

THE TRANSFORMATION OF GLOBAL GOVERNANCE PROJECT

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THE GOVERNANCE OF CLIMATE CHANGE: MAKING IT WORK

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1. Climate change is the most pressing and challenging collective action issue. Climate change mitigation exhibits all the characteristics which ought to drive collective action. The preservation of the climate is a paradigmatic public good problem whose urgency is underscored by abundant and unequivocal scientific evidence. Climate is also a policy area where delays may lead to potentially irreversible damage. At the same time, it involves an unavoidable risk of free-riding on any solutions commonly agreed upon, as regards governments' willingness to enter into commitments to reducing carbon emission or in implementing these. Furthermore, climate change raises daunting intergenerational and international equity issues that are hard to solve in theory and even harder in practice. Any solution involves distributional choices along those two dimensions, and also raises in all countries further issues of distributional equity amongst living citizens.

The transition to a socially superior equilibrium therefore creates both winners and losers across generations, between countries and within countries. For these reasons collective action in the field of climate requires solving major problems of intertemporal choice, international coordination and distributional equity, as well as tackling enforcement challenges.

2. The global climate governance framework is not up to the task. At its centre sits the 2015 Paris Agreement on mitigating climate change, which de facto substituted the more coercive but far less comprehensive Kyoto Protocol of 1997. After having failed in 2009 to negotiate and implement binding targets for each and every country, the eventual agreement on a series of nationally determined, non-strictly binding objectives was and remains indicative that the international community has chosen breadth at the expense of depth. Yet, despite the fact that “the house is burning”, the sum of individual commitments by countries, local authorities, businesses and investors do not add up to the collective objective set by the Paris Agreement: limiting the average temperature increase to well below 2°C, aiming for 1.5°C.

The Paris agreement reflected a new reality and a recognition that emission reduction pledges could not be limited to the advanced countries, that the model of timetables and targets could no longer work, that national sovereignty could not be circumvented, and that agreements needed to represent the diversity of the multiple players involved. It was a watershed as it represented a shift from negotiated national commitments to coordinated unilateral pledges. In essence, it defines a process, a learning method, an enabling framework coupled with a peer review and an agreement to assess at regular intervals whether intentions and actual actions measure up to the commonly agreed overall goal.

It is meant to be a platform for accelerating climate action, a way to motivate countries — but also the many other actors of the climate regime, through a process of information exchange, of constant benchmarking and pressure, with the aim of aligning objectives as a substitute to a centralised governance mechanism. Its effectiveness however is yet to be ascertained; it has certainly been hamstrung by political shifts since 2015, most notably the US withdrawal from the Agreement. Nevertheless, commitments under the Agreement must be revised and increased by 2020, when it starts its effective implementation. The idea is to progressively internalise the long-term goal as net zero GHG emissions by 2050, making it become the new reference point for governments and other actors.

As things stand, the intended contributions registered under the Paris agreement are grossly out of line with its stated goal. Incentives to free-ride by under-pledging and under-delivering remain massive. Furthermore, climate coalitions are by nature unstable and leadership risks being ineffective as first-movers in the emissions reduction game end up having made themselves, by their very success, irrelevant for the next step of climate action. This best-performer curse is inherent to the problem at hand.

3. Departure from the simplistic one-agent, one-period model may lead to more optimism.

Climate change mitigation strategies cannot be assessed through simplistic lenses. To start with, states are not the only players. Cities and local governments are also involved, especially as greenhouse gas emissions and local pollution are often correlated. Several have started using the regulatory means at their disposal to foster speedier decarbonisation than envisaged by national governments. Second, private companies have incentives to engage in the development of low-carbon technologies because of the first-mover advantage that may result from early research and investment. Third, states themselves have reasons to encourage such investment because of the comparative advantage that may result from having been involved in the shaping of new technologies.

The important point here is that for those dynamic forces to be set in motion and strengthen the drive towards decarbonisation, it may not be necessary that international agreements be credible and deliver decarbonisation with a high probability. It is sufficient that they credibly set the course towards an irreversibly greener economy. This may be enough to change the nature of the game and make it possible that a soft agreement such as the Paris Agreement provides enough incentives to action to affect private behaviour significantly.

4. A widening gap between frontrunners and laggards raises concerns about the adequacy and the viability of the current framework. The Paris Agreement brings under the same umbrella front-runners (such as Scandinavian countries) actively engaged in the decarbonisation of their economy and laggards (such as Poland, the US or Gulf states), whose commitment to reducing emissions is at best shallow. The question is how long all of these can remain, nominally at least, part of the same endeavour. Front-runners are likely to be increasingly concerned that they are incurring the cost of climate action while others free-ride on their dedication while enjoying the benefits from lower production costs. Laggards meanwhile may feel that they are not part of the race for technology leadership and are unlikely to reap the benefits of investing into clean technology. The former may insist on more binding agreements or compensatory measures. The latter may fall further behind as following the lead is a challenge and there is little scope to expect being rewarded for one's effort.

This logic may result in an unstable bimodal distribution of efforts and outcome, with the consequence that an economically inefficient and politically toxic two-tier club structure may emerge. Solutions to such divergence may involve specific trade measures (such as adjustment taxes) and/or transfers on a wider scale than envisaged (and hardly implemented) thus far.

5. The plethora of available policy tools need to be harnessed to deliver the desired result. The climate governance challenge today is to create a collective action framework which amounts to more than the sum of its parts; to reconcile precise and binding global top-down goals with voluntary bottom-up contributions that do not add up to the stated goals - certainly not to the aspirational goal of capping temperature increase to 1.5°C or carbon neutrality by 2050.

Given the size of the task and the collective action challenge, this necessitates an approach which combines incentives for behavioural change (such as agreements to reduce emissions in particular sectors) with direct action (such as direct carbon capture). It is also an approach which needs to pay more attention to the problems that both consumers and producers are faced with in the transition period, and to issues of burden-sharing and fairness. Practically speaking, this may also imply segmentation as a future policy direction: breaking up problems into pieces and looking to create

agreements on smaller climate-related issues, as a complement to the global climate framework rather than a substitute.

A number of policy tools have been used for climate change mitigation: Pigouvian price-based such as carbon taxes; Coasean rights-based such as emission trading permits; regulatory, driving the adoption of cleaner technologies; and legal requirements, which have helped phase out harmful substances. These have all individually contributed to climate change mitigation but have not however created the critical mass required.

Part of the reason lies in the lack of political support for tools such as a global carbon tax or the coordinated phasing out of fossil fuel subsidies. Such support has been undermined by policy design not taking into account distributional effects or failing to include side payments (for example incremental costs to developing countries being borne by richer countries). More broadly, an impact assessment on the various policy tools is required; a broader view incorporating their macro (economic and social) impact, and their potential to help tip the incentives from the static costs to the dynamic benefits of shifting to clean technologies.

- 6. The climate emergency is also a unique investment challenge.** Seen in a dynamic setting however, a major policy challenge is to change business expectations concerning the future in order to generate a critical mass of investment in clean technology, renew the capital stock, accelerate the transition and turn the climate issue from a catastrophic vision to a solution for growth. This requires the transformation of private finance to support such investments (some of which is already taking place), coupled with large public investments in the same direction that act as demonstration effects and as incentives.

It is often hoped that a change in investors' attitude and the promotion of green finance will be key drivers of the transition to a carbon-neutral economy. Despite the certainty about the impact of climate change, however, there is a case of market failure combined with information failure when it comes to forward-looking investments: the existing uncertainty as well as the increasing returns involved in clean technology are bound to generate investment below what is socially optimal in the longer run.

- 7. Climate action must not be left to specialised bodies and institutions.** Governance at global level is mostly driven by states; and it is most successful when political support (expressed for example at G7 or G20 level) combines with existing multilateral institutions to generate cooperative behaviour and solutions. This is unfortunately not the case in climate governance at the moment: the most effective global institutions such as the IMF and the WTO are supportive of climate action but not actively engaged in promoting it.

There is by now a clear need to mainstream climate change mitigation, so that it is taken on board in policy design, policy coordination and policy surveillance. This should apply for example to public finances, tax policy, financial stability policies (where action has started already) and trade and investment policies, to mention key fields only.

Climate governance furthermore exhibits some promising characteristics. One is the already mentioned mobilizing role of sub- and supra-national entities (cities and regions); these cannot substitute for action at state level, but act as complements, generating pressure as well as a real contribution towards attaining climate goals. A second is the political pressure from grass roots movements. Both in the US and in Europe, civil society is making up for lack of leadership at political level; as a result, climate issues have risen in the political agenda. This may help generate the required ambition in the governance framework, with the danger however that whatever positive governance developments materialize are swamped by the extent of the climate problem.