BT Investment Solutions

Turning over a new leaf

A global agreement on environment action finally exists

Kyoto. Copenhagen. Paris. Scenes of major environmental discussions and yet, Paris holds a key difference to its predecessors.

The recent Paris agreement signals the first time 195 nations have reached and signed an agreement. Adrian Trollor, Head of Portfolio Construction and Sustainability, looks at the key components of the Paris agreement and what it means for investments.

A fresh start

The Paris climate change agreement was reached on 12 December 2015 and includes:

+ A long-term goal to limit global warming to 1.5 degrees Celsius above pre-industrial levels.
+ Commitment to be carbon neutral between 2050 and 2100.
+ Pledges on emissions by individual nations to be reviewed and strengthened every five years. (Pledges can be market, regulatory and other measures.)

The hallmarks of change

Previous agreements struggled for success and this agreement has some key differences compared to the past.

+ The inclusion of developing countries and specific emission targets for them.
+ Each nation submitted individual pledges prior to the agreement rather than negotiating these during discussions.
+ Support from the UN and the US.
+ The involvement and pledges of 1200 parties outside countries like companies such as Westpac Group.

What does the agreement mean for Australian policymakers?

Australia has pledged a reduction of 26-28% from the 2005 level of greenhouse gas emissions by 2030. The current policy and regulation is the Direct Action Plan and Safeguard Mechanism which consists of an Emissions Reduction Fund – where companies purchase emissions reductions through a reverse auction by optional involvement – and the safeguard mechanism where companies are penalised for exceeding an emissions reduction baseline or ceiling from past emissions.

However, there is a possibility of further policy changes in the future, as debate over the most effective method to limit greenhouse gas emissions continues.

Depending on the policies, these will impact on companies and consumers alike in negotiating potential costs to implement, with resources and heavy industry in particular likely to be impacted. The International Energy Agency has estimated $US13.5 trillion globally will need to be invested in energy efficiency and low-carbon technologies between now and 2030.

The impact to investments

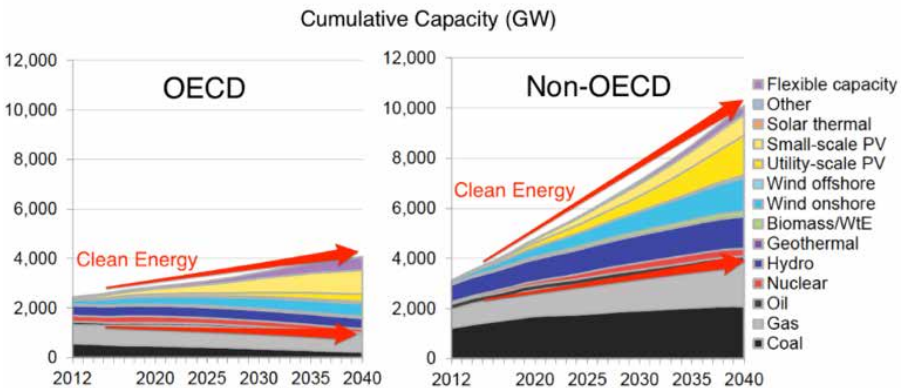
Investors need to be aware of the potential risks and opportunities that arise due a global response to climate change.

Regulatory changes globally based on the Paris agreements are likely to have significant implications for investment strategies.

Companies operating in high emission industries, such as energy sub-sectors and the utilities sector, are particularly likely to see substantial structural changes to meet emissions constraints and regulatory requirements in the coming decades. This includes power generation, steel, cement, aluminium, LNG, oil refining and coal, oil and gas production industries. For example, the Australian electricity sector, which when compared globally is particularly fossil fuel intense, will require significant change.

Companies operating in renewable energy, or businesses with innovative and flexible models which can respond rapidly to change, are likely to benefit from the Paris Agreement. Consumers are also likely to benefit over time given the cost of renewable energy has continued to fall as the market for it has expanded. Interestingly, of anywhere, emerging markets are best positioned to capture the opportunities of renewable energy sources given high levels of investment as shown in Chart 1.

Chart 1: Power shifts to emerging markets



Source: Bloomberg New Energy Finance

Outside of companies, other opportunities for investments are the introduction of new products and services. An example of this in the finance industry is the rise of Green Bonds which allow investors to fund projects with positive environmental benefits. The issuance of Green Bonds in 2015 totalled $41.8bn according to the Climate Bond Initiative. Clearly technologies that play a role in supporting the transition that has been signed up to as part of the Paris agreement are going to be attractive.

Reaching agreement

There is no question the Paris Agreement is a historic moment for the world. It is an agreement that spells hope for the environment but means a variety of changes, and opportunities, for investors and companies alike.

BT Financial Group is a signatory to the United Nations' Principles of Responsible Investment and also to the Montreal Pledge, which commits investors to measuring and publicly disclosing the carbon footprint of their investment portfolios. As part of the Westpac Group, BT Financial Group is also a signatory to the Paris Pledge which demonstrates a commitment to support the objectives of the Paris Agreement.

For more information on this, or how these principles are incorporated in your investments, please contact BT Financial Group.

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