Fossil Fuel Divestment Protects Long-Term Investment Portfolios

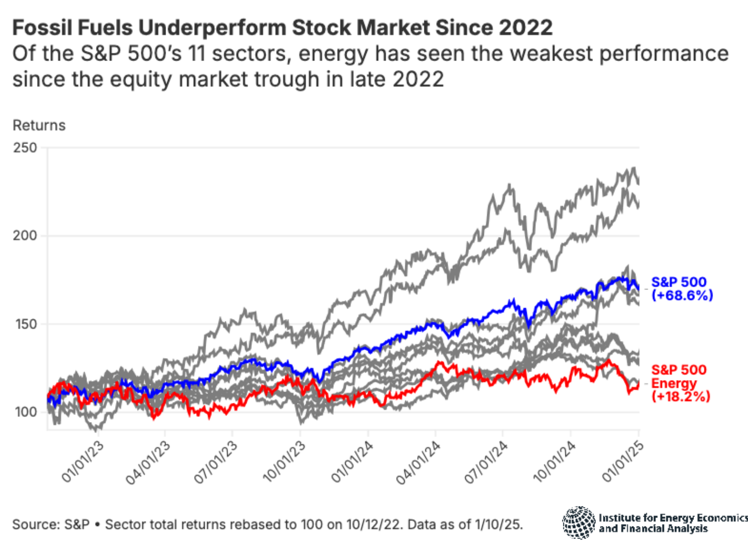
Financial underperformance and intense competitive pressures drive a negative long-term outlook

The fossil fuel sector has lost its investment rationale. It has underperformed the broad market for a decade and has a negative long-term financial outlook. It faces intense competitive pressures that it is poorly positioned to successfully navigate.

Divestment from fossil fuels is a defensive move to protect the long-term value of an investment portfolio while continuing to meet investment return targets.

Fossil Fuels Have Financially Underperformed for a Decade

- The fossil fuel sector has exhibited the lowest returns and highest volatility among sectors of the S&P 500 index for a decade.
- The sector has underperformed the market seven times since 2014 and performed worst among sectors five times.
- The weighting of fossil fuels has collapsed from nearly 30% of the S&P 500's value in 1980 to 3.2% as of December 31, 2024.



Fossil Fuels are Poorly Positioned to Navigate Competitive Pressures

• Volatile commodity prices threaten prices, revenues, and profits
Oil and gas prices are prone to large and extended drawdowns due to intense competition between oil and gas producers amid growing supply and slowing demand growth. This combination tends to undermine prices, lower revenues, and suppress profits. Geopolitical disruption has driven price spikes in the recent past, but the effects have not endured.

• Non-fossil technologies take growth and market share
Fierce competition from renewable energy and electrified technologies is slowing demand growth and increasingly taking market share across key end-markets for fossil fuels, including transport, electric power, and space and water heating.

• Fossil fuel companies don't have a credible business plan for the future

Fossil fuel companies are not meaningfully investing in renewable energy: the sector devotes less than 4% of its capital expenditures to clean energy, and its clean energy spending accounts for under 1.5% of total clean energy investment globally.

Fossil fuels have no commercially viable low-carbon technology. Despite fifty years of research and development, history is littered with failed carbon capture utilization and storage (CCUS) projects. Existing facilities capture far less carbon dioxide than the 90-95% level advertised by proponents. Retrofitting the technology onto carbon emitting facilities requires significant capital outlays and adds operating costs, which are increasingly seen to require permanent public subsidies.

Fossil fuel investments in petrochemicals face a deteriorating competitive landscape. The fossil fuel sector has made significant investments into the production of petrochemicals as a diversification strategy away from pure fossil fuel extraction. Petrochemical markets are seeing overcapacity that will likely weaken prices and undercut expected financial returns.

Divestment is a Tool for Protecting Portfolio Value

More than 1,600 investment funds who manage a total of $40 trillion have committed to divest from fossil fuels, including pension funds in New York City, New York State, Oregon, Quebec, Australia, and Europe.

Pension funds in other states like New York have divested their investment portfolios without incurring significant losses or management fees. This is because there are now many fossil-free investment strategies and products available at low costs. For example, the University of California's investments office provides fossil-free investment options at a cost of only 5 cents per $100 of invested money. It invests a different pool of money fossil-free at a cost of only 1 cent per $100.

Fiduciaries of long-term investment funds should carefully consider the negative long-term financial outlook for fossil fuels for protecting their fund's investment portfolio. Proper consideration demands deliberation over multiple investment options that meet a fund's investment return targets without fossil fuels in the portfolio. Trustees can only come to a fully informed judgment of the impacts and any timing considerations after considering a plan specifically designed for their fund.

READ IEEFA'S RESEARCH:

- https://ieefa.org/resources/passive-investing-warming-world
- Credit raters' warnings on carbon risk
- How divestment can help investors meet their goals