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GS SUSTAIN

The Low Carbon Economy

Goldman Sachs

Equity Research

US withdraws from Paris; Technology stays in the Driver's Seat

US exit from climate agreement increases policy uncertainty

President Trump announced yesterday that the US will withdraw from the 2015 Paris Agreement. Key US climate policies (such as various tax credits and emission standards) are not affected by this decision. Other key signatories (including China, the EU and India) have indicated that they remain committed to their climate targets.

But is unlikely to shift dynamics of the low carbon transition

With innovation and markets, rather than solely politics, increasingly driving the use of low carbon technologies, we believe the impact of the US decision on the low carbon economy should not be overstated (see *GS SUSTAIN: The Low Carbon Economy: Technology in the Driver's Seat*; Nov 28, 2016). Rather, we see an increase in regulatory uncertainty in carbon-intensive sectors such as autos, utilities and energy as the main implication of the withdrawal, as companies and investors try to anticipate further decisions by the Administrations on key climate policies such as the CAFE standards.

Market share gains for key technologies likely to continue

We maintain our view that technologies such as LEDs, EVs, and wind & solar are likely to continue to see rapid market share gains on the back of further cost reductions and performance improvements. Electric vehicles are a case in point, with 2016 marking a fourth year of 50%+ volume growth and a series of announcements for new, long-range fully electric offerings from major carmakers. As they seek to prepare for a potential disruptive shift to electric vehicle technology across key global markets, we think companies are unlikely to scale back their EV investment in response to regulatory changes in individual countries.

Note: The following is an abridged version of *US withdraws from Paris; Technology stays in the Driver's Seat,* published June 2, 2017.

Jaakko Kooroshy
+44(20)7051-2875 jaakko.kooroshy@gs.com
Goldman Sachs International

Derek R. Bingham
(415) 249-7435 derek.bingham@gs.com
Goldman Sachs & Co. LLC

Justus Schirmacher
+44(20)7774-1080 justus.schirmacher@gs.com
Goldman Sachs International

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Q&A on the US decision to exit the Paris Agreement

What did President Trump announce?

President Trump announced yesterday that the US would withdraw from the Paris Agreement, fulfilling one of his campaign promises. At the same time the President announced that he would "begin negotiations to re-enter either the Paris accord or an entirely new transaction".

The President did not specify how the US would exit the Agreement. The Agreement stipulates that a country can only withdraw from the Agreement three years after it went into force, and mandates a one year notice period – potentially putting the withdrawal date off until around the next Presidential election in 2020.

How does this change US climate policies?

The immediate impact for US businesses and foreign businesses operating in the US is likely to be limited. Under the Paris Agreement, the US had submitted a so-called "Intended Nationally-Determined Contribution" (INDC) pledging to reduce its greenhouse gas emissions by 26-28% below its 2005 level by 2025. This commitment, however, was voluntary and the Paris Agreement has no enforcement mechanism. The Obama administration's Clean Power Plan (CPP), the main instrument for achieving the reduction target, continues to be litigated and is under review by the Trump administration.

Other key US climate policies remain unaffected by the decision, including the federal tax credits from solar (ITC), wind (PTC) and electric vehicles, the Corporate Average Fuel Economy (CAFE) standards, and state-level renewable portfolio standards (RPS).

What are the implications for the Paris Agreement?

The implications for the Paris Agreement are unclear. Key signatories including China, the EU and India have pledged to maintain their commitment to the Agreement. While withdrawals by other countries are possible at this stage, they do not appear particularly likely, given the limited formal obligations the Agreement puts on its signatories.

However, the US withdrawal could impact the level of ambition for the next round of voluntary INDC commitments, which are due to be announced ahead of the next major climate summit in 2020.

What are the likely implications for low carbon technologies?

We believe the growth dynamics for key low carbon technologies including LEDs, electric vehicles, wind and solar power will remain largely unaffected.

The regulatory pressure facing companies to adopt low carbon technologies in industries like autos, lighting and power generation will only change marginally with the US decision. Indeed, there is a long history of such policy reversals, which have contributed to volatility but have ultimately had a limited impact on the overall growth trajectory for the low carbon economy (see The Low Carbon Economy: GS SUSTAIN Equity investor's guide to a low carbon world 2015-25 Nov 30, 2015).

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