Tortoise QuickTake
Sustainable Energy Podcast

Tortoise

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Welcome to the Tortoise QuickTake podcast. Thank you for joining us. Today, Tortoise provides a timely update on trending topics in the market.

Hello! This is Michel Sznajer, Portfolio Manager at the Ecofin Platform of Tortoise in London. Today we would like to talk about The European Green Deal. Despite the recent setback of the COP25 meeting in Madrid, momentum for more ambitious and more urgent "Climate Change" objectives has been growing through 2019 as we witnessed new commitments at three levels: Corporate Level in the likes of RWE and Amazon who announced the objective to reach carbon neutrality by 2040, the level of Institutions, like in November, the European Investment Bank announced it will not finance fossil fuel energy projects after 2021, as well as Governments. Back in June, France and the UK made legally binding commitments to reach net zero carbon emissions by 2050.

Moreover, a week ago, the European Commission has reached another major milestone by presenting its Green Deal, as progress to-date is impressive yet insufficient. Indeed, between 1990 and 2018, the EU reduced greenhouse gas emissions by 23%, while the economy grew by 61%. However, current policies will only reduce greenhouse gas emissions by 60% by 2050.

So, the new President of the European Commission, Mrs von der Leyen, has made this major piece of policy the cornerstone of her mandate with the following two key objectives:

- First, the EU will be climate neutral by 2050
- Second, the EU will increase the EU's greenhouse gas (GHG) emission reductions target for 2030 to at least 50% and towards 55% compared with 1990 levels. The current target is only 40% reduction.

In order to achieve these targets, the EU Commission puts the emphasis on the following areas that happen to also be core to our Energy Transition strategies:

First, reduce carbon emissions in the energy sector as 75% of EU GHG emissions come from the energy sector.

Second, more than double the annual building renovation rate, currently between 0.4 to 1.2% in the EU in order to reduce energy consumption because buildings represent 40% of the EU energy consumption.

Third, reduce transport emissions by 90% by 2050. Transport will represents 25% of EU carbon emissions. In that context, fossil-fuel subsidies should end and the Commission will look at the current tax exemptions for aviation and maritime fuels.

Fourth, accelerate the industry's transition to a sustainable model. The industry represents 20% of EU GHG emissions but only 12% of materials used by the industry come from recycling.

And then the fifth and final point, the EU wants to develop requirements to ensure that all packaging in the EU market is reusable or recyclable in an economically viable manner by 2030.

So moving onto the Carbon Border Tax. In a historical develop and potentially a game changer in global trade, the EU recognizes the need to harmonize global emissions standards or, at the minimum, level the playing field to the highest standard by taxing the higher carbon content of some imported goods. In that context, the EU Commission introduces for the first time the concept of a Carbon Border Tax (CBT), and it quotes, "Should differences in levels of ambition worldwide persist, as the EU increases its climate ambition, the Commission will propose a carbon border adjustment mechanism, for selected sectors, to reduce the risk of carbon leakage. This would ensure that the price of imports reflect more accurately their carbon content."

The Carbon Border Tax is a recognition that unchecked globalization of trade is not compatible with the global challenge of climate change. Hence, the expectation is that taxes will encourage faster adoption of clean manufacturing worldwide. However, the implementation of a CBT will be complicated as it needs to respect WTO rules and be compatible with the Emissions Trading System (ETS) currently in place in Europe. The EU Commission has therefore indicated that it might start with a few polluting sectors like steel or cement before extending the CBT broadly.

So what about the political ambitions and how to put those into action? Some will certainly believe that these political ambitions are doomed to fail given the quasi-insurmountable objective to reconcile diverging interests with political, social and economic forces pulling in various directions. However, the sense of purpose in Europe has never been stronger, at all levels, and we can expect to see momentum as the EU Commission will prepare research, publish reports and introduce legislation with a sense of urgency in the coming years. As such, the Commission has set clear milestones to ensure implementation:

- By the end of this year 2019, each Member States will present their revised energy and climate plans
- By March 2020: First, the EU commission will introduce the European 'Climate Law' to enshrine the 2050 climate neutrality objective in legislation. Secondly, the Commission will adopt an EU industrial strategy to address the twin challenge of the green and the digital transformation. Finally, by the spring 2020, the Commission will present the 'Farm to Fork' Strategy, paving the way to formulating a more sustainable food policy
- Then by the Summer 2020, an impact plan to increase the EU's GHG emission reductions target for 2030 to at least 50% and towards 55% compared with 1990 will be introduced
- Then by June 2021: The EU Commission will review and propose to revise where necessary all relevant climate-related policy instruments, including the Emissions Trading System. The Commission will also propose to revise the legislation on CO2 emission performance standards for cars and vans, to ensure a clear pathway from 2025 onwards towards zero-emission mobility

So why is this meaningful opportunity for us and for investors? The Green Deal is in our view a strong signal that the Energy Transition is entering a phase of acceleration. The fast-declining cost of offshore wind, the spread of rooftop solar, the broadening line-up of electric cars (EVs), bans on diesel…are a few examples of the Energy Transition in motion with the space attracting a growing share of investments going forward. The EU Commission has quantified that achieving the current 2030 climate and energy targets will require €260 billion of additional annual investments, about 1.5% of 2018 GDP.

The Green Deal focus on cleaner power, more efficient buildings and industries, cleaner transportation and better environmental and waste/recycling practices parallel the themes we invest in. We see the EU Green Deal as a catalyst as well as a strong endorsement of what we do and are reinforced in the idea that investors need to increase their exposure to the space.

Thank you for listening to our podcast.

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