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The New Green Agenda – Politics running ahead of Policies

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Politicians seem to be outdoing themselves in the bid to appear “greener than thou”. The Labour Government has set a target of a 60% reduction in CO_2 emissions by 2050 and is proposing to make it binding, with five year “carbon budgets” set for at least 15 years ahead; the main proposals are likely to go ahead as the Conservative and Liberal parties only want to go further – a more than 60% reduction by 2050, with annual targets. Similarly, the EU summit recently agreed binding targets of a 20% share for renewables in EU energy consumption, and a 20% reduction in EU greenhouse gas emissions by 2020 – more, if other countries follow suit. Even the US is joining in – the US Energy Secretary has said that climate change is now one of Washington’s top priorities in the energy field, and the US plans to reduce gasoline consumption by 20% over the next decade (for energy security as well as environmental reasons), mainly by increased use of biofuels.

This new greenery certainly represents a significant change in the terms of the political debate, and no doubt responds to the recent rash of expert warnings – for instance from the Intergovernmental Panel on Climate Change which concluded in early February that the evidence for global warming is “unequivocal”, and in the Stern Report published at the end of last year, which suggested that early action to combat climate change would make economic as well as environmental sense.

Targets not measures

But what the announcements have in common is that they are more about targets than about policies and measures; more about commitments than action. The question of whether and how these targets can be delivered is largely ignored. In its *Climate Change Strategic Framework* published on 13 March, for instance, the UK’s DEFRA says “we have a good understanding of the policies that will be needed”; the EU has made similar comments.

But this assumption deserves a little more thought – if in fact governments do not have the means to deliver quantified emissions reductions (or do not have the will to implement the policies which would be required) these targets are largely meaningless, or could lead to serious economic distortions. Experience with the many missed policy targets over the past decade of Labour government should breed a certain caution.

The Bank of England Model

The UK Government appears to be trying to get round this problem by using the targets as a way of stiffening its will (or, more accurately, its successors' will). It is proposing to do this in two ways: by making the targets "binding" (see below) and by introducing an independent element into the process – a *Committee on Climate Change*, which will recommend and report to Parliament on the establishment and achievement of five year carbon budgets. The apparent model is the Bank of England Monetary Policy Committee, set up shortly after the Labour Government came to power and which is generally agreed to have been a great success in controlling inflation.

But the parallel is not close:

- First, because inflation is essentially a monetary phenomenon. The Bank has the necessary instruments to influence monetary conditions, in the form of interest rates. By contrast, the proposed new Climate Change Committee will be advisory; policy instruments will remain in the hands of the Government.
- Second, because the timescales are different. Interest rates take time to work their way through the economy – up to two years – but do not depend on a wholesale replacement of the economy's capital stock. Carbon emissions do, however, depend on that capital stock. Capital items have a relatively short lifetime (eg light bulbs); some (eg cars) last for a decade or so; many of the most important (eg power stations and housing) have a lifetime in terms of many decades. One of the purposes of the new arrangements is "to provide the long term credibility required to stimulate investment in a low carbon economy" – a desirable objective, but difficult to implement in practice. It implies that investors will have a clear view of the level of activity in the economy decades ahead, of the carbon intensity required to meet the emissions target at that level of activity, and of the investment required now to comply with that level of carbon intensity. As an example of how difficult such forecasts are, one can look at the recent EU proposal, cited in the Climate Change Strategic Framework, that all new fossil fuel fired power stations built in the EU from 2020 should capture and store CO_2 "subject to developing the necessary technical, economic and regulatory framework to achieve this". In other words we will do it, if it still seems like a good idea at the time. Those familiar with California's Zero Emissions Vehicles programme which foundered on similar problems, must wonder how firm a basis for investment this is likely to be.
- Third, because the Bank's framework is in fact quite flexible. Its inflation target is 2% but the range is quite large (1-3%). Furthermore, the target can be changed and the Government recognises that the actual inflation rate will on occasions depart from the target because "any economy at some point can suffer from external events or temporary difficulties, often beyond its control" and that attempts to keep to the inflation target in these circumstances may cause "undesirable volatility in output". In other words, if the target has too much influence on the real economy it can be set aside - the only sanction is that the Bank has to send a letter to the Chancellor explaining what happened

and what is being done to put things right. By contrast, although there is some flexibility in the proposed carbon budgets, an intermediate target is fixed of 26 to 32% in 2020 (by comparison, the Bank's range of 1-3%, compounded over the period up to 2020, would give a range of 14 to 47%). The only basis for changing the 2020 and 2050 targets is a change in the science or international law or policy and, as discussed below, the targets are potentially legally enforceable.

- Fourth, because no fundamental contradiction is seen between the Bank's target and the Government's real economy objectives – specified as "to achieve high and stable levels of growth and employment". The framework for the Bank specifically calls low inflation a "precondition" for meeting these objectives. Climate change policies, even if they bring economic benefits in the long term as Stern suggests, are much more likely to come up against growth and employment objectives in the shorter term. Although the Government and the proposed Climate Change Committee are supposed to take account of the economic impact of their decisions, this does not allow them to change the 2020 or 2050 targets.

For all these reasons, the new system looks very different from the monetary framework.

Binding targets

Nor is it easy to see what exactly "binding" targets means in this context. The only clear obligation in the draft Bill published by the Government is on the Secretary of State to set targets and to "ensure" that they are met (subject to some flexibility, for instance in relation to carry-over between periods). Yet meeting the target is not ultimately a matter for the Secretary of State but for the many firms and individuals across the country. In some ways, the new obligation is like the objective, which once governed economic policy but has now been abandoned, of ensuring full employment - which depends on the actions of employers and employees. However, the new targets are set in statute: the Government would be open to Judicial Review if it failed to meet its emissions targets (or indeed if the carbon budgets it set looked inappropriate to some outside lobby). To some readers this might seem like a lawyers' charter – opening up endless scope for argument about whether a particular package of measures was indeed sufficient and necessary to keep the country on target. It also contains the scope for creating major economic distortion – if the only way of meeting the target is by some highly costly and damaging measure, the Government could apparently nonetheless still be required to introduce that measure. Compare that with the current renewables programme. Albeit on a much smaller scale of economic significance, this contains provisions limiting its potential impact on electricity prices. Yet the impact of the national emissions programme on growth and employment (the Government's primary economic objective) is not to be limited in this way.

The fundamental problem with delivering quantified emissions reductions is that there is no absolute way, at least in a non-command economy, of forecasting what the impact of any given policy will be on the level of emissions (or the economic impact of such a policy).

To give some idea of the inherent difficulty of meeting targets in this area, it is worth remembering that:

- The UK missed its 2000 renewables target and will almost certainly miss its 2010 target.
- The EU has also missed all its past renewables targets and will miss its 2010 target.
- The EU is not on track to meet its Kyoto target, according to most observers, including its own equivalent of the Climate Change Committee, the European Environmental Agency. Only two countries in the EU 15 are more or less on track to meet their individual targets – Sweden and the UK (and Sweden has a positive target, ie it is aiming at an increase of 4%).
- Kyoto countries as a group are even further away from meeting their targets – ie non-EU countries like Japan are even further away from compliance than the EU.
- While the UK should meet its Kyoto target, it is not on track to its own CO_2 target for 2010. It is only on track as regards Kyoto because of cuts in non CO_2 greenhouse gases and a decrease in CO_2 emissions which took place in the first part of the 1990s before the Labour Government came to power – CO_2 emissions have actually increased since 1997. The new target structure is solely concerned with CO_2.

In other words, it is clear from experience that governments do not have the policy tools they need to implement their climate change targets. Yet they are continuing to rely on essentially the same tools. In the case of the EU, the main measures are renewables and energy efficiency – as has been pointed out in previous comments (see *CO_2 emissions reduction: time for a reality check* from February 2005), these have not delivered as expected, and are unlikely to do so in future.

The UK Government puts more stress on emissions trading and one part of the new draft Bill is specifically concerned with trading. Trading has many attractions in theory, yet it remains to be fully proven in practice. The EU Emissions Trading Scheme is the pioneer in this area. While its current (first) phase is generally agreed to have been a success in practical terms, it has not been particularly effective in reducing emissions (one reason why the EU is not on track to its target). Allowances seem to have been set at too generous a level, producing considerable volatility but ultimately low carbon permit prices. Thus the scheme may have had a minor effect on fuel switching (and more on electricity prices) but has done little to stimulate investment in clean energy.

Whether the next phase of the scheme (2008-2012) is any more effective remains to be seen. It is noteworthy that every single EU country, in making its own proposals for the next phase, wanted an increase over 2005 levels of emissions. The Commission has cut back most of the bids, but this reluctance on the part of member states to make emissions reductions does not speak well for the collective will to achieve the new targets – there is clearly still a great deal of horse-trading to be done on the allocation of the EU's renewables and CO_2 emissions targets.

More widely, this experience suggests that one of the primary objectives of the new regime – to show leadership and act as a role model, encouraging other states to propose big reductions – may be a forlorn hope. The UK's new targets may simply undermine its own negotiating position in international fora.

Conclusion – delivery is what matters

The recent green tinge to policy making suggests a willingness on the part of politicians to face up to what scientists and other experts are telling them about climate change. However, as yet they have only addressed the relatively easy part – target-setting. If this is not backed up by effective policy-making, a gap will open up between the rhetoric and means of delivery. Politicians seem to be hoping that if the will is there, a way will be found. However, experience in this area casts considerable doubt on the realism of that position. It suggests that they should be focusing on delivery, not on targets, if they are genuinely serious about climate change.

See also *The European Union's new targets on emissions and renewables: pluses and minuses* OIES Energy Comment by David Buchan.