

Trump's Climate Policy is Based on Cost-Benefit Analysis



By Theo Vermaelen , INSEAD Professor of Finance

President Trump's decision to withdraw the U.S. from the Paris accord is based on economic arguments.

President Donald Trump has pulled the United States out of the Paris climate agreement and, interestingly not because he does not believe in man-made global warming, something we could have expected since he called global warming a “hoax” during his campaign. He could have used many **different arguments** to question the theory that climate change is mainly driven by human activity. Instead he used an economic argument. Signing up to the Paris Agreement would impose large costs on the U.S. economy without any significant impact on global temperatures. In his **speech**, Trump cited a 149-page **study** by National Economic Research Associates that argues the Paris Agreement would cost 2.7 million jobs by 2025, totalling loss of US\$3 trillion in lost GDP by 2040. He also cites the forecast of a study that predicts that the Paris Agreement would result in 0.2 degree Celsius less warming, a trivial

impact. So, a project with significant costs and very little benefits should be rejected, as we teach in our investment courses.

Not surprisingly, the conclusions were immediately challenged by the Paris Agreement [supporters](#). The first response, as usual, is to discredit the economic report by discrediting its authors: the report was produced for the American Council for Capital Formation that receives money from Exxon-Mobil and The Petroleum Institute. (Full disclosure: I am not subsidised by the oil and gas industry.) And, of course, unlike climate change forecasts, long-term macroeconomic forecasts are highly uncertain. Nevertheless, not even the strongest Paris Agreement defenders can deny some significant costs to developed countries, i.e. the US\$100 billion per year (starting in 2020) of global climate finance to be raised by the Green Climate Fund (GCF). Although the private sector is supposed to contribute, the fact is that taxpayers of the developed countries are expected to subsidise the GCF. To wit, the GCF currently has received \$10 billion, largely financed by American, European, Canadian, Japanese and Australian [taxpayers](#), with US\$3 billion contributed by the U.S. by the Obama administration. So far I have been unable to find any trace of contributions from the private sector, which is not surprising considering that the S&P Global Clean Energy Index has lost 15 percent per annum over the last 10 years. So Trump is right in that the agreement represents a massive wealth transfer of trillions of dollars from developed countries to developing countries. United Nations officials in charge of environmental policy have admitted this; [Ottmar Edenhofer](#), who co-chaired the UN Intergovernmental Panel on Climate Change working group from 2008 to 2015, said, "One has to free oneself from the illusion that international climate policy is environmental policy...We redistribute de facto the world's wealth by climate policy."

Tipping point?

The second response is to claim that Trump has cherry-picked a study that shows only a 0.2C degree decline in global warming because of the Paris accords. According to [Climate Scoreboard](#), collaboration between MIT and Climate Interactive: "Full implementation of current Paris pledges plus all announced mid-century strategies would reduce expected warming by 2100 to 3.3 degrees Celsius, a reduction of 0.9 degree compared to the no change prediction of 4.2 degrees Celsius."

This would mean we spent trillions of dollars to reduce global warming by only 21 percent. Considering the significant uncertainty of making predictions over an 80-year horizon, this reduction does not seem to be statistically significant, in contrast to the costs. Moreover **3.3 degrees Celsius** is above the “tipping point” where global warming would be run out of control. Implementing the Paris Agreement is like wanting to build a bridge across a river, but only having enough resources to build 20 percent of the bridge. In this case, it is better not to build a bridge and think of alternatives to reach the other side.

A third and most peculiar critique on Trump’s decision is that the Paris treaty is not a **binding** commitment. In 2015, the European Union had wanted to make it a binding commitment, but the only way all countries would sign on was to make the treaty non-binding. Countries can set their own targets, and revise them at any time. If they fail to meet their targets, there is no penalty. So, the Trump critics want him to follow the hypocritical attitude of his fellow politicians: pretending that you make a commitment without any intention of keeping it. At a time when voters questions are becoming increasingly sceptical about mainstream politicians, this is a remarkable recommendation indeed.

President Trump’s decision to withdraw from the Paris Agreement should not come as a surprise. Trump is not a traditional politician driven by ideology. He is a businessman trading off costs and benefits. Even the defenders of the treaty admit the impact of the Paris Agreement on the climate in 2100 will be trivial. At the same time, if the commitments are respected, the costs to taxpayers of developed countries will be substantial and honest European politicians should disclose this to their voters. If the commitments are not respected the whole Paris Agreement is an exercise in extreme hypocrisy. So, I believe Trump should be complimented, rather than scorned, for rejecting leadership in wealth destruction and/or hypocrisy.

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