

Sustainability is the new security issue

How the war in Ukraine has **changed the sustainability transition**

By Massimo Castelli

Head Global Strategy, Global Sovereign Markets, UBS Asset Management

How the changing geopolitical and financial landscape impact sustainability and the implications for alternative asset classes

Recent events, in particular, the Russian invasion of Ukraine have the implications for sustainability and the energy transition, especially in Europe. Change is upon us regarding sustainability in this new environment marked by geopolitical uncertainty and rising commodity prices.

Energy security and energy transformation are two sides of the same coin: and the list of reasons to speed up the energy transition is getting longer. In particular, the green agenda could get a boost from the national security agenda, and this may help to mobilize the resources for alternative energy sources.

In the long term we believe that there is no conflict between energy security and energy transformation. However, in the short term, when there is risk for 'energy blackmail' or international pressure not to finance war efforts with energy purchases, the security environment might actually dictate short-term action that could set back the green agenda to some degree.

For example, the more extensive use of coal-fired plants or the easing of carbon emission limits is a cheap way to stimulate sectors of the economy that are affected by high energy prices. Another problem could come in the short term from a lack of international cooperation.

Deglobalization is a central issue

In a world marked by deglobalization, regionalization and fragmentation, the setting of international environmental standards in cooperation in international bodies or conferences is critical, but there is risk, for instance, for the Paris Agreement or Glasgow Climate Pact to be impaired by or influenced by the geopolitical decision-making process.

With deglobalization likely on the horizon, the free flow of capital and growing market risks could slow down the adaption of effective tools to fight climate change. One of the casualties could be the expeditious implementation of a truly global carbon pricing system.

Finally, there is the question of capital to fund the energy transition: the estimates of the amount of investment that will be needed in order to fund the energy transition is in the trillions of dollars.

Looking at the role of government on the fiscal front, countries which already experience a substantial rise in government tariffs as a result of the pandemic, and in times of fiscal restraint, could put public investment, particularly in the energy area, under pressure.

At the same time, we also see some renewed effort, for instance the reorientation of the EU Next Generation Fund toward the energy transition, as the war in Ukraine has put more pressure on European countries to accelerate the decrease of their dependency on Russian gas.

Overall, this means the financial sector will have to provide massive additional financing to fill the gap, not only for ambitious nice-to-have projects, but to ultimately guarantee energy security for Western economies. It also appears clear the private sector will have to play a much more active role going forward in order to mobilize the investment needed to fund the energy transition.

Alternative assets can play a role

The good news is that investors are willing to deploy capital to this effort, and alternative asset classes are one of the best vehicles for that.

For example, long/short investing in a global transition to net zero. With the reshoring and decarbonizing of supply chains in full progress, and further amplified by the war in Ukraine, there are investment opportunities not only on the long but also on the short side.

For instance, what are the most interesting technological innovations today that are investable and that could get us closer to net zero? And, conversely, what are the companies and industries that could be left behind? Looking beyond energy securities, to commodities in general, what are the implications of rising metal and commodity prices on the energy transition?

In the real asset sector there are implications from the current geopolitical events for the energy infrastructure and real estate sector. It is clear that carbon reduction will have a measured impact on energy investing. So, what is the investment outlook for the energy storage, LNG, nuclear or hydrogen sectors, and, in particular, following the war in Ukraine, what are the differences across regions?

With the operational emissions of buildings accounting for just less than 30% of total global emissions, what will it mean for future regulation of new buildings?

Finally, what action could be taken in the transition from brown to green for existing buildings, and what that might mean for investors?

In the context of the changing energy landscape in Europe, North America and emerging markets as a result of the war, soaring commodity prices and deglobalization, there will be challenges for investors, but also, we believe, many opportunities, particularly in the alternative space.

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