



2020 Year-end CIO Letter

Dear investors and friends,

Climate Action posted a return of 87.61% net of fees in 2020, 71 percentage points above the MSCI World Index.

We would like to make the following remarks about our performance:

1. It was achieved without a single dollar ever invested in the FAANGs and Microsoft, arguably the strongest performers in the index;
2. It was the result of a balanced combination of industrials, utilities, and technology investments, all of which were dedicated to reducing carbon emissions around the world and were trading well below their intrinsic value; and
3. It recognized the upside of many foreign companies whose stocks were undervalued for reasons unrelated to their fundamentals.

We would like to take this opportunity to thank our investors for their continued trust and support, especially at a time when the rest of the market was skeptical about the upside potential of a strategy focused on reducing carbon emissions. Our bottom-up stock picking approach combined with a portfolio construction was instrumental in delivering outperformance while minimizing risks. By contrast, many investors including those concerned about the environment, have simply favored large-cap momentum growth tech stocks, namely the FANGs, whose actions to help with climate change are negligible and leave investors overly exposed to valuation and regulatory risks.

The investment industry has a major role to play in selecting and properly valuing companies with a positive impact on the environment vs. those that continue to emit greenhouse gases. As the oil and gas or the auto industry found out, investors can flee entire sectors of the economy when they fear secular changes and adverse policy measures.

We believe that the fight against climate change will be a great unifying cause in the near future. As an example, one of the most encouraging steps favored by both sides of the aisle is to accelerate CO₂ emission reductions through the development of carbon capture, utilization, and storage (CCUS). As can be seen below, this is not just an area of recent interest; it has been around for years. The US already boasts the world's largest carbon capture facility: the Petra Nova coal-powered plant owned by NRG near Houston, Texas.



Source: <https://www.nrg.com/case-studies/petra-nova.html>

The above plant has captured 92% of its CO₂ emissions since it went into operation in 2016. Sadly, it recently stopped operating because of COVID-19. Still, it suggests that all emissions from fossil fuel plants, responsible for 20% of the world's total CO₂ emissions, could theoretically be captured at their source and prevented from entering the atmosphere. Could CCUS just need a boost to become mainstream? A new administration may be just what is needed to accelerate its development:

"Areas in which Biden hopes to make far-reaching investments includes at least one new term: negative-emissions technologies. That phrase encompasses [a number of approaches](#) for drawing greenhouse gases out of the atmosphere".

Source: <https://www.technologyreview.com/2020/11/09/1011859/>

The US is also home to the world's largest carbon capture project, Project Tundra in North Dakota. This project, if approved by the EPA, will result in removing 95% of carbon emissions from the Milton Young generator, equivalent to 600,000 gasoline-fueled vehicles taken off the road every year.

<https://www.projecttundrand.com/>



Critics of CCUS point out that so far, the technology has allowed fossil fuel production to continue unabated, including coal plant operations and enhancing oil field recovery. However, CCUS now seems poised to take off as new discoveries and business models encourage its widespread adoption. One such discovery was announced by the MIT a year ago:

"A new way of removing carbon dioxide from a stream of air could provide a significant tool in the battle against climate change. The new system can work on the gas at virtually any concentration level, even down to the roughly 400 parts per million currently found in the atmosphere."

Source: <https://news.mit.edu/2019/mit-engineers-develop-new-way-remove-carbon-dioxide-air-1025>

This is significant because carbon capture has been focused primarily on the highly concentrated levels of CO₂ coming out of coal plants, whereas it is much harder to isolate it from the atmosphere where it can be found in a diffuse state.

Among the new business models that successfully utilize carbon capture, the cement and construction industry deserve a special mention for sequestering carbon dioxide into building materials:



CarbonCure for Ready Mix

CO₂ injected via CarbonCure improves the compressive strength and performance of ready mix concrete, which enables ready mix producers to optimize their mix designs while reducing their concrete's carbon footprint.



CarbonCure for Precast

CO₂ injected via CarbonCure improves the compressive strength and performance of precast concrete, which allows precast producers to further optimize their mix designs and reduce the carbon footprint of their precast products.



CarbonCure Masonry

CO₂ sequestered via CarbonCure reduces the carbon footprint of concrete masonry, which enables masonry producers to differentiate their CMU brand and increase sales with the growing green building market.

While the above initiatives are bound to take off, carbon capture will address potentially 30% of CO₂ emissions vs. less than 1% today. Clearly, there is a need for governmental support to increase the scale of CCUS operations. But many programs are under way to foster a wider adoption, both at a state and federal level. Starting with the Federal Bill passed in February 2018, dubbed 45Q:



"45Q generates a tax credit: \$50 per ton of carbon dioxide (CO₂) buried in [underground storage](#), \$35 per ton for either [utilization](#) or enhanced oil recovery. With no cap on the available tax credits and 12 years to claim them, This bill is poised to do for carbon capture what similar incentives did for wind and solar power: unleash private sector investments that catapult the technology into its maturity."

Source: <https://www.triplepundit.com/story/2018/federal-budget-bill-includes-massive-tax-credits-carbon-capture/13441>

The above was closely followed by new regulations and tax incentives in California:

- "In September 2018, California Air Resources Board voted on including CO₂ reductions from Carbon Capture and Sequestration technologies under its Low Carbon Fuel Standard Program by incorporating a CCS Protocol into the regulation.
- Credits under the LCFS program stacked with the 45Q tax credit for CCS make CO₂ reductions worth between approximately \$135 and \$150 per metric ton. This is a valuable combination of incentives to enable CCS technology to deploy more widely."

Source: <https://www.catf.us/2018/11/californias-co2-reduction-program/>

As the California Clean Air Task Force points out:

"North America has the enormous capacity to sequester CO₂ with about 500 years' worth of captured energy-related emissions in its deep geologic formations. For California projects, there are billions of tons of geologic capacity in depleted oilfields and deep sedimentary basins such as those in the central valley. "

Other countries are also well on their way to turn CCUS into a viable and lucrative industry, starting with Norway's Northern Lights project:

"The full-scale project includes capture of CO₂ from industrial capture sources in the Oslo-fjord region (cement and waste-to-energy) and shipping of liquid CO₂ from these industrial capture sites to an onshore terminal on the Norwegian west coast. From there, the liquified CO₂ will be transported by pipeline to an offshore storage location subsea in the North Sea, for permanent storage."

Northern Lights Project

Source: <https://northernlightscs.eu/en/about>



The above developments make us more optimistic than ever about our sector and its potential to generate attractive returns for investors.

We look forward to updating you again on our progress and hopefully sharing more good news about our collective fight against climate change.

We would like to thank our investors for the trust they have placed in us at a time when many questioned the case for carbon focused portfolios. The case has only grown more compelling today. It is incumbent upon us to apply the lessons learned from science and continue to look for companies that actively develop solutions to global warming. We look forward to welcoming many more to this cause.

With our very best wishes for 2021,

Ariane