

Sustainability Practice

CEO interview: CDPQ invests in climate action

Charles Emond oversees more than \$291 billion in investments around the world. He wants to see real action on climate change.



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Charles Emond has a unique perspective on the powerful role that capital can play in driving change. He is the president and CEO of Caisse de dépôt et placement du Québec (CDPQ), which has worldwide investments of more than \$291 billion, including in pension funds, insurance plans, and other organizations in Québec. Emond came to the role in February 2020 with a commitment to invest sustainably while generating returns and helping develop the economy of tomorrow.

As part of that commitment, Emond cochairs the Investor Leadership Network (ILN) CEO Council, representing the leaders of 14 global investment firms that want to help drive the transition to a more inclusive and sustainable low-carbon economy.

Emond recently spoke with McKinsey senior editor Diane Brady about his increased focus on addressing climate change and how that is shaping CDPQ's investment strategy. An edited version of their conversation follows.

McKinsey: What inspired you to take on this leadership role at ILN?

Charles Emond: From the pure organizational perspective, this initiative is dear to our hearts. ILN is focused on concrete actions, giving investors tools to assess and incorporate climate risk into their portfolios. Here are the sectors that produce the most carbon and the levers that reduce it. As a portfolio manager, it helps you assess a company's disclosure. Is it credible? Is it complete? Disclosure is absolutely key to making informed decisions. It helps to drive a conversation.

McKinsey: Your companies have invested in ESG [environmental, social, and governance] for years. What's changed?

Charles Emond: A CEO recently told me that, a year or two ago, ESG was the last question that would

come up in [an investor] meeting, if there was time. Now those meetings start with that question. We have 42 depositors that care about these issues and trust us to manage their money. We have this commitment to be carbon neutral by 2050. To drive sustainable and inclusive growth, it's helpful to have a grid and act accordingly.

To meet our commitment to be carbon neutral by 2050, we need to act now. In 2017, we really focused our climate strategy on three things. The first was increasing investments in low-carbon or greener assets by 80 percent. We doubled our target so that today we have about \$26 billion in those assets. We're one of the top investors in the world in renewables. The second target was reducing our carbon intensity by 25 percent by 2025. Today, we're at 21 percent. The third was ensuring that leadership aligns with the low-carbon transition.

The team has annual carbon targets that impact their compensation. We give an ESG report to our depositors and the public. Instead of being a constraint, having these targets tied to compensation has become a source of pride.

It's moved from being a "nice to have" to a "need to have." For shareholders, it's no longer peripheral. There's a vast and growing number of people who demand it. Increasing low-carbon assets is easy. When we invest in a wind farm or light-rail transit, everybody applauds. Reducing carbon intensity can be trickier. The reality is that some sectors pollute more. We think it's important that investors not run away from those problems but confront them and help companies transition to cleaner output. The question is how to do it. That's why we're measuring our impact not only from greener assets but also from helping the transition of the real economy underneath. You've got to have both.

McKinsey: What's the outlook for the fossil-fuel industry in terms of attracting capital?

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Charles Emond: Transition is the key word. We closely monitor sectors with high carbon emissions. As long-term investors, we are working to accompany companies on this important transition. We expect to see improvements and are helping them to identify more sustainable business opportunities and drive effective change.

McKinsey: How do you work with companies to help them make this transition?

Charles Emond: A few years ago, talking about emissions was like raising a sensitive topic to an old friend. Now that friend likely understands the importance. It's no longer a conversation about the need to change but rather the pace of change. You can influence that through a dialogue with the management team. You can also use your votes, which speak loudly. We help them set targets and identify sustainable opportunities. We ask them to stop harmful practices, if there are any. And we tell them to improve disclosure.

In November of last year, we announced a new policy governing the exercise of voting rights for public companies. It targets 300 companies in our portfolio in about 28 countries. It sets our expectations in areas such as disclosing climate risk. We give people time to change, but it's meant

to have some teeth because the clock is ticking. So it's a balancing act. We're supportive, but we also provide what I'd call "healthy tension."

McKinsey: Do you see this as a fiduciary duty or a moral duty?

Charles Emond: Whether you're an investment manager, pension fund, or a portfolio company, if you don't act according to these new standards, it's going to impact your revenues. Increasing inequalities impacting minorities, younger people, and women will affect your long-term growth and our collective benefit. We're not creating an ecosystem that sets winning conditions. It's arithmetic. And this is the right thing to do.

McKinsey: Are you worried about climate change on a personal level?

Charles Emond: Yes. Absolutely. We believe the clock is ticking, and science is clear about that. I don't need numbers to get worried, but they can get you even more worried. In Canada, the weather-related costs of the last decade alone are double the total cost of the past 30 years. And Europe's got the hottest year on record. So it's like compounded interest here. At some point, there's going to be a limited ability to reverse this trend.



Charles Emond

We're managing the pensions of six million Québécois. We owe it to them and to future generations to invest in making this transition. Also, I have two kids. And even though they're young, they're sensitive to these issues.

McKinsey: What do you think is the role of regulation in addressing these issues and in driving the behaviors you want to see in your portfolio companies?

Charles Emond: You always need regulation. Governments can help set up a framework so that behaviors adapt accordingly, or there's an incentive to move in a certain direction. Then I think the private sector is sometimes better equipped to set that into action.

The voting policy I talked to you about spells it out. Our preference is to engage with companies, to lead by example and benchmark our own progress, to give investors relevant tools, and to endorse the behavior we're looking for.

And that's why we think that the climate-change initiative is so important, because it will speed up the use [of carbon-reducing tools.] Do I see a need for regulation? Yes. It's part of the solution, but it doesn't bring you to the final destination, in my mind. You need widescale endorsement of these objectives.

McKinsey: How should investors measure the success of their portfolios going forward?

Charles Emond: You've got to anchor it on principles, moving from capital to constructive capital. That means taking a broader view of investment. Depositors need solid returns over the long term, and factoring in climate change is part of that. Now there is another layer whereby you take a step back and say, "What is the impact that's coming with our investing? Is that directionally positive? Is that in line with our core values?" These are all difficult things to measure, but there's a sanity check on top of all of it at that end that is an important element.

McKinsey: If I'm a CEO of a company, what do I need to do to get more of your money?

Charles Emond: Well, I'd say get ahead of the curve. Show leadership in your industry and ambition that will bring in capital, and hence, good returns. When there's an important trend, differentiate yourself. Best-in-class companies in every sector attract capital and differentiate themselves.

That's about competitive positioning, which is a language that CEOs can relate to. The mindset is also shifting. The sales pitch needs to be less focused on the bad things that might happen if you don't do something, and instead focus on the good things that could come if you do something.

There are a lot of possibilities out there. To me, it's about showing leadership and conviction, not just checking the box because you have to. If we take climate change as an example, it is a factor that is here to stay and will become more and more material in the future. Whether we are talking about transition or physical impacts, companies that today are fully integrating the climate factor within their strategies to help identify opportunities and mitigate risks have a better chance to outperform in the future.

McKinsey: What is your message to CEOs?

Charles Emond: This train is not reversing. It's here to stay, and it's going to accelerate. We talk about that with leaps forward in technology. It's also happening with climate and ESG. These issues are here to stay and may actually represent the biggest investment opportunity.

There's a Venn diagram in which doing the right thing actually creates a good outcome. I think we're at this juncture; this crisis probably made us realize a lot of important things at an important moment. We can't miss this opportunity or let that momentum drop, because it will have an impact for generations to come. It's a privilege to invest people's money, but it comes with responsibilities.

Charles Emond is the president and CEO of Caisse de dépôt et placement du Québec. **Diane Brady** is a senior editor in McKinsey's New York office.

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