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Carbon package moving in the right direction

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*The carbon package is a good start on a bigger challenge, writes **Tony Wood**.*

The long-awaited climate-change package is a step in the right direction as it provides considerable certainty to business and the public and creates a framework on which to build. This framework will be critical for Australia to become a low-carbon economy in the coming decades.

While the details need to be examined closely to determine whether the government has got the economic and environmental balance right, we can say the following things.

First, on balance the package is not a job killer. We live in a dynamic economy where jobs are constantly being created and lost. Overall, the package is unlikely to change total unemployment.

Second, the sky is not going to fall on households. Average incomes will continue to rise and jobs will be created. The impact of this package will be less than that of other increases in energy costs unrelated to climate change.

Third, the sky will not fall for business, either. With this package it is very unlikely that Australian industry will move overseas.

The package has made a good start on satisfying industry's demand for policy certainty. The initial carbon price of \$23 a tonne sets the scene. The combination of a price floor and cap when the fixed price is removed provides further comfort against price shocks.

In the short term, limitations on access to international permits or credits are a relatively small price to pay for market stability.

Finally, locking the forward cap at the bipartisan target of 5 per cent by 2020 provides some certainty for the environment.

Of concern is the decision to pay brown-coal electricity generators and their financiers for early shutdown of coal-fired plants and to provide free permits to some other generators. This does nothing for the environment and is bad for taxpayers. Over time, high-emission generators would almost certainly have shut down anyway, driven by rising costs under a carbon price.

Given the successful operation of the Australian electricity market over several decades, electricity shortages from the package would have been most unlikely.

Putting a price on carbon will reduce the value of emissions-intensive assets, particularly fossil-fuel generators. However, there is no principle that governments should compensate companies whenever the rules are changed.

Changes in environmental and social standards over several centuries, for example with asbestos or cigarettes, would also suggest that arguments about sovereign risk, demands for direct compensation or threats to supply security should all have fallen on deaf ears.

While the renewable energy initiatives in the package require closer study, there are good reasons to provide additional support for low-emission, developing technologies. However, the success of the new Australian Renewable Energy Agency will depend on it using more of its \$3.2 billion of funding for market-based approaches rather than the grant tender schemes that dominated past funding programs.

The creation of the Clean Energy Finance Corporation will provide more flexibility in clean energy funding, although details are unclear. The exclusion of carbon capture and storage from this funding is disappointing.

Finally, the carbon price package shows signs of repeating mistakes in the carbon pollution reduction scheme by compensating emissions- intensive, trade-exposed industries.

Grattan Institute's April 2010 report, *Restructuring the Australian Economy to Emit Less Carbon*, found that much of the protection proposed for these industries is unnecessary or poorly targeted. Free permits are justified only when a carbon price would force industry overseas without reducing greenhouse gas emissions.

In this regard, compensation is based more on the loudest voice than clear analysis. So the Productivity Commission's review will be critical in ensuring these problems are not permanent.

There will be winners and losers and there will be growing pains. You don't have to be a genius to predict where the loudest cries and complaints will come from in the days ahead. But the government's package has made a solid start on a long journey for Australia to play its part to address climate change.

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