

Letter n°92

Why have stocks linked to the energy transition collapsed on the stock market?

(1) The continued development of fossil fuels.

"Moderation is a fatal thing. Nothing succeeds like excess." Oscar Wilde.

- Oscar Wilde, in the opening quote, referred to success linked to excess. Here, we think about the excesses in the development of fossil fuels and the stock market success of companies in these sectors.
- So, we will start this Letter with 5 questions: why, since the beginning of 2021, this outperformance of companies related to fossil fuels and the underperformance of those related to energy transition? Why do the goals of limiting global warming to 1.5 degrees compared to the pre-industrial era seem unattainable? Why is there an acceleration in investments in oil? Why a record production of coal? Why does the production of plastics continue to grow to such an extent?
- So many questions, so many elements of answers to be found, and that is the objective of this Letter 92, awaiting Letter 93, which will delve into the issues related to renewable energy.

Why do climate goals seem unattainable?

Reasons for satisfaction:

Certainly, the Chinese and Americans, the world's top two polluters, have just agreed to triple renewable energy capacities by 2030.

Certainly, emissions in 2023 are decreasing by 3% in the United States and by 7.4% in Europe.

Certainly, investments in fossil fuels in 2023 only represent 60% of investments in renewable energy.

Certainly, according to the International Energy Agency, China's investments in renewable energy exceeded \$500 billion in 2022. The strongest growth there has been in solar energy because installations are twice the total installed capacity in the United States.

Reasons to be pessimistic:

Notwithstanding these four reasons for satisfaction, four temperaments must be presented:

For the first time, in November, the global temperature was two degrees higher than the seasonal average of the pre-industrial era.

The warming trend, by the end of the century, is now 2.9 degrees because the goal of reducing greenhouse gas emissions by 22 billion tonnes by 2030 to limit warming to 1.5 degrees seems unattainable.

The current trend is only a 2% reduction in greenhouse gas emissions in 2030 compared to 2019, far from the ambitious 43%.

This year, emissions are increasing by 4% in China and 8.2% in India, emissions from ships and planes by 12%, oil exploitation-related emissions by 1.5%, and gas-related emissions by 0.5%.

Overall, worldwide emissions are still increasing in 2023 by 1.1%, a pace higher than the average of the last 10 years, which requires a 50% reduction in emissions in the next 7 years to meet the goal of a 1.5-degree warming. A rather unrealistic gamble in the current state!

Why the increase in investment in hydrocarbons?

Initial objectives:

A few years ago, oil companies were announcing an exit from fossil fuels; today, they are counting on staying in, as demand and profit margins increase.

Oil companies were supposed to allocate half of their investments to renewable energies; currently, it is only 2.5%, and European oil companies, such as TotalEnergies, Shell, BP, and Equinor, are the main contributors to these investments.

The sad reality:

Three records set this year: global crude oil production at 102 million barrels per day (Mb/d), U.S. production at 13.2 Mb/d, and Chinese consumption at 17.1 Mb/d. Three records that will be surpassed next year.

- Why do the United Kingdom, Canada, Australia, the United States, Russia, and Brazil allow the exploration of new oil fields? Why do the United Arab Emirates, organizers of COP 28, plan to invest only \$15 billion in renewable energy when they anticipate \$150 billion in expenditures in hydrocarbons over the next five years? Why do around 20 oil-dependent countries, relying on oil for over 30% of their revenues, hinder the energy transition?
- Why are the five majors developing, according to Energy Monitor, nearly 160 fields in addition to the 1350 in production? Why do Exxon and Chevron want to make acquisitions in shale oil? Why did Exxon acquire Pioneer for \$60 billion and Chevron acquire Hess for \$53 billion? Why has Exxon's stock more than doubled from \$45 at the beginning of 2021 to \$100 today (peaking at 120) to reach a market capitalization close to \$400 billion? It's because Exxon is capable of reporting results of \$58 billion in 2022, double those of BP, as it continues to increase its crude oil production, ignoring investments in renewables under the pretext of focusing on decarbonization research. Meanwhile, BP, after announcing a 40% reduction in crude oil production between 2019 and 2030, has adjusted its expectations to only -25%.

The conviction of oil companies rests on the idea of the planet's inability to do without oil in the coming years.

- In the global energy balance, oil accounted for 50% in 1970 and, today, still represents 34%. In the meantime, the share of renewable energy has increased from 0.1% to only 3.3%. In 2014, spending on exploration and production reached \$750 billion, in 2020 and 2021, due to the COVID environment, just over \$300 billion, but by 2024, it is expected to rise to \$420 billion.
- In the long term, the price of oil will be sensitive to the evolution of electric car prices since 40% of the world's crude oil consumption results from transportation.
- The war in Ukraine and the increase in energy prices resulted in a doubling of subsidies to fossil fuels in 2022 compared to 2020, reaching \$1.3 trillion, according to the IMF, of which \$830 billion is for price relief for consumers and the rest for hydrocarbon and coal producers, already favoured by record profits.

According to the International Energy Agency (IEA), the oil and gas sector would have allocated only 2% of its investments to clean energy.

Disappointments in carbon and methane capture:

- Investments in low-carbon emission projects, favoured by American oil companies, have so far yielded neither significant successes nor substantial budgets.

In 2022, only \$20 billion was spent on carbon capture projects. Moreover, nearly two-thirds of these expenditures come from four European companies: Equinor, TotalEnergies, Shell, and BP.

Carbon capture advocated by American oil groups remains a distant prospect. According to the IEA, it would be necessary to invest \$3.5 trillion annually by 2050, an unrealistic figure as it is equivalent to the current revenue of companies in the sector.

- Methane, through leaks from oil field operations, coal mines, and gas transport, accounts for nearly 30% of global warming. It is crucial to reduce methane emissions.

Around 160 countries and about 50 oil companies have committed to halting their methane emissions by 2030, but the largest emitters, China, India, and Russia, have not yet joined this objective.

Why a record coal production?

Since the late 18th century, the coal industry has been infinitely more deadly than nuclear power, but coal has been the source of our current wealth, and today, emerging countries see coal as a cost-effective energy source.

The two reasons for hope:

Europe and the United States accounted for 40% of global coal consumption just 30 years ago, but today it is no more than 8%. Other countries could follow suit.

By 2024, according to the IEA, renewable energies could surpass coal in global electricity production, as China's increased solar energy capacity for the year 2023 alone would be equivalent to twice the installed capacity in the United States.

Concerns:

- Chinese and Indian, accounting for 70% of global consumption between them, seem to want to ignore the problem and meet the energy demand in their countries.
- But why resort to coal, whose emissions are 1.5 times higher than oil and 2 times higher than gas? Why this expansion of coal, the most polluting fossil fuel, responsible for 40% of emissions, compared to 32% for oil and 21% for gas? Why do Chinese authorities allow a one-third increase in production capacity compared to the end of 2021, and why do they not consider reducing coal production before 2027, given that China consumes 4.8 billion tonnes out of the 8.3 billion consumed worldwide?
- In China, electricity demand is growing rapidly. Coal has the advantage of not being imported, and coal represents more than 55% of the energy mix. China opens the equivalent of two coal-fired power plants per week, but fortunately, according to the IEA, 2025 could mark a peak in these developments.
- In India, in a phase of demographic growth and urbanization, emissions this year will surpass those of the entire EU; 75% of electricity production is derived from coal, and coal represents 45% of the energy balance.

India declares that it does not aim for carbon neutrality before 2070 and plans to triple its coal production excluding open-pit mining.

In response to criticism, Modi argues that India's coal consumption per capita is half that of Americans and that the country will triple its renewable energy capacity by 2030.

- China and India are not alone. Other countries are still developing capacities. Consider Bangladesh, Indonesia, and Pakistan.

The 3 reasons for the increase in production:

- Why did global coal demand reach a record level in 2022 of 8.3 billion tonnes despite a decrease in the share of coal in the global electricity mix from 38% in 2020 to 35.6% in 2022?
- There are three reasons for this: the increase in electricity consumption worldwide, drought leading to a reduction in the flow of hydroelectric dams, and a current coal price in India and China that is cheaper than gas.

Why these developments in plastics?

- Annual plastic production has doubled worldwide in the last 20 years, and according to NGOs, it could triple by 2060.
- Only 9% of these plastics are recycled, and due to the resistance of oil-producing countries and plastic producers, no agreement has been reached to limit production.

Conclusion: "Scratch a pessimist and you will often find a defender of privilege" William Beveridge.

These are the reasons for the reluctance and resistance of coal or hydrocarbon-rich countries, eager to exploit the wealth beneath their soil and defer the energy transition.

Beyond this remark, 6 conclusions can be drawn:

- ***The geopolitical angle:*** One of the few countries to benefit from climate change could well be Russia, as its agricultural lands will expand.
- ***The climate angle:*** Certainly, some banks are slowing down their loans for hydrocarbon financing, but it is not sufficient as carbon emissions already reach 40 billion tonnes per year.

According to the UN, the global reduction in CO2 emissions will only reach 2% by 2030 instead of the targeted 43% to limit global warming to 1.5 degrees.

- ***The financial obstacle represented by cheap fossil fuels:*** In France, for example, around 1900, it took two hours of work to pay for a litre of gasoline; in 1950, it took 30 minutes, and today it takes 10 minutes of the minimum wage. The evolution is similar for gas. To accelerate the development of renewable energy, fossil fuels would need higher taxes, but it is socially impossible to implement.
- ***Growing energy demand:*** Fossil fuels generate over 80% of the world's primary energy and are not likely to be replaced soon. According to the IEA, at the current pace of renewable energy development, investments in fossil fuels will still be needed to meet demand. Renewable energies are growing rapidly but only represent 15% of the energy balance, and three-quarters of greenhouse gases result from fossil fuels.
- ***Insufficient mutual aid:*** Indonesia, South Africa, Vietnam, and India consider international assistance necessary to offset the additional costs of renewable energy development. However, there is at least a two-year delay in the promised financial aid from rich countries to emerging economies.
- ***The stock market horizon:*** Since January 2021, the MSCI World index has appreciated only by 2.4%, but Exxon has gained 118%, TotalEnergies 63%, Chevron 57%, BP 56%, and Peabody, in coal, 607%. Since that date, we have been bullish on the sector, and unfortunately, we will continue to be so.

Geneva, 14 December 2023

Bruno Desgardins

Bruno Desgardins
CIO
Switzerland



SingAlliance Pte Ltd

20 McCallum Street
#18-01 Tokio Marine Centre
Singapore 069046
T: +65 6303 5050
E: info@singalliance.com

SingAlliance (Switzerland) SA

16bis rue de Lausanne
1201 Geneve
Switzerland
T: +41 22 518 85 85
E: info.switzerland@singalliance.com

SingAlliance (Hong Kong) Ltd

Unit 904-907, 9/F Dah Sing Financial Centre
248 Queen's Road East
Wanchai, Hong Kong
T: +852 2639 3659
E: info.hongkong@singalliance.com

**SingAlliance Pte Ltd
(DIFC Representative Office)**

The Gate, Level 13 East, Office 10, DIFC
PO Box 121208 Dubai, UAE
T: +971 (0) 4 401 9158
E: info.dubai@singalliance.com



This document does not constitute an offer or a solicitation to purchase or subscribe financial instruments. Information contained in this document has been obtained from carefully selected public sources. Although every care has been taken to ensure that this information is accurate at the time of publication, no representation is made as to its accuracy, completeness, or truthfulness. Any opinion contained herein is subject to change at any time without notice. Past performance is not indicative of future results.