Macro*Plus*
Comment

A changing climate

- *Climate change policy was pushed into the background by the global financial crisis*
- *As the post-crisis situation improves environmental issues are returning to the fore*
- *A slew of initiatives emerged in 2014, notably the US-China deal*
- *Perhaps more significant, however, is the burgeoning number of private sector proposals*
- *Possibilities of a low-carbon transition stranding fossil fuel reserves are increasing*

Back on the agenda

The GFC stalled efforts to tackle climate change

Following the UN climate change conference in 2009 – and the failure to reach a widely expected global deal – it appeared that efforts to tackle climate change had stalled. In retrospect, limited progress in Copenhagen was perhaps unsurprising, given the scale of the Global Financial Crisis (GFC): it was not only climate change policies that were pushed to the background by the sizeable efforts required to rescue individual economies and indeed the world financial system.

But six years on progress is reviving

Six years on, progress on climate change is reviving. In part this no doubt reflects the abating of the crisis. But a slew of initiatives in 2014, across a number of areas, suggests that the issue is returning to the fore: action is both broadening and deepening.

Policy momentum

2014 saw a slew of initiatives …

The sheer number and range of developments relating to climate change last year was remarkable. Most widely lauded, and most notable, was the US-China deal: it is action from the world's largest emitters that will define global outcomes. After years of disagreement it appears that the two countries will now work together and endeavour not to undercut each other's efforts. Moreover, China has finally acknowledged that 'developing countries' will have to contribute in some way to global emissions reductions.

In addition to this landmark deal, there were many other important announcements and actions, across all regions, in 2014. Taken together, the message is that climate change policy is evolving in such a way as to be more geographically diffuse and more enlightened. Consider:[1]

… across all regions

- **Asia.** China announced that its CO_2 emissions are to peak by 2030 or so, and its non-fossil-fuel share of all energy will rise to around one-fifth. All seven pilot Emission Trading Systems (ETS) are now up and running; Malaysia released a draft energy efficiency action plan; South Korea confirmed the cap and start date for their ETS – becoming the world's second largest after the EU; and Vietnam revised its environmental protection law to add articles on climate change.
- **Europe.** The EU has agreed to reduce emissions by at least two-fifths by 2030. Within the EU, a number of countries have introduced, or are in the process of introducing, new laws: Denmark adopted a climate act, and Finland also approved one. Both include legally binding targets. France has a climate bill passing through its parliament. In the UK, the Bank of England wrote to insurers asking whether climate change might affect the viability of their business models. In light of initial discussions the BoE plans to widen and deepen its inquiry.
- **North America.** The US President announced new targets to cut greenhouse gas emissions, and the EPA set new standards to cut power plant CO_2 emissions; California and Quebec linked their ETSs[2]; Rhode Island passed a climate change act with a legislative target for 2050.
- **Latin America.** Chile announced that the power sector will be taxed on its CO_2 emissions from 2017, the first country in Latin America to do so; and Mexico set new renewable and clean-tech electricity generation targets.
- **Australasia.** Australia, one of the few countries to move in the opposite direction, has repealed its carbon tax. Nevertheless, the government has passed into law a Direct Action plan that pays polluters to reduce emissions.
- **Africa.** Egypt has announced that it will transform El Gouna city into the first carbon-neutral city in Africa, with assistance from Italy; Rwanda officially launched its climate action fund, which in part aims at spurring green growth; and Morocco passed a national charter for the environment and sustainable development.

Better together

Joint initiatives are gathering pace

Furthermore, a number of joint initiatives made progress last year. These included:

- The UNFCCC which made steps in Lima, including agreement that a global deal would apply to all parties and not just developed countries. The hard issue, however, the respective contributions from developed and developing countries, remains to be addressed fully. This could prove the biggest hurdle to reaching agreement in Paris this year.
- The Green Climate Fund receiving pledges from 27 countries totalling \$10bn, including \$3bn from the US, \$1.5bn from Japan, and around \$1bn from each of Germany, France, and the UK. The mobilising of adequate climate financing for developing nations will, in addition to major emitters' commitments, also be central to securing an international deal in Paris.
- The G20 announcing an action plan for energy efficiency. The group also reaffirmed their commitment to rationalise and phase out inefficient fossil fuel subsidies. Certainly, lower oil prices afford countries scope to cut fuel subsidies: India is doing so, and Indonesia has followed suit. If oil prices remain weak, other structural reforms may follow, including the broader introduction of carbon taxes. Calls for such measures have already started, including by former US Treasury Secretary Lawrence Summers.

The divestment rush

Funds are divesting from fossil fuels …

What is perhaps more important than evolving, national and international, public policy is that unilateral action is now increasingly taking place in the private sector. One area that gained particular momentum last year is the disassociation of investment funds from fossil-fuel-related assets. Some of the more notable announcements:

- Stanford University is selling its shares in coal mining companies held by its multi-billion dollar endowment fund. The Rockefeller Brothers' Fund is to sell its investments in the coal and Canadian oil sands industries, and review its remaining fossil fuel holdings for possible sale in one to two years. The University of Glasgow is to sell holdings in fossil fuel companies. Australia's Local Government Super (LGS) pension fund has said it will negatively screen high carbon activities. KLP, Norway's largest pension fund, is to downsize its interests in coal companies and plans to boost its investment in renewables.

… as are cities and municipalities

Meanwhile, the growing number of cities committed to some fossil fuel divestment includes:[3]

- US: Seattle; San Francisco; Portland; Santa Fe; Madison; Ithaca; Providence; Cambridge.
- Beyond the US: Oxford, England; Dunedin, New Zealand; Fremantle, Australia; Boxtel, The Netherlands; and Örebro, Sweden.

Reading the runes

A low-carbon transition could gather pace

The sum of these initiatives may be quantitatively insignificant in decarbonisation terms; taken together they will not limit climate change to 'safe' levels. Nevertheless, the direction is clear; and the consequences could be dramatic. Martin Wolf of the *Financial Times:*

> *" … it is always possible that humanity will wake up and make the needed investments in rapid change, driven by the magic of the market and technological innovation. If that happened, fossil fuel reserves would indeed be stranded. Investors beware: the risk of that cannot be zero."*[4]

Fossil fuel reserves may become stranded

Renewed efforts from governments, coupled with the changing approach of investors and the broader private sector, suggest that this possibility is becoming more likely.

'Watch fors'

Against this backdrop of announcements and actions, three further developments would be of particular significance were they to occur:

- First, environmental policy and investor sentiment increasingly moving against coal. Oil and gas may get caught up in the divestment crossfire, but probably not markedly so.
- Second, the widespread removal of fossil fuel subsidies, particularly if oil prices remain weak.
- Third, broader deployment of carbon-pricing policy using both taxes and emissions trading. 'Cap and trade' is likely to be preferred as ETSs can be linked across regions, lowering costs. ■

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Annex

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Endnotes

[1] See: Annex for details and hyperlinks.
[2] ETS is short for 'Emissions Trading System'.
[3] See: http://gofossilfree.org/commitments/.
[4] See: Wolf, M., 17 June 2014. *A climate fix would ruin investors*. The Financial Times. See: http://www.ft.com/cms/s/0/5a2356a4-f58e-11e3-afd3-00144feabdc0.html?siteedition=uk#axzz3Jb6DU1dX.