Market Commentary – US withdraw from Paris Climate Agreement

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US president Trump has decided to withdraw from the 2015 Paris Climate agreement. While we regret this decision as we are worried about the future of our planet, we would also argue that this decision is potentially economically dangerous for the country he wants to make great again. We also believe that the impact of the decision will be mainly psychological as the combination of improved and improving technologies and economic realities in energy generation and energy efficiency, state regulation and individual and corporate reaction will reduce the potential negative impact. Furthermore, the terms of the existing agreement only allow for withdrawal no earlier than 4 years after the ratification, which for the US means November 2020, normally the month of the next US presidential election. So either terms will be renegotiated, or the agreement will be an important discussion topic during the next presidential campaign.

We believe withdrawing from the Paris agreement will have significant international political consequences as the US will join a select number of countries who have not signed the agreement, Syria and Nicaragua to be more precise. After signing first and withdrawing a few months later, the US could be seen as an unreliable partner in future international negotiations, climate related or not. We also believe that with this decision, president Trump is trying to postpone the inevitable. Creating a climate which almost encourages companies to not adjust to future needs, is likely to lead to economic disaster. Investors don't like uncertainty and neither do companies when making long term investment decisions. Recent initiatives by corporate America to put pressure on the president to not withdraw from the Climate agreement are to be seen in this context.

It is difficult to predict how equity markets will react, although we believe the reaction will be muted. Immediately after the Trump victory in the US presidential election, fossil fuel companies performed strongly, while more sustainable sources of energy generation underperformed. This reversed however this year to date. Renewables are economically viable. Individual state regulation also calls for greenhouse gas emission reductions. Companies and individuals continue to invest in renewables and energy efficiency as it gives them more energy independence and access to affordable, relatively stable energy prices. Cheap gas prices push utilities to continue the switch from coal to (less emitting) gas for their electricity production. We believe, this will not change now that the US has decided to withdraw from the climate agreement.

As a responsible investor, or even just as an investor, we strongly believe in a transition towards a less carbon intensive economy as consumers prefer more energy efficient products and the cost or renewable technologies continues to fall. At first glance, we believe this decision will have little impact over the short term on equity prices and we shall therefore not change our investment strategy after this decision.

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