Policy Brief

European pension funds increasingly divest from fossil fuels—but company pension funds not competing for clients lack behind

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https://doi.org/10.1016/j.ecolecon.2021.107237 (free download)

Messages for policy

- Fossil fuel divestment gained momentum since the Paris Agreement, particularly for funds that are publicly-owned (and hence often held to higher standards) and for funds that have to compete for clients
- There is ample room to further increase divestment among publicly-owned funds (including going beyond coal), which could be mandated by policymakers that oversee them
- Fostering knowledge exchange and data-sharing on climate-related risks and opportunity could benefit smaller funds that are not linked to the financial industry

The policy problem

Divestment from fossil fuel companies could help align financial flows with climate targets and reduce the related risk exposure of investors. Long-term institutional investors, such as pension funds, are particular important in that regard. Yet, fund managers reach different conclusions whether to divest. Policymakers increasingly consider green financial policies to stimulate climate-friendly investment behavior, but without a better understanding of the drivers for deciding to divest or not it is difficult to design effective policy interventions.

The findings

From the 1000 largest European pension funds, we find that 129, or 13%, have divested from fossil fuels, representing USD 2.6 trillion in assets under management (33%). Most of the divestments concern coal only. We find that divestment is more likely among larger and publicly owned pension funds (see Figure). Among privately owned pension funds, open funds competing for clients are more likely to divest compared with company funds restricted to employees.

Fossil fuel divestment by pension fund type
[USD billion Assets under Management]

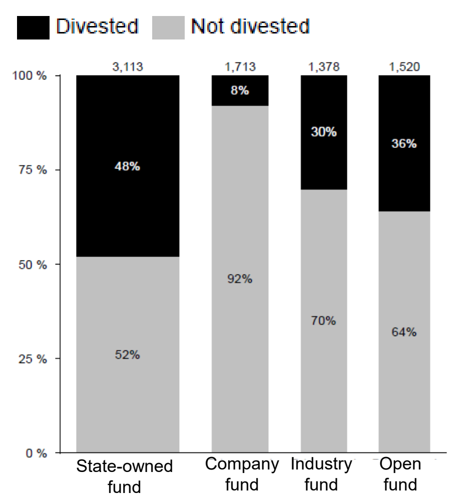

Figure: Divestment from funds with beneficiaries from the state/state-owned companies, from one company, from an industry, and funds open to individual investors

We identify size, ownership and market competition as key determinants for divestment decisions, leading to implications for policymakers aiming to foster fossil fuel divestment (see box on top right). We find weaker evidence for sectoral differences (e.g., higher likelihood in financial sector), albeit independent of carbon intensities, and a positive effect of climate policy stringency.

Our study

We compiled a new dataset on the 1000 largest European pension funds, including financial and institutional information, as well as hand-researched details on divestment steps based on public announcements of the funds. Regression analyses are used to test five hypotheses on divestment determinants that were derived from the literature on climate risk considerations and on socially responsible investments.

Link to the full article (free download), and related work at www.cfp.ethz.ch

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