A MOMENT IN MARKETS – HOW COP26 CAN MOVE MARKETS AND CHANGE THE WORLD

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Nothing quite like a crisis to catalyse change.

The 2021 United Nations Climate Change Conference (COP26) is an excellent opportunity for policymakers to reaffirm their commitment to climate change goals. Remember it was COP21 in 2015 when the historic Paris Agreement was signed. Call it a crunch, call it a crisis, but with everything happening in energy markets recently, the timing of the conference couldn't be better.

But why is this conference receiving so much attention? Two key things have changed since the Paris Agreement. First, the urgency from policymakers to act has increased. And second, green technologies – which will enable the transition to a cleaner world – have moved from the margins to the mainstream. These two shifts are more prominent today than ever before.

Global stock of passenger electric vehicles (EV) rose from just above 1 million in 2015 to over 10 million in 2020[1]. With sales on an exponential trajectory and a proliferation of new EV models coming to market, the automobile industry may see a profound shift in the next five years. This is unsurprising given the bans on the sale of new internal combustion engine vehicles coming into effect in many countries within the next decade. Such a notion was unheard of in 2015.

So, what can we expect from the latest COP? We can hope policymakers will plug a crucial gap in our approach to tackling climate change. While many countries have made net zero pledges, mostly shooting for 2050, a clear roadmap for getting there is generally missing. Getting all the answers we need is unlikely by the end of this conference, but we may still see steps being taken in the right direction.

Having said that, progress is already being made. Europe's increasing focus on using carbon pricing as a preferred tool for achieving its climate goals is one clear example. The proposed Fit for 55 legislation aims to achieve a 55% reduction in greenhouse gas emissions by 2030 compared to 1990 levels. Such interim targets make the ultimate net zero ambition more fathomable. They also move markets, as we have seen in the case of the strong rally in European Union Carbon Emission Allowances (EUAs) – a market that is expected to become progressively tighter as Europe pursues decarbonization.

Actions of policymakers are moving markets elsewhere as well. China has embarked on an arduous journey of decarbonizing its coal-heavy aluminium industry by curtailing production and looking to transition towards renewables. This process could take years keeping aluminium undersupplied for years, an expectation creeping into the metal's market pricing.

The UK, which was the first major economy to commit to reaching net zero emissions by 2050, has now pledged to make its electricity supply entirely green by 2035 and introduced a ban on the sale of new internal combustion vehicles from 2030. Such lofty goals require significant investment. The government is currently seeking £50-60 billion each year from the private sector[2]. With so much that can be (and needs to be) done, the figures may end up being even higher. From building an entire network of battery energy storage systems to support a transition towards renewable energy to put in place a robust infrastructure of electric vehicle charging, there is much work to do.

But seldom has the opportunity for an industry to thrive been so well supported by policy. Governments are likely to continue paving the way for private investing to step in – to fuel the innovation and fund the infrastructure. For investors taking a holistic view of the megatrend, the opportunities may be endless.

Sources

[1] International Energy Agency Global EV outlook 2021

[2] Reported by the Financial Times

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