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After Bubbles in Dotcoms and Housing, Here's the Carbon Bubble

Tom Gara | May 16, 2013

You're familiar with the dot com bubble and U.S. housing bubble. True financial geeks may even know of the Poseidon nickel bubble. But have you heard of the carbon bubble?

The Carbon Tracker Initiative, a London based group, first raised the specter of a bubble in 2011. It totaled up the amount of carbon that publicly traded companies held in reserves of discovered oil, natural gas and coal. Then it asked what would happen if all of this was taken out of the earth and burned. The simple answer: catastrophic climate change. If the earth was to avoid a temperature increase of more than two degrees centigrade, it argued, only 20% of these fossil fuels reserves could be extracted.

Most of the carbon – the basis for these companies' gargantuan market valuations – was "unburnable." Investors should realize, it argued, that if government policies curtailed carbon emissions, the value of these companies would fall. The bubble, if it exists, would pop.

A few months ago, the concept of a carbon bubble went mainstream. Last December, the International Energy Agency lent its credibility when it noted that many of already-discovered deposits of coal, oil and gas might need to be placed off limits by future government steps to constrain carbon. Then came reports by Standard & Poor's and this one from British bank HSBC PLC. The Carbon Tracking Initiative, in conjunction with the London School of Economics, updated their research in April.

But these reports didn't answer one big question: do investors care? That question got its first airing earlier this month at the annual shareholder meeting of Consol Energy Inc. "It is of concern to investors," an activist-sponsored proposal stated, that some of the company's reserves "may become unusable, unmarketable, or otherwise not economically viable as a result of greenhouse gas restrictions." It asked for a report on how Consol planned to respond.

This Tuesday, Consol released the proxy vote results. The proposal received 19.7% of the votes cast. That is well short of a majority, but shows that a small but not insignificant minority of institutional shareholders saw some merit in at least looking at the question of how much coal the company will be able to burn.

Andrew Behar, chief executive of the As You Sow foundation, which sponsored the proposal, said the vote was proof that "all energy companies need to look at this issue very seriously."

Is climate change a material risk to shareholders? Mr. Behar thinks so, but for the time being, the majority of Consol's shareholders were happy to stay with the status quo.