Green energy funds underperform the oil and gas sector

While the global demand for clean and renewable energy sources is growing, the performance of the funds that invest in them has been lagging the conventional energy sector, which is dominated by oil and gas companies. Since January 2022, the total returns of exchange traded funds (ETFs) that focus on solar, wind, and other green technologies have been negative, while the traditional energy funds have risen strongly.

One of the main reasons for this divergence is the surge in oil prices, which has boosted the profitability of the fossil fuel industry and hence its attractiveness to investors. Another factor is the rising cost of financing new green energy projects, given the sharp increase in interest rates seen since the US Federal Reserve delivered the first hike in this cycle in March 2022.

The underperformance of green energy funds illustrates that fundamentals are the most important determinant of investment-allocation decisions, and that environmental, social and governance (ESG) considerations are secondary.

Unless policymakers intervene to alter the relative fundamental investment proposition by supporting renewable energy at least to match governments’ subsidies of oil and gas production, the long-awaited capital reallocation will struggle to materialise.

Source: IATA Sustainability and Economics, Macrobond.