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WHAT'S NEXT FOR GREEN FINANCE AFTER UNITED STATES WITHDRAWAL FROM PARIS CLIMATE AGREEMENT?

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Donald Trump's decision to withdraw from Paris Agreement is unquestionably a major signal by his administration, as it demonstrates a real intention of implementing the policies outlined during the election campaign[1]. From a political perspective, the message is unexpected, forceful and certainly will generate economic repercussions, especially in the global energy production landscape in the coming years. Nevertheless, we believe that in the financial markets, Trump's decision will not change the well-defined growth path of sustainable investments from the whole business community. In fact, this trend has already been underway for years and, above all, is supported by the EU, China, India and now even individual US states and cities.

In the short term, there will probably be an increase in volatility in specific sub-sectors linked to renewable energy, but we do not estimate significant changes in market direction following this announcement.

From an **international regulatory perspective**, we would underline that:

- In 2015, the US was committed to reducing greenhouse gas emissions by 30% by 2025 from the 2005 levels through promoting renewable energy[2].

- Trump announced his intention to renegotiate the US' entry into the climate agreement with different terms in order to politically and indirectly support the traditional US energy industry and to not contribute to the $100 billion fund promoted by the Paris Agreement[3].

- The process of withdrawing from the Paris agreement will last approximately four years, which leaves the US in the treaty until 2021, one year after the next US presidential campaign.

- The US will not exit the UN Framework Convention on Climate Change, the UN Convention which has led to the Kyoto Protocol in the past.

Furthermore, in our view, **Trump's decision shows elements which demonstrate the administration's intention to put the agreement under discussion rather than boycotting it completely**. Also, Trump's intentions of not contributing to the climate fund will mean that the US would not be involved in this international initiative and therefore would have little control of this fund. By doing that, Trump would allocate public money from international cooperation on climate change to domestic affairs. For this reason, in our opinion abandoning the Paris accord championed by the US and the international business community represents a crucial point which has not been fairly emphasized by the media as it expresses the US isolationist agenda.

The choice of exiting the Paris agreement will most likely impact the energy industry linked to climate change mitigation. In the short term, there may be an increase in volatility, especially in US companies operating in the industry, as well as the international ones exposed to the US market.

On the one hand, concerns could increase for the companies focused entirely on renewable energy and renewable technology. The most exposed companies will be the pure players of the industry – such as the large players in solar, wind and yieldcos – which are currently benefiting of state subsidies to compete with traditional energy companies. Due to the high capital requirements of the latest technological innovation, the pure players generally require support from the federal government.

From a growth perspective, the vast majority of the pure players have already grown significantly during the last two years and today are heavily leveraged and operate principally in the primary market looking for valuable assets (i.e. construction and management of new installations heavily dependent on public subsidies) conducting M&A and refinancing activities (i.e. offshore wind and solar power).

On the other hand, Industrial players, companies in industrial and manufacturing sectors, such as water and waste management, which have minimal revenues from the renewable energy, will be less exposed to a potential reduction in renewable energy incentives. Their revenue streams are marginally linked to renewable energy production, while they are more positively exposed to the increasing private sector demand for innovation in CO2 reduction (i.e. energy efficiency, green buildings, sustainable transport).

Looking at the **market reaction**, renewable energy companies were more volatile and had relative price declined in the hours following the announcement[4]. By contrast, the traditional energy and infrastructure sectors (i.e. oil and gas, construction) did not show

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significant variations. In the last months, markets had already priced in many uncertainties connected to climate change, such as the reduction of federal subsidies for the renewable energy sector.

Comparing the renewable energy and fossil energy indices from the beginning of the year, renewable energy recorded a + 9.45% increase compared to a -7.54% decrease for the oil and gas index[5].

In addition, there are three factors that will counter Trump's decision:

- **The renewable energy industry in the US will not stop suddenly.** Recent data from the International Energy Agency shows that the industry is growing by 7% every year, is accounting for approximately 4 million jobs and is one of the most profitable sub-sector in the energy business[6]. The Trump Administration can could not completely ignore these statistics.

- In the US, **individual states will continue to implement environmental policies and support renewable energy policies, leaving unchanged the positive outlook on the industry**. Some states, led by California and New York, have already declared publicly their intention to meet their commitment to the standards set in Paris. Internationally, the EU, Canada, China and others have strongly reaffirmed their commitment to a transition to a low-carbon economy by encouraging sustainable investments. As a consequence, political support for fighting climate change is undebatable. In this scenario, Europe and China would be the most likely driving forces of innovation, having the tremendous opportunity to bridge the leadership gap left by the US Administration.

- **The private sector will continue to drive growth in the field of energy efficiency**, as most large companies have realized that investing in efficiency and sustainability represents a tactical cost-reduction process able to deliver benefits in the long-term. Within in the business community, the level of environmental awareness continues to rise and consumers as well are increasing demanding sustainable products.

In our view, these factors, coupled with the drastic cost reduction in solar and wind power production, global storage devices costs and technological progress, will more than compensate the unbalances generated by Trump announcement, reinforcing a global trend that will be hard to stop using political statements.

[1] https://greatagain.gov

[2] https://www.thegwpf.com/in-white-house-momentum-turns-against-paris-climate-agreement/

[3] https://www.whitehouse.gov/blog/2017/06/01/president-donald-j-trump-announces-us-withdrawal-paris-climate-accord

[4] www.bloomberg.com/markets

[5] iShares Global Clean Energy ETF; iShares Global Energy ETF. YTD as of June 1, 2017

[6] www.iea.org

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