *Climate Change Reconsidered* series[4]. All four volumes, each nearly 1,000 pages, include well-documented, in-depth articles by hundreds of reputable and highly credentialed scientists, scholars, and economists from around the world who offer a more realistic and sceptical assessment of climate issues.

A deep dive into the science behind climate alarmism shows it to be unsound on many levels. Predictive models fail to predict accurately or to line up with measurable data. Data is often 'adjusted' to line up with failed models[5].

Portfolio managers fail in their fiduciary duties by taking popular nostrums and climate alarmists' assertions on faith as gospel.

Pressures to invest

Portfolio managers rightly look for investment opportunities that maximize returns at risk levels acceptable to clients. But their liberty to make such investments is often limited by outside pressures, especially from governments.

Requirements that managers report the degree to which their investments support the climate alarmist anti-fossil fuel agenda or even to demonstrate that their investments promote that agenda is a major source of pressure.

In France, 2005/2008 legislation targeting pension funds and investment companies requires the *"introduction of a sustainable investment strategy and mandatory inclusion of at least one fond solidaire."*[6]

In the Netherlands, the 2008/2013 Pension Fund Act declared a *"pension fund must publicly disclose details of its sustainable investment strategy"* and a 1995 act offered tax reductions for green investments[7].

The Swiss regions of Geneva (in 2014) and Vaud (in 2015) changed their laws so that they *"now oblige their respective pension funds to comply with sustainable development and responsible investment objectives."*[8]

In September 2018, California passed legislation mandating that the state's two largest pension funds, California Public Employees' Retirement System and the California State Teachers' Retirement System, take climate change into account and report on meeting the anti-CO_2 goals of the Paris Climate Agreement[9]. (In June 2017, the Trump administration announced the United States will pull out of that agreement.)

In May 2018, the European Commission presented three proposals aimed at establishing disclosure requirements on how institutional investors integrate ESG factors in their risk processes and creating a new category of benchmarks that will supposedly help investors compare the carbon footprint of their investment[10]. No portfolio manager is likely to respond, *"I don't care about these benchmarks based on bad science. I'm protecting my clients' funds."*

If sustainable investments were good investments, governments would not need to force portfolio managers to make them.

Relying on government subsidies

Many sustainable investments are made attractive by government subsidies and favours rather than on their own merits. However, governments do a poor job of picking technologies that are economically viable.

In the US, Solyndra[11], which sought to manufacture its uniquely designed photovoltaic solar panels, received a $535 million government loan guarantee in 2009. When the company went bankrupt in 2011, taxpayers had to cover that giant loss. Any sustainable investments that would have been made in Solyndra would have been lost.

Wind turbines provide another example of a highly subsidized technology that has failed to meet expectations and has left investors with large losses. Some offshore wind farms have suffered rapid salt-induced erosion of their turbines, forcing them to shut down years before their expected end date. In total, the United States is estimated to have 14,000 abandoned wind turbines[12].

In Germany, 5,700 of the country's 29,000 wind turbines with an inherited capacity of 45 MW are expected to be abandoned in 2020, when their subsidies run out and they become uneconomical. It is thus likely that after 2020, Germany's wind power output will decline. Under German law, the entire turbine, including the massive concrete base, must be removed when the turbine ceases operating. Removing turbines is a mammoth task, because each German wind turbine weighs 3,000 tons, including its reinforced concrete base[13].

Promoting cronyism and corruption

Those portfolio managers who are tempted to virtue signal or are being eco-shamed into making sustainable investments must appreciate that they are an integral part of a corrupt, crony system—one that they are effectively endorsing by continuing to take part in it. They are handing over their clients' funds to be used by businesses and special-interest groups that profit from government power and influence, rather than by producing goods and services to sell to willing customers. Such arrangements can rightly be described as 'legal corruption.'

This is certainly contrary to the letter and spirit of the Environmental, Social and Governance criteria. The ESG criteria are supposed to allow socially conscious investors to earn profits while making the world a better place.

But unless one accepts the most extreme fears of climate alarmists—namely that without draconian government measures to restrict CO_2 emissions, humanity's future and millions of lives will be endangered—it is unreasonable to say those participating in government-supported sustainable investments are improving the planet in a reasonable way.

Global economic effects of sustainable investments

If there is any consideration portfolio managers should take account of beyond immediate returns on investment on their clients' funds, it's that there be a healthy, growing, dynamic economy in which to invest. Investors in sustainable assets promoted or mandated by government are complicit in the serious economic damage they have and will continue to cause, and they are undermining the markets upon which a sound economy depend.

A 2016 Manhattan Institute report noted, *"Between 2005, when the EU adopted its Emissions Trading Scheme, and 2014, residential electricity rates in the EU increased by 63 percent, on average. In Germany, those rates increased by 78 percent; in Spain, by 111 percent; and in the UK, by 133 percent. Over the same period, residential rates in the US rose by 32 percent. In 2016, households in Germany paid about 40 cents per kilowatt-hour for electricity, compared to the American average of about 12.5 cents."*[14]

A September 2013 article in *Der Spiegel*, acknowledged the destructive effects of the war on fossil fuels in an article exploring *How Electricity Became a Luxury Good*[15]. It reported in 2013 German consumers would be forced to pay six times the price for electricity from solar, wind and biogas plants as would be the market price for that energy.

No wonder in 2013, car manufacturer BMW decided to build a new $100 million plant to manufacture carbon fibers for its vehicles in Moses Lake, Washington. A major reason it chose not to build this factory in Germany is that German electricity costs six times more than the hydro-electric power available in Washington State[16].

Australia, one of the world's major coal producers which had generated 80 percent of its electricity from that resource, has similarly pursued economically destructive anti-fossil fuel policies[17]. The state of South Australia committed to transitioning to a system relying almost entirely on renewable energy faster than other states.

As a result, a September 2016 blackout in that state left 1.7 million people, approximately 7 percent of Australia's total population, in the dark. It was 12 days before power would be fully restored. A similar blackout hit the region in February 2017. Australian electricity prices soared and in 2018, the ruling Liberal Party replaced its leader, the countries prime minister renewable energy proponent, Malcolm Turnbull, with Scott Morrison who pledged lower energy prices.

In any case, expensive renewable resources meant to protect the environment are anything but clean[18]. A recent study by Environmental Progress, for example, warns toxic waste from used solar panels poses a global environmental threat, creating 300 times more toxic waste per unit of energy than do nuclear power plants.

Further, it would almost be physically impossible to replace all fossil-fuel generated energy with renewables. In 2016, several American environmental groups offered a plan to replace all fossil fuel energy with renewables by

2050. But the 46,480 solar PV plants envisioned would take up almost the total land area of Texas, California, Arizona and Nevada[19].

Taking the investment high road

Global commerce today is directly threatened by the unsubstantiated assumptions of climate alarmists: that the atmosphere is warming dangerously; that human use of fossil fuels rather than natural or sunspot cycles or other causes are responsible; that sustainable resources can generate enough energy to replace fossil fuels; that the clear damage to global commerce and economies caused by draconian climate alarmist policies will be offset by future benefits. Portfolio managers are put in a difficult situation because this orthodoxy does often go unquestioned.

But their fiduciary duties would at least require them to obtain explicit, informed consent from clients about the risks of so-called 'sustainable' investments. Better still, socially conscious investment managers could take the moral high ground and attempt to educate their clients about the fallacies of sustainable investments. Why passively follow an investment strategy that is likely to harm a client's interests?

It's better to protect prosperity and portfolios by engaging in responsible investment practices that properly balance the real risks and rewards of investing than to depend on the fantasies of 'green' extremists. ■

ABOUT THE AUTHOR

Martin Hutchinson based this piece on his Heartland Institute study Fallacies of So-Called 'Sustainable' Investments.
Hutchinson is a former merchant banker with more than 25 years of experience working for some of the world's most prominent financial institutions, including banks in his native Britain, United States, and Europe.
In 2000, Hutchinson moved into journalism, becoming the business and economics editor at United Press International

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Hutchinson has appeared on television on BBC, Fox News, Fox Business, TFN, and RTV Slovenija, and he has lectured at the Cato Institute, Texas Workforce Conference, Institute of Economic Affairs, National Economists Club, and at Princeton University.

Hutchinson is the author of the book Great Conservatives (2004) and the coauthor, with Kevin Dowd, of Alchemists of Loss (2010).

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