THE INFLATED COST OF THE ENERGY TRANSITION

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Attempts to limit global temperature rises by 1.5° could add 1.6 percentage points to inflation each year over the next decade, according to Carmignac research. But the alternative of permanent climate disruption is far costlier.

***Lloyd McAllister**, head of sustainable investment, **Raphaël Gallardo**, chief economist, and **Michel Wiskirski**, commodities specialist, explore the true cost of the energy transition over the next decade.*

Climate change is inherently inflationary. Rising average temperatures and their seasonal fluctuations, natural disasters and enduring environmental changes will have negative effects on the supply of goods and labour and positive effects on local demand.

Contrary to the unmitigated scenario, the inflationary effects of the energy transition are both more predictable and time-limited. And its social consequences are far easier for public authorities to manage.

In order to limit temperature rises by the Paris Agreement target of 1.5° versus pre-industrial levels, an inflation tetralogy – namely greenflation, fossilflation, demandflation and strandflation – can be expected to add 1.6 percentage points to annual inflation over the next 10 years, according to our research.

THE INFLATIONARY IMPACTS OF THE ENERGY TRANSITION OVER THE NEXT DECADE*

Greenflation:
+01% on annual inflation
- Wind turbines 40% more expensive than previously.
- Green metal prices expected to double over the next 10 years.

Fossilflation:
+0,8% on annual inflation
- Maintenance and investment slowing on fossil fuel infrastructure - decay.
- Drop in output.
- Oil prices to rise by 20% per year.

Demandflation & strandflation:

+0,7% on annual inflation

Demandflation

- Resources being diverted from other areas of the economy.
- Consumption postponed as a result.
- Higher prices and higher interest rates ensue.

Strandflation

- Price premium of 25% to 300% on new technology adoption: green cement, heat, aviation, shipping.
- Forced creation of stranded assets - government intervention - will have a large inflationary effect.

*All figures based on Carmignac research

While this is comfortably better than the unmitigated scenario, this transition period will still pose considerable challenges to central banks, the guardians of price stability.

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