

News – Opinion

## **Greenhouse cost equation gets compelling**

Frank Jotzo

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*To make progress towards a 'new Kyoto', Australia must first ratify the old one, writes Frank Jotzo.*

The tide is turning on climate policy. This week's Energy Futures Forum report confirms the key findings of the Stern review, in the Australian context: the benefits from reducing climate change risks far outweigh the costs of cutting greenhouse gas emissions.

This is remarkable, coming in a report prepared by CSIRO, using modelling by the Australian Bureau of Agricultural and Resource Economics, and with some of Australia's largest energy companies involved, alongside non-government organisations. And it comes on the heels of the nuclear taskforce saying that nuclear power can be viable only if carbon emissions are priced.

The pressure for meaningful greenhouse policy is rising.

Economic cost estimates for Australia of significant global emissions reductions are moderate. In the report's main scenarios, they are in the range of 2 to 3 per cent of GDP at 2050, or around 0.05 per cent lower average annual growth. The figure of a 10 per cent GDP loss, often quoted and misused, is also there, but it derives from an unrealistic modelling scenario where Australia implements a carbon tax eight times higher than the rest of the world. Mainstream international analyses show costs in a range around 1 per cent of global GDP, as reflected by the Stern review.

These new studies price the economic damages from climate change, including the risk of abrupt non-linear change. The numbers are debatable, but the core argument is solid: the future costs of doing too little now could be huge. Australia is vulnerable, not least because the south-east could get permanently drier.

What to do? Prime Minister John Howard, in his recent speech to the Business Council of Australia, announced a taskforce on emissions trading, but again ruled out ratifying the Kyoto Protocol, vowed to protect Australia's natural advantage in fossil fuels, and reiterated the need to involve all major emitters in an international system. The UN Framework Convention on Climate Change, ratified by Australia as well as the US, calls for the developed countries to take the lead in cutting emissions, with the expectation that poorer countries like China and India will follow. Kyoto is only a first step, and negotiations are under way on post-2012 commitments.

The Kyoto approach has its shortcomings, perhaps chief among them uncertainty about the future cost of complying with any given target. But political realities clearly favour cap-and-trade over taxes for greenhouse gas control, and it can be made more

flexible through GDP-linked targets, opt-out provisions, sector targets, a permit price cap, and even links to commitments for technology investment.

Australia as a non-ratifier is now excluded from main UN negotiations, as are the US and some 30 mostly small developing countries. Australia could help push for a post-Kyoto framework with maximum flexibility, just like it did in the 1990s to help bring emissions trading into the Kyoto Protocol. But to regain influence and to shed perceptions of being merely obstructionist, Australia must ratify.

Ratification would come at no or low net cost for Australia. Overall Australian greenhouse gas emissions are only a little above 1990 levels, even though emissions from energy are already up 35 per cent on 1990. That is thanks to a slowdown in emissions from land clearing in Queensland, included in Kyoto accounting on Australia's insistence.

Challenges to Australia's energy industries arise more from importers than domestic policies. Australia's main export destinations are under growing pressure to limit their emissions, and substituting away from coal is an obvious response.

Coal has a future only if carbon dioxide can be captured and stored at low cost. To get there, substantial R&D is needed, as well as a price signal to drive adoption of new technology. Uranium and renewable energy by contrast stand to gain in a carbon-constrained world, and Australia has great potential for both.

Energy-intensive industries like aluminium will feel the pinch of domestic carbon pricing, but the threat of massive industrial migration to developing countries is unlikely to materialise if there is an expectation of future carbon constraints there also. A significant price on carbon in most of the world is all but unavoidable further down the track. Industry needs early signals about future policy settings, and Australian companies are well advised not to expect the current policy of no carbon constraints or pricing to last.

Ratifying Kyoto would regain Australia's seat at the negotiating table, immediately establish a modest price signal, and link Australia to emerging global carbon markets. A stitch in time of this sort would be a good thing for the economy.

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