Cooperation and emissions price harmonisation without linking: prospects for ‘climate teams’ in East Asia

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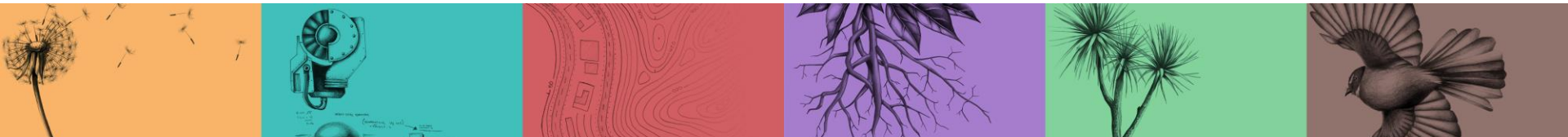
Small changes have been made to these slides based on feedback from workshop participants.



The challenge

Globally we need to get to net-zero long-lived gases

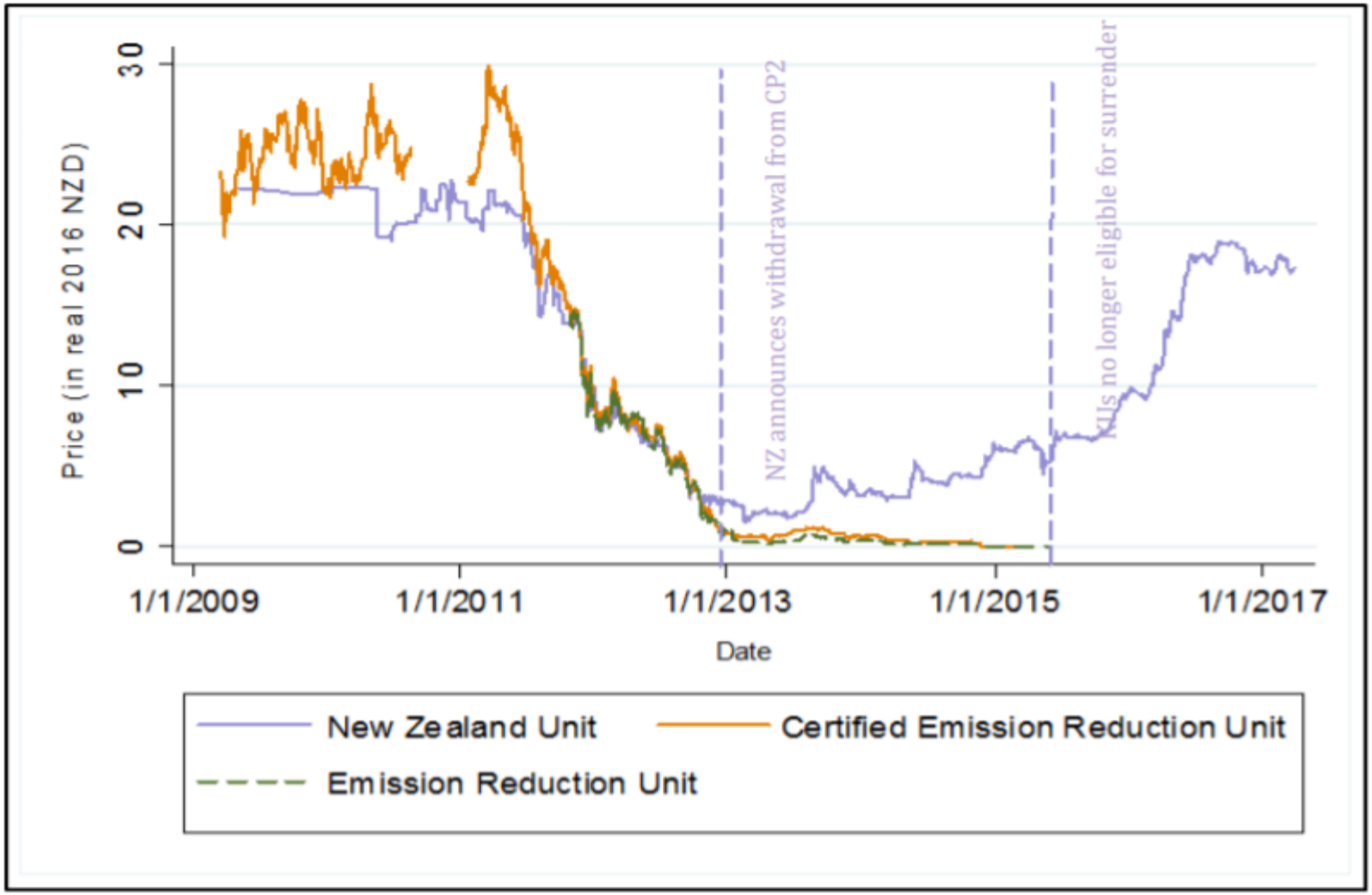
Mismatch between mitigation opportunities and resources to mitigate

Ideally, equalise marginal emission reduction costs across countries – now and across the investment horizon

But Nationally Determined Contributions reflect only domestic costs and willingness to pay (which depends on local benefits including those from altruism, from being seen to be cooperative, and from anticipation of reciprocal reductions by other countries)

Hosts - Low marginal costs:	Colombia, Thailand, Vietnam, …
Investors - High marginal costs:	New Zealand, Korea, Norway, Canada, Australia, USA …

ETS linking is risky – especially for the small

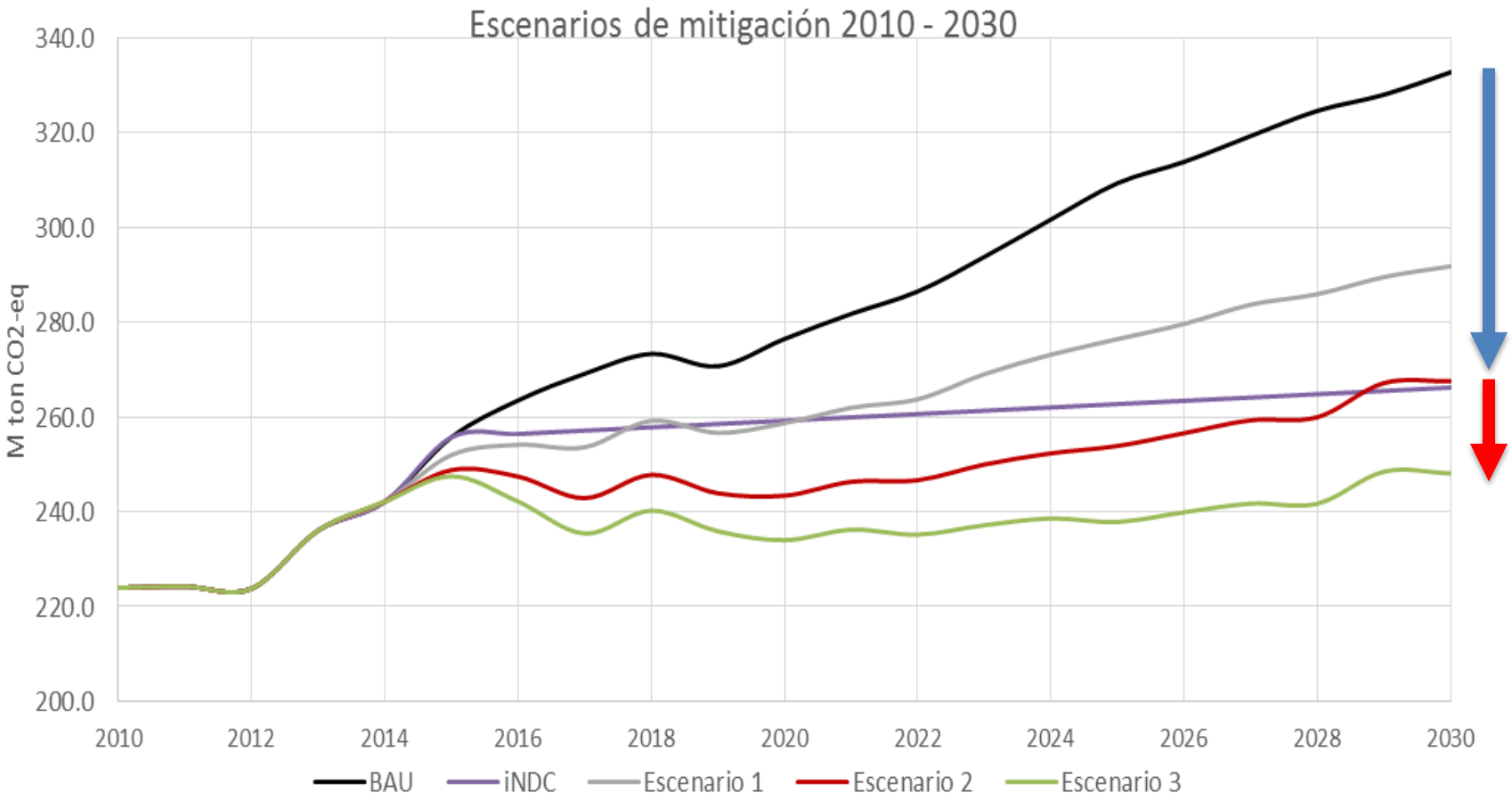


Linking also provides no security to host countries who need to make large investments

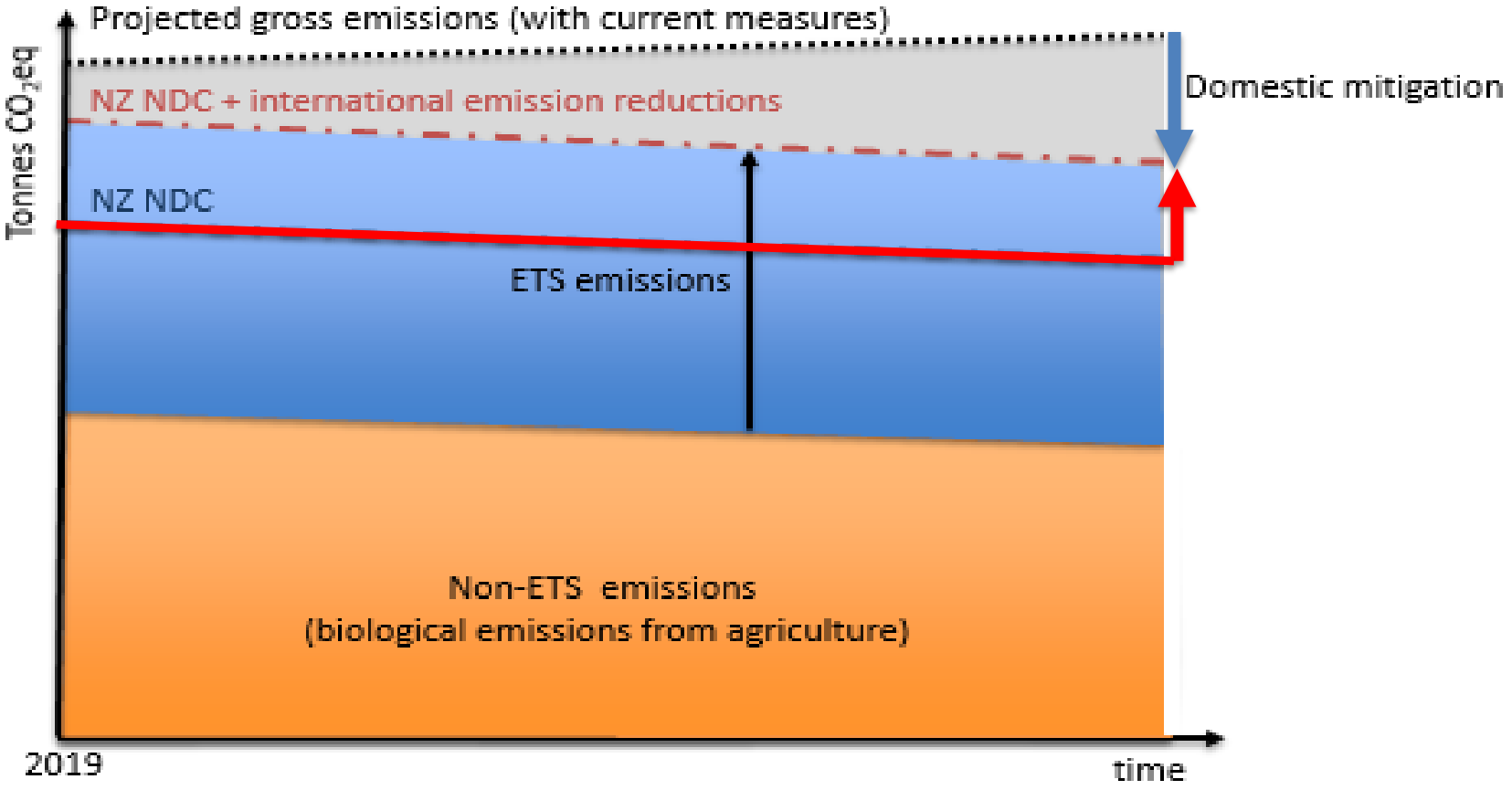
How can we most effectively structure contracts for large government-to-government trades instead?

Colombian supply

20% reduction in 2030 (NDC) at US$20 per tonne

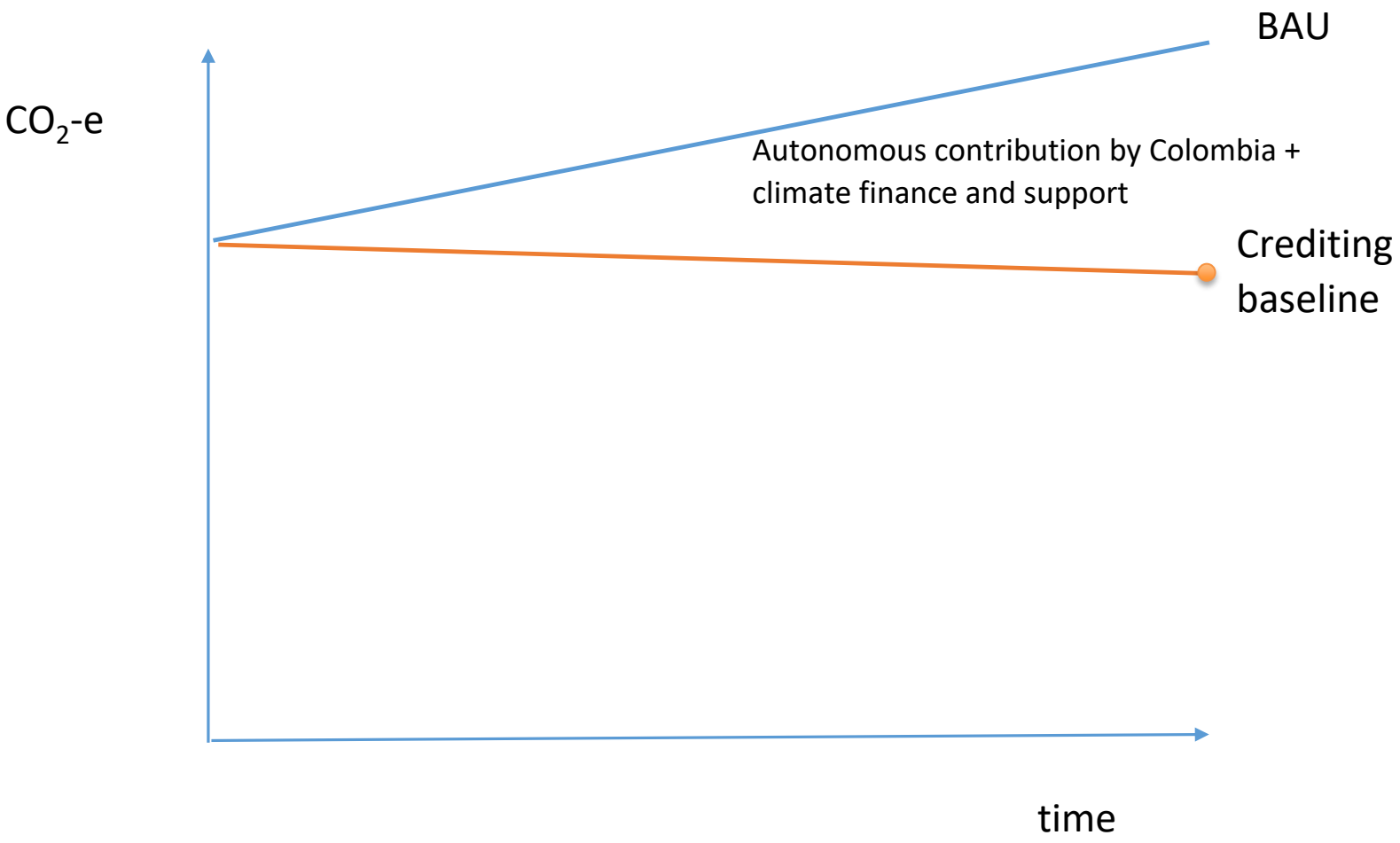


New Zealand demand

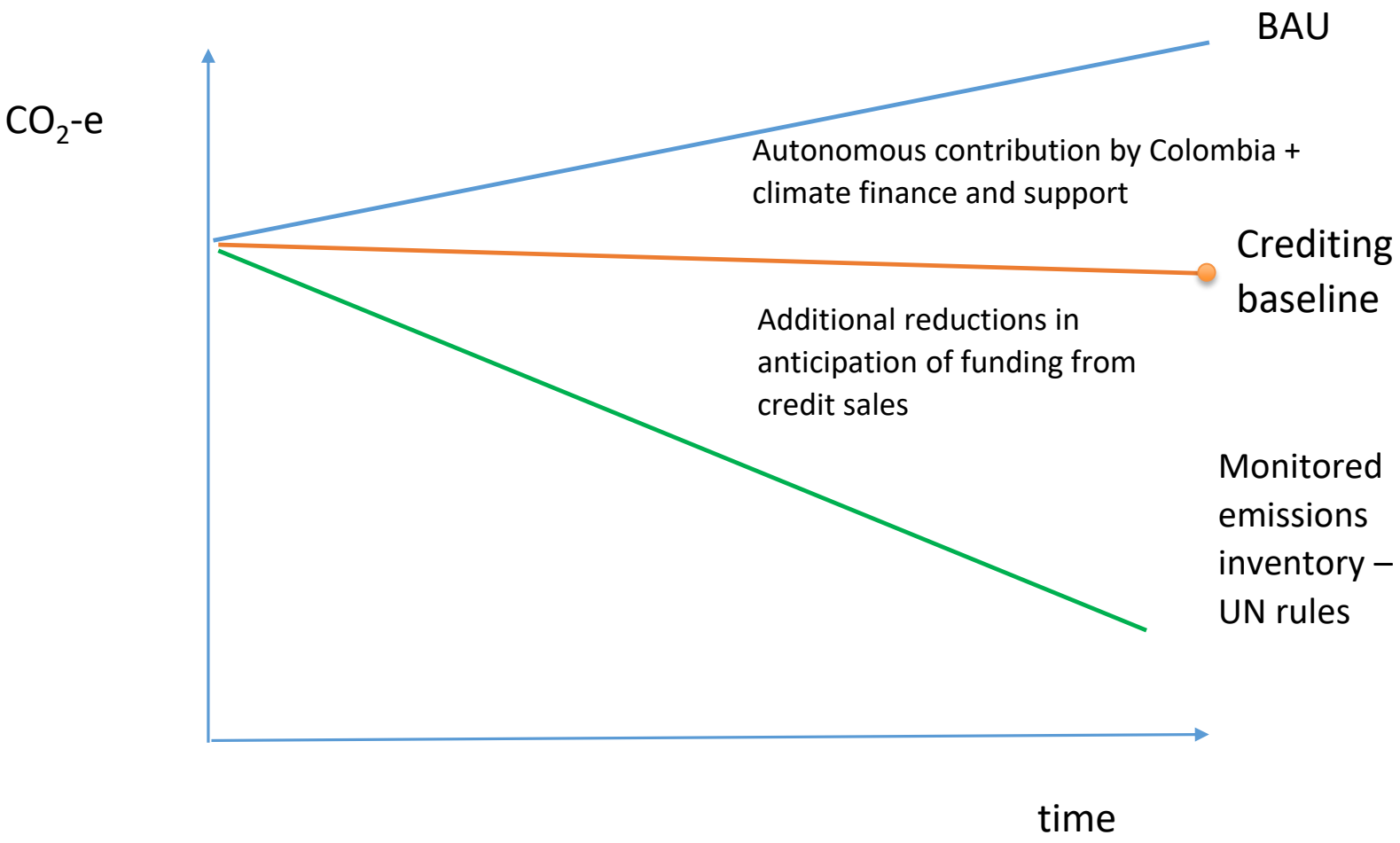


NZ Government predicts a need to purchase $170 m tonnes over the 2030s at ~US$30

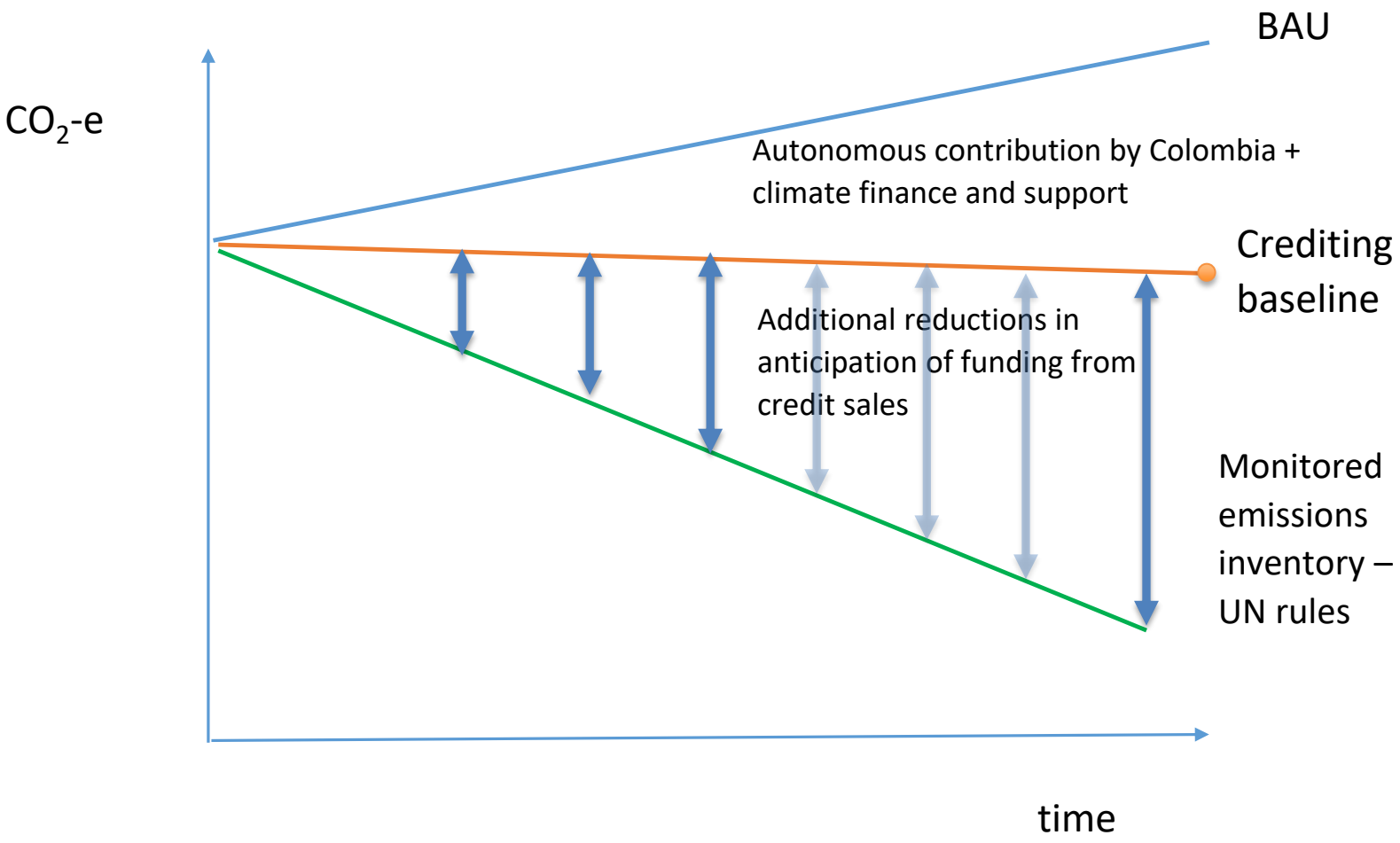
Climate team model



Climate team model



Climate team model



What host countries need

1. Guarantee of income flow if they make large costly (economically or politically) systemic changes

   For example: energy transition

   - public transport infrastructure
   - electrification of vehicles

   CDM did not provide this.

2. Expertise

3. Access to capital

What investors need

1. ‘International units’ to meet ambitious international targets during period of domestic transition to low emissions

2. Credible units in eyes of domestic taxpayers and voters

   and in eyes of other countries – to encourage reciprocal cooperation

Co-benefits associated with resource transfers help make contract work for host and investor

– e.g. poverty reduction, assist peace process

Key challenges for contract design

1. Risk of ineffective action (no sales)
2. Baseline risk – host can make effort and earn nothing
3. Credibility
   a. Additionality: NDC baseline and scale help
   b. Leakage: scale helps
4. Permanence of reductions relative to NDCs
5. Hold-up

Hold-up and underinvestment

Effective enduring mitigation requires:

- long-term investment,
- innovation,
- policy change and
- structural change

Once investments are made, the host has little bargaining power during renegotiation

they will be unwilling to invest.

Therefore: long-term ‘commercial’ contract, not treaty pledge

Climate team

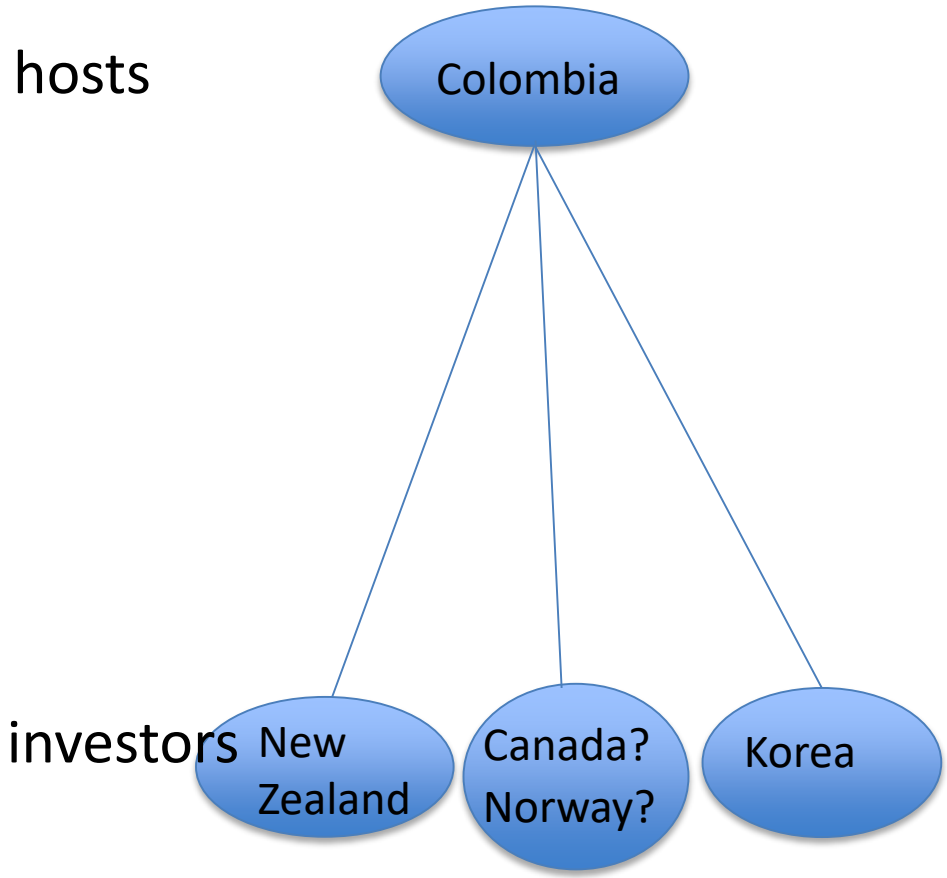
1. Agree on a crediting baseline – at least as ambitious as NDC
2. Use ‘climate finance’ strategically to help host country reach NDC
3. Agree on a minimum credit price – to protect the host

   The investor is required to pay at least this amount
4. Agree on a maximum credit price – to protect the investor against high international prices

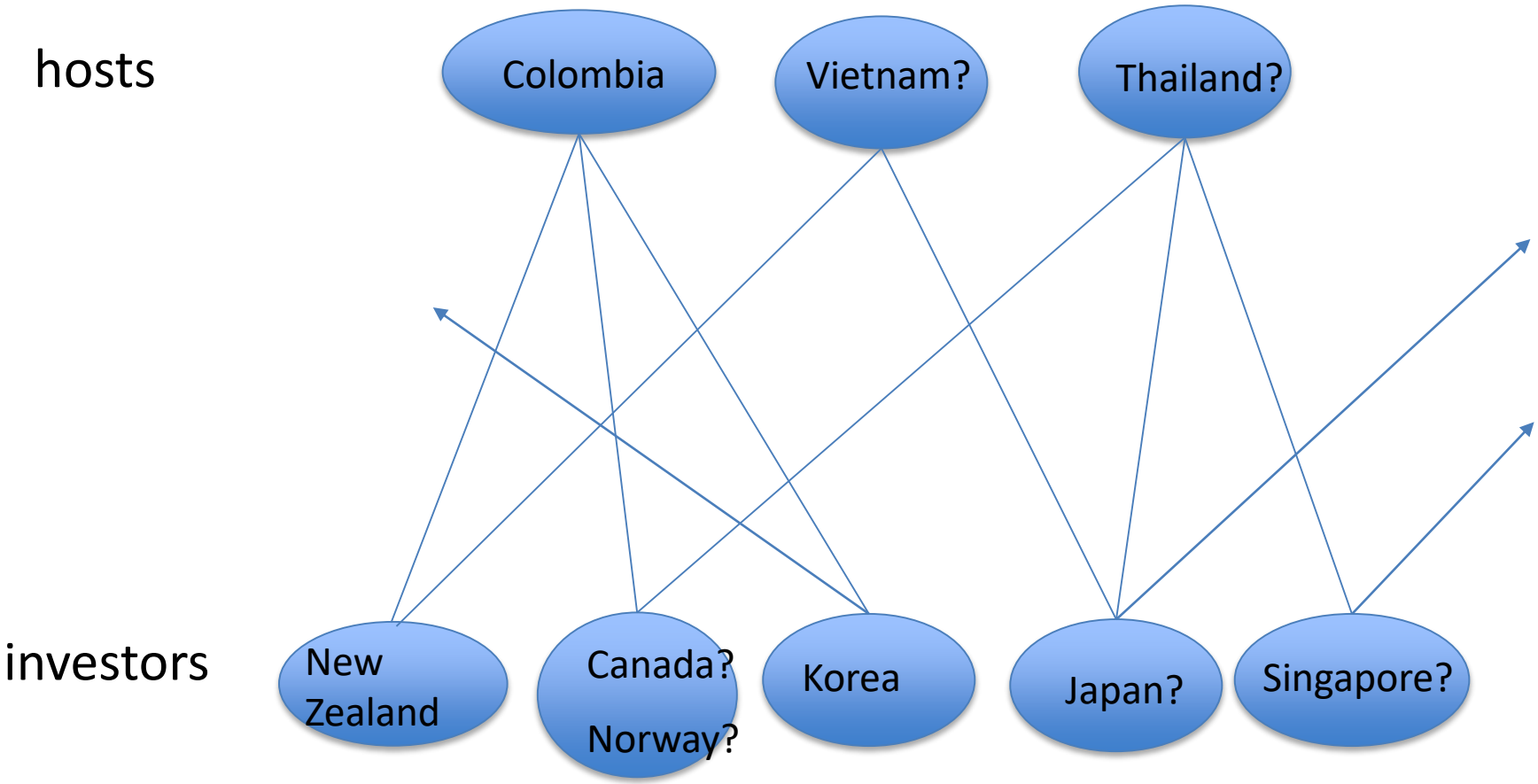
   The host may not sell to others unless the investor agrees
5. Agree on a level of funding committed in advance by the investor

   Once this is spent on credits, the contract ends
6. Complement contract with aligned finance and expertise

Risk of lack of supply: host constrained to sell to team



Network of climate teams?



Key thoughts

1. Some countries are willing to transfer significant resources to increase speed of others' transition to zero net emissions
2. No international mechanism currently exists – but 6.2 provides space for innovation
3. 'Climate teams' could help bring developing countries into 'Climate clubs' to increase the efficiency of global mitigation and enhance cooperation
4. We are designing a prototype model among New Zealand, Korea and Colombia

Potential in East Asia?

What is needed in the host country?

- Strong inventory
- Clearly defined and acceptably ambitious NDC
- Significant low-cost emission reduction opportunities beyond NDC
- Ability to implement policies that will achieve reductions
- Strong relationship with investor helps
- ETS - or other clear quantity control on emissions at a broad scale – helps

What is needed in the investor country

- Willingness to purchase units
- Willingness to commit to prices and purchase in advance
- Ability to help reduce host emissions helps