

Need to heed global forces

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New Zealand will get an emissions trading scheme later this year.

Legislation is required to establish the scheme and interested groups have been commenting on the draft law.

Some, e.g. business groups like Business NZ, support having a trading scheme (but we think this year is too soon and would make our energy too expensive - we should only do it when countries with whom we compete do it too).

Others, e.g. environmental groups, don't worry so much about high energy prices as long as the scheme will strictly reduce New Zealand emissions.

The debate's so technical, probably everyone else has stopped listening – a danger, because it will have real price consequences in the near future.

To help shed some light, I would like to focus on just one aspect of the proposed scheme – the 'cap'.

Emissions trading schemes are often called cap and trade. The 'trade' is in carbon credits that can be bought to offset carbon emissions. The 'cap' is the maximum allowable emissions decided for a company, sector or country.

A key criticism made last week by Greenpeace was that our proposed scheme doesn't have a national cap (national maximum allowable emissions).

Without a national cap, Greenpeace argues, there won't be a firm incentive on New Zealanders to reduce their emissions – we will just keep increasing emissions as our economy grows, and buy carbon credits from overseas to offset them.

The sensible argument against this is that nobody wants to pay good money for carbon credits, so there will actually be quite a strong incentive to reduce emissions.

I believe the Government is right to not include a national cap in the proposed legislation.

A national cap would be a "Fortress New Zealand" way of dealing with climate change. It would mean that New Zealand couldn't buy credits overseas to offset emissions.

New Zealand businesses could only trade credits with other New Zealand firms, with New Zealand overall strictly limited to emission levels as determined by the cap.

On the positive side it would mean we could be absolutely certain that New Zealand's emissions were reducing.

But we could also be certain that our economy would reduce too.

It would mean that our best and fastest-growing companies would not be able to expand beyond a certain point.

Once their emissions got beyond the point where they could be offset by the relatively few New Zealand carbon credits available, they would not be allowed to buy more from other countries.

They would be constrained to be small or medium sized forever, unable to get beyond the size threshold needed to become exporters to the world.

That would be the terrible consequence of having a national cap - a 'fortress New Zealand' of small and dying companies, with New Zealand living standards steadily declining.

A national cap on our emissions would make no difference to world climate change anyway since New Zealand contributes less than 0.2% of the world's emissions (this is not an argument for doing nothing – New Zealand still has to be part of the solution).

Climate change, after all, is a global problem. It requires global solutions. Logically this should include global trade in carbon credits.

A major feature of today's global trade is efficiency. With instant communications and electronic funds transfer, major amounts of capital can be and are rapidly moved anywhere in the world - towards efficient producers and away from inefficient ones.

This competitive phenomenon produces ongoing quality improvement and innovation and keeps prices down.

This is positive. We want to see industries that use energy efficiently get larger at the expense of industries that use energy inefficiently.

Many of New Zealand's large energy users are the most efficient in the world – our dairy processors, aluminium smelters, pulp and paper producers and so on.

They are global players that earn valuable export earnings for New Zealand and give us a first world standard of living.

Yes, they use energy and create emissions – it would be impossible for them to do otherwise. But the important point is that they use energy efficiently. That is one of the reasons why they can compete successfully against competitors who use energy wastefully.

Because they are efficient producers, there will be less global damage from increasing their output than if others increased their (inefficient) output.

A national cap would hogtie these efficient producers, to the detriment of energy efficiency overall.

Of course, everyone, including companies that are large energy users, should reduce emissions over time – we are all agreed on that.

So the idea of using less energy *and* using it more efficiently has been captured in the Government's proposed emissions trading legislation and Business NZ supports this principle.

It makes the best use of global competitive forces.

But to be consistent the Government should drop its plan to rush in the scheme ahead of other competitor countries and should make more use of emissions intensity measures to make sure our efficient energy users are not disadvantaged against inefficient users elsewhere in the world.

Moving too soon will increase our energy costs sooner than in other countries and result in those same global competitive forces biting value out of the New Zealand economy, with negative impacts on New Zealand companies and the communities they serve.

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