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The U.S. Election and Energy: More Than Meets the Eye

The presidential candidates have well-known policy profiles on energy, but how could they translate in the real world?

The Biden-Harris administration has staked much of its political capital on the energy transition—curbing carbon emissions and encouraging the use of electric cars and renewable energy—while former President Donald Trump is known for his support of the fossil fuel industry and streamlining energy regulation. Given recent progress on alternative fuel sources, slowing shale growth in the U.S. and burgeoning energy needs, what do those stances mean for the energy sector? The potential answers may surprise you.

Where We Are

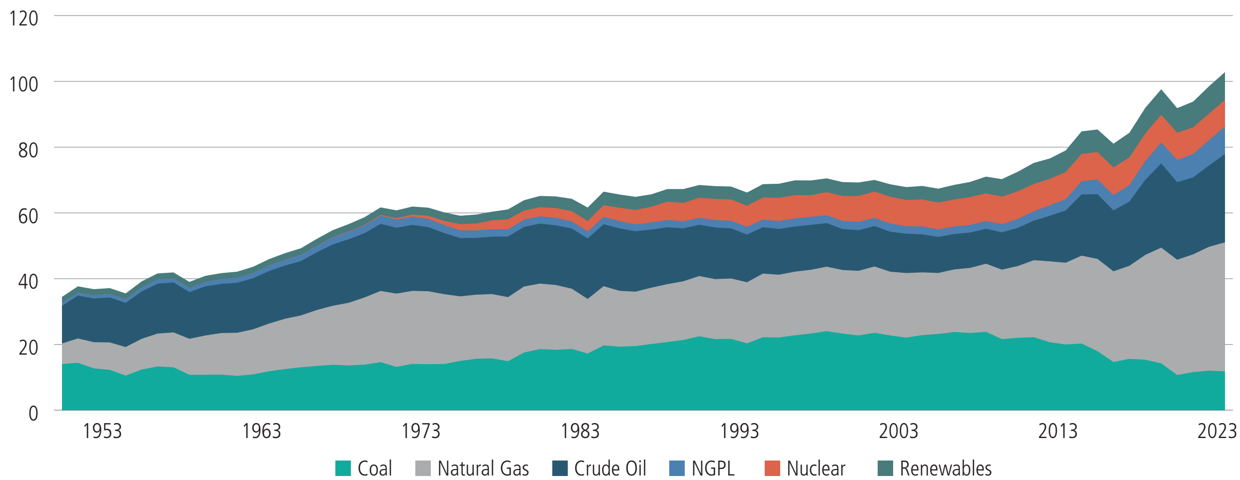
President Joe Biden began his four-year term with a flurry of actions reversing Trump executive orders, including reentering the Paris Agreement on climate and revoking approval of the Keystone XL pipeline between western Canada and Nebraska. Since then, he has generally aligned with climate advocates and conservationists, stiffening clean-air goals for automobiles, blocking exploration in parts of Alaska, and delaying new leases in the Gulf of Mexico, even while making select moves favoring oil and gas companies, such as approving Conoco's Willow oil project in Alaska. He also paused permitting for new liquefied natural gas (LNG) export projects, a measure that was reversed by a federal judge and remains subject to litigation.

Perhaps more telling than Biden's limitations on fossil fuels has been his support of renewable energy, reflected in key legislation during his term—most notably the 2022 Inflation Reduction Act, which provided hundreds of billions of dollars in tax subsidies and grants for low-carbon energy projects, supply chains, electric car purchases and more. In our view, this legislation could serve as a clean energy investment catalyst for many years to come.

Overall, a combination of resilient economies and technology-driven needs for power has helped to maximize the growth of the energy sector across all categories, with record production of oil, natural gas and alternative fuels alike.

U.S. ENERGY PRODUCTION: 'ALL OF THE ABOVE'

U.S. primary energy production by major sources, quadrillion British thermal units



Data source: U.S. Energy Information Administration, data through 2023. NGPL refers to natural gas pipelines.

Broad Expectations

Looking ahead, it appears easy to create initial profiles of the Democratic and Republican presidential tickets. With Kamala Harris, many anticipate a continuation of pro-clean energy policies—including support for renewables, maintaining fuel efficiency requirements and preserving environmental regulations around oil and gas production and related emissions. With Donald Trump, the emphasis would likely be on domestic energy production ("Drill, baby, drill") through a friendlier permitting application process and reduced red tape.

Although political promises are often unreliable, in her 2020 presidential election bid, Harris took various policy positions that went beyond even the current administration—including outright opposition to fracking, a stance that she has already walked back. She advocated building a clean economy by 2045, with 100% carbon-neutral electricity by 2030. And with a focus on environmental justice, she supported climate pollution fees on companies and the implementation of "equity scores" as part of the energy approval process. As a senator, Harris was a co-sponsor of the failed Green New Deal in 2020, and before that, as California attorney general, she was active in litigating against energy companies on environmental issues.

Trump, meanwhile, has always emphasized energy security and "dominance" through fossil fuels. The U.S. became the world's largest oil producer in 2018, a status maintained ever since. As mentioned, Trump could roll back IRA subsidies for electric vehicles and renewable energy, while likely trying to accelerate energy infrastructure approvals and level the playing field for internal-combustion gas-powered vehicles. Under a second Trump administration, U.S. membership in the Paris Agreement could lapse once again.

Clean Energy: Perception vs. Reality

Nevertheless, it's important not to overly discount the impacts of these high-level positions, particularly when considering the structural realities of the political and energy landscapes.

In our view, clean energy has become more cost-competitive in recent years, making up a growing portion of the fuel mix needed to run the U.S. economy while also lowering greenhouse gas emissions. Moreover, given the country's decentralized system of government, many of the decisions around energy are actually made by states—somewhat limiting the impact of whoever sits in the White House. Finally, it's hard to put the legislative genie back in the bottle. The process of applications for green-energy projects is already underway, with an estimated $369 billion earmarked[1]—and much of that in Republican-dominated states. Pulling back those dollars may be politically difficult given job creation and tax benefits at the local level.

Then there is market demand. Energy demand has been steadily rising across the economy, we believe particularly due to the acceleration of power-intensive artificial intelligence and onshoring of manufacturing. Continuation of these trends will likely require a significant increase in energy supply, of which a portion could be addressed through cleaner resources such as wind and solar power. However, given their intermittent nature (the wind doesn't always blow, and the sun doesn't always shine), these resources do not provide the baseload capacity needed to maintain a reliable electrical grid. Hydropower can help to a limited degree, and while existing nuclear generation is a reliable zero-carbon resource, new plants will be very costly and take years to complete. Higher carbon-emitting coal continues to be retired, while oil is not generally used for electric power needs. Practically speaking, this leaves relatively clean-burning natural gas, which we think will remain a key component of the energy picture for many years to come, regardless of who wins the election.

The case for an "all-of-the-above" approach also comes from the consumer, whether corporate or individual. Many companies are facing pressure from stakeholders to reduce carbon emissions, so they are likely to favor drawing on a range of fuels to help make that happen. Some mega-operators of data centers have even looked to locate near clean energy sources to limit reliance on fossil fuels and an overtaxed electrical grid. Meanwhile, with continued coal plant retirements and potential grid reliability challenges, it makes sense not to put all the energy "eggs in one basket." Even traditional sources carry risks—remember the freezing of Texas pipelines in 2021 and the historical oil spills in the Gulf of Mexico and California waters. The importance of reliable power will likely lead local and national politicians to keep the lights on through a mix of fuel sources that provide the best combination of dependability, lower emissions and cost effectiveness.

For renewable energy suppliers, while headline risk around policy remains an issue—particularly relating to the fate of IRA stimulus—outcomes are likely to be more nuanced and driven by market demand. Aside from periods of economic softness, long-term global fuel demand should remain strong, supporting the bottom line for a range of providers. Further, given the upward inflection in power demand and broad electrification tailwinds, we will likely need all the energy we can get to electrify the future, with the most dominant sources being natural gas, renewables and nuclear.

Oil & Gas: Supply, Demand and Geopolitics

On the traditional fuel side, we would warn that increased output alone would not necessarily benefit energy companies or their investors.

Although it may be counterintuitive, we believe higher hurdles imposed by greater regulation can help limit excess drilling activity, reducing the risk of potential supply gluts that have often derailed oil and gas investors. Over the past few years, a combination of such limitations, along with greater capital discipline (companies not growing for growth's sake) and operational efficiency gains, has helped improve profits at many energy companies. In short, while companies prefer less regulation, most producers have moved away from the "drill, baby, drill" mantra, instead choosing to focus on free-cash-flow generation and higher dividends to shareholders. In our view, the investment community does not want to see a reversal of this strategy, no matter who holds office.

[1] Source: U.S. Treasury.

Moreover, demand will naturally play a significant part in fossil fuel prices in addition to supply trends. We know a Harris administration would continue to support the energy transition, which, in the long run, would likely reduce demand for traditional energy. Trump's impact on demand would be more complex. Some are concerned that tariffs and trade wars would weigh on global growth, while, conversely, lower taxes and other pro-growth policies could more than offset such issues. Trump's policies could delay the energy transition, boosting medium- and long-term demand for traditional energy.

Geopolitics are also a critical factor. As we write this *Insights*, tension in the Middle East remains elevated—a potential support for oil prices should it lead to curtailed output from Iran (where exports are currently about 1.5% of global output[2]) or elsewhere in the region. Further, Iran's volume could be at risk should a Trump administration re-enforce more stringent sanctions on the country, with the same issue potentially applying to Venezuela's oil output, but on a smaller scale.

Supply disruptions are a concern for the market, although right now the Saudis and other OPEC members have spare capacity that could help offset a supply shock. While tapping this idle production could help limit near-term volatility, we think reductions in spare capacity are supportive of pricing in the longer term given less room for further outages. Separately, OPEC activity will continue to be closely monitored as Trump is known to have a friendlier relationship with the Saudis and could encourage them to cooperate in limiting oil prices to fight inflation. We note that while Trump wants a strong energy sector, he will still be cognizant of prices at the pump, suggesting a delicate balance between the two.

Ultimately, while policies can have an impact, we believe oil and natural gas prices are key drivers of activity levels. At oil prices of above $70 and natural gas prices around $3 per thousand cubic feet, we believe U.S. production is likely to continue growing in the near and even medium term (albeit at a more modest pace as drilling inventory depletes) regardless of whether a Democrat or Republican is in the White House (assuming that Harris's policy will be a continuation of Biden's). That said, it bears remembering that the current supply of U.S. oil and natural gas is not limitless, and volume growth from the Permian Basin in West Texas and other shale basins will likely slow over time. A drilling-friendly administration might soften that trend by allowing more frontier exploration (deepwater, Alaska, Arctic), but these are all longer-cycle projects that are difficult to commit to, given the often-changing political winds in Washington, D.C.

Conclusion: Predictable Uncertainty

Despite the temptation to categorize politicians in familiar buckets, their ultimate impact can be difficult to anticipate. There is often much more than meets the eye. For instance, both parties have a history of environmental stewardship. In fact, the Environmental Protection Agency (EPA) was established during the Nixon administration, while the initial wind and solar investment tax credits were instituted under Republican Presidents George H.W. Bush and George W. Bush, respectively. In addition, it has been under the Biden administration that oil and gas production has continued to grow to record levels, despite massive spending to build out clean energy resources.

This is not to say that the broad characterizations of Trump and Harris—as more or less friendly, respectively, around fossil fuels—are not correct. But their potential impacts could be anything but predictable, and may depend on events far beyond their control—whether recession, geopolitical conflict, grid reliability or technological advances.

As we move closer to the election, news flows around the IRA and policy are likely to increase volatility in energy names, just as they may for the broader market. Depending on the results of the presidential and Congressional contests, we could also see a surge in the share prices of companies associated with one side or the other. However, we believe the real test will not occur this year, but rather further down the road as legislative and regulatory direction becomes clearer and interacts with broader trends affecting the global economy.

[2] Source: IEA Oil Market Report, July 2024.

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