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## **CEPR-RIETI Symposium “Changing Course: Multilateral Cooperation toward Green Growth and Digital Transformation”**

### **Session 1: Green Growth**

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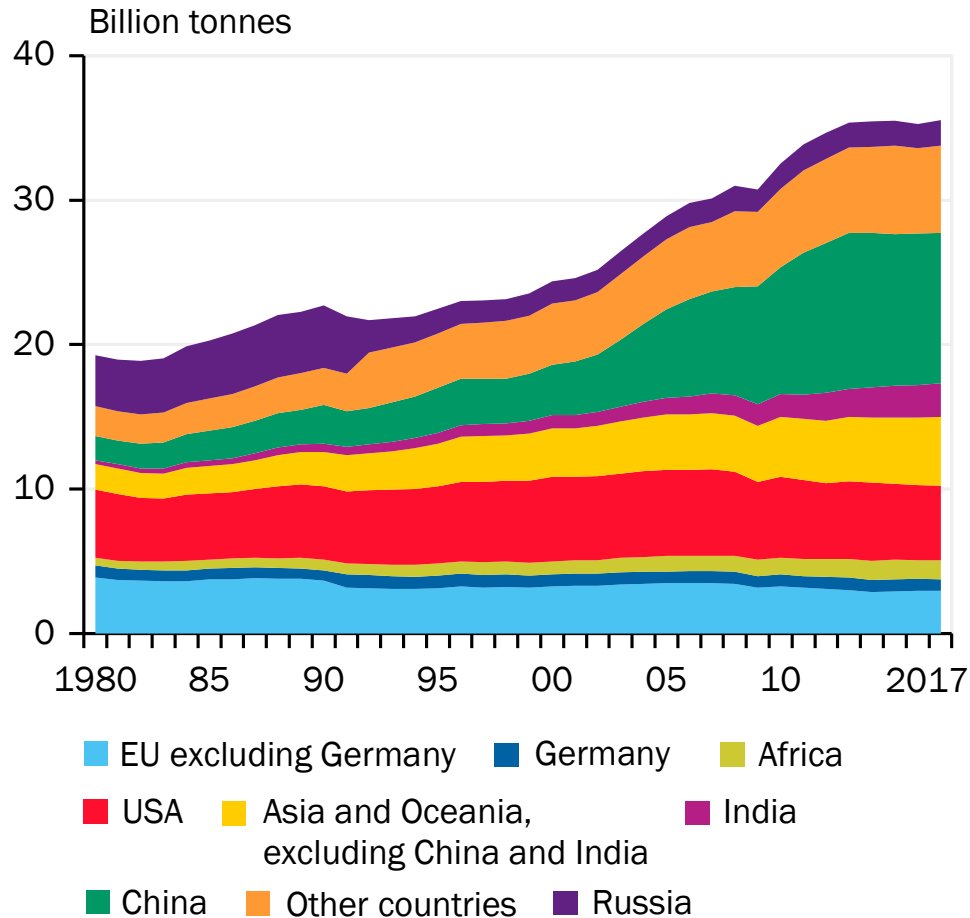
**Video conference, 2<sup>nd</sup> March 2021**

# **Rational EU climate policy**

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# The case for uniform carbon pricing

CO<sub>2</sub> emissions in selected countries and country groups



Sources: EIA, own calculations

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Curbing climate change requires drastically reduced global climate gas emissions.

The EU, and not the (sub-)national level is the appropriate level for climate policy: principle of division of labor ...

Ultimately, all efforts must feed into a global approach to fight global warming: protecting a global public good ...

Strong arguments for uniform carbon pricing.

# Uniform carbon pricing: rationale and implications

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## Uniform carbon pricing: rationale

- Principle of division of labor: prices as coordination signals
- Entering uncharted territory: choices reveal marginal cost

## Important implications:

- A plethora of (sectoral) targets is counterproductive: “(non-)ETS”
- Arrangements for burden sharing are indispensable.

## Implementing carbon prices: EU

- Augmenting the EU ETS to integrate the non-EU-ETS sectors
- Setting a price floor, reforming energy taxes & surcharges

## Managing the transition:

- Avoiding a disruptive regime change is sensible, but costly.
- Translating climate policy ambition into a shadow price of carbon.

# The European Green Deal

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# The political economy of uniform carbon pricing

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Effectiveness & efficiency are indispensable, but not enough: three additional challenges arise at different levels of responsibility

- Alleviating regressivity: a national prerogative and responsibility
  - prices as messengers, not causes of regressivity
- Preserving competitiveness (avoiding carbon leakage): EU responsibility
  - prices and shadow prices
- Providing incentives to other countries: EU as promoter or pioneer?
  - limited contribution to global emissions, EU is energy importer (**H2 strategy**)

All these issues become more pressing w/ higher climate ambitions

# EU Green Deal: Great Ambitions

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Important repercussions for medium-term ambitions

- vision: more carbon pricing, carbon border adjustment, research funding

Intention to eventually widen the scope of the EU-ETS

- prices would have to rise steeply

Proceeding separately in non-ETS sectors is now much more costly

- faster integration of EU-ETS required

Necessary for policy makers to emphasize their determination

- publishing shadow prices of carbon, earmarking revenues

Increasing carbon prices will harm competitiveness (“carbon leakage”)

- solution of free allocation of certificates will wane w/ increasing prices
- yet outsourcing decisions will be difficult to reverse

# Preventing carbon leakage

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# Border carbon adjustments: rationale and implications

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A promising alternative: border carbon adjustment (BCA)

W/ perfect information: avoiding distorted international competition

- resembling a VAT; the EU would forfeit control over carbon emissions
- limiting the BCA to imports could entail a loss of competitiveness
- dilemma would be mitigated in a global alliance on carbon pricing

EU Council has announced a BCA as a source of revenue for the EU budget

- potentially conflicting w/ strategic nature of climate policy

Technical, regulatory and legal challenges will have to be mastered

- measuring the carbon content (throughout the complete value chain)
- advisable to focus initially on energy-intensive and highly tradable goods

# Via Preparation for a BCA Towards a Carbon Club

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Which exporting (into the EU) countries will be subject to the BCA, what qualifies as “equivalent” climate policy?

- shadow carbon prices of similar magnitude as in the EU (difficult to estimate)
- motivating the BCA as a device to ascertain competitiveness would be unfortunate

Irrespective of this communication, other countries might interpret a unilaterally implemented BCA as protectionist

- take advantage of the tailwind created by new administration of US-President Biden

The BCA should only be considered after establishing a clear and credible uniform carbon pricing mechanism

- key to providing incentives to other countries to join an alliance for carbon pricing