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FUNDS

Wellington's Climate Strategy

By Crystal Kim

As sustainable investing becomes more mainstream—and embraced by mainstream active managers—it's evolving. Like all evolution, it's accompanied by tension and an explosion of creativity.

Wellington Management, the venerated $1 trillion money manager, has increasingly become a behind-the-scenes force in sustainable investing. The firm subadvises two of three funds for Domini Investments, one of the pioneers of socially responsible investing. And it was recently tapped to expand its longstanding relationship with Vanguard Group, which has launched its first actively managed fund that incorporates environmental, social, and governance criteria into its stock-picking; Wellington will subadvise the fund.

Wellington brings an unusual approach to this effort. Last year, the firm partnered with Woods Hole Research Center, which studies the effect of climate change around the world. The result has been an interesting new investing methodology.

Call it spatial finance, says Chris Goolgasian, Wellington's director of climate research. Spatial finance is essentially building a three-dimensional map that layers climate-science data on top of stock fundamentals and macroeconomic indicators, he explains. The mapping initiative, in turn, helped garner a dozen research initiatives at Wellington, and the shop is now paying very close attention to a factor that most asset managers might not have considered—geographic location.

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"Location is not a classic asset-management input, but we believe it will have a much bigger impact in the future," Goolgasian says.

Phil Duffy, the president of Woods Hole Research Center, adds, "We set up this partnership based on an assumption that the investment world wasn't really thinking about physical climate risk. That turned out to be truer than we thought."

Extreme heat puts a company's or municipality's assets—customers, labor force, and supply chains—at risk. That's where location comes into play. Areas most exposed to extreme heat could see mass migration, as livability becomes an issue. "Once we showed these maps to our investors, it generated ideas across fixed income, equity, global, macro, and emerging markets—some right down to the individual security level," says Goolgasian.

For example: Take two hospital bonds with similar ratings and yields, one from the U.S. Northeast, and the other from the Southwest. An investor might think they're identical. Wellington, however, says that because the bond from the issuer in the Southwest has greater exposure to extreme heat and migration risk, it could be mispriced. The logic is that migration caused by heat could rapidly change the economics of a municipality and its ability to pay back its stakeholders.

This partnership is new, and won't necessarily be incorporated into all of the strategies that Wellington oversees. But the firm says it has uncovered stock ideas using a similar approach. Goolgasian says certain companies stand to benefit as people and nations most exposed to heat, drought, or natural disasters, which tend to go hand in hand, spend money to address those problems. Which stocks those are Goolgasian won't say. That's one thing that hasn't changed about Wellington's style—the shop still jealously guards its portfolio.