

TITLE: A very inconvenient report on RET

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Economics and politics don't really have much in common. While it is the job of politicians to decide what is fair and what is not, students are taught in economics 101 that economics is not concerned with fairness and distribution. The main job of economists is to help grow the pie, and the main job of politicians is to share it out. Last week's review of the Renewable Energy Target (RET) chaired by Dick Warburton provides a textbook example of just how incompatible economic and political logic can be.

Dick Warburton is proud to call himself a climate sceptic. And like many people with no expertise in the energy market, his starting point was the assumption that the RET was a source of upward pressure on electricity prices. Unfortunately for Mr Warburton however, the modelling conducted for his inquiry soon showed that the opposite was the case. Indeed, Mr Warburton spent hundreds of thousands of taxpayers' dollars on modelling by ACIL Tasman that confirmed the conclusion of four other modelling exercises.

They all showed that the RET pushes electricity prices down, not up. Whoops.

It gets worse for whoever in the PM's office wrote Mr Warburton's terms of reference. The ACIL Tasman modelling also shows that the RET, by pushing the profits of the coal-fired power stations down, delivers significant windfall gains to electricity consumers. The same consumers Tony Abbott promised lower electricity prices to at the last election. Despite evidence that the RET is good for consumers, and despite the Coalition's pre-election commitment to maintain the RET, Mr Warburton recommended that it be abolished. Unfortunately for Mr Warburton, the ACIL Tasman modelling provides clear advice on the likely winners and losers from scrapping the RET. It states: "The shift to the lower mandated RET improves coal-fired generators' values by around \$9.1 billion."

And, you guessed it, it tells us that that money comes from households and other businesses, mainly in the form of higher wholesale electricity prices. This is where the difference between politics and economics gets interesting. Mr Warburton proudly takes the economists' point of view to argue that \$9.1 billion "wealth transfers" between coal-fired power stations and Australian households is not worth considering in a cost benefit analysis. He actually argues that as such transfers have no impact on the GDP level, only its distribution, they can be safely ignored.

Again, in the words of ACIL Tasman, “An economic evaluation of the (RET) policy would not normally include wealth transfers where either producers or consumers benefit at the expense of each other. This makes projected changes to retail electricity prices mostly irrelevant in any economic assessment of the policy.”

Oh dear.

RET NOW HARDER TO SCRAP

It's not clear when Mr Abbott's office twigged to the significance of Mr Warburton's rather naive view that the distribution of winners and losers doesn't matter. But it is clear that both his inquiry, and his attempts to sell its recommendations, make the task of scrapping the RET much harder. The Coalition went to the last election promising to retain the RET in its current form. The Palmer United Party, the ALP and the Greens have all made clear that they will not allow significant changes to the RET to pass the Senate. The government's hand-picked economic modellers found that the RET pushes electricity prices down and that its removal would redistribute billions of dollars from households to coal-fired generators. Mr Warburton's recommendations must have been about as welcome in the PM's office as those made by the Commission of Audit. The renewable energy industry is growing strongly in Australia, generating not just electricity but jobs, investment and cheaper power bills. Despite these facts, and the disastrous Warburton review, a minority in the Abbott government still want to break both the industry, and an election promise.

Mr Warburton might not think it matters whether consumers have lower prices or coal-fired power stations have higher profits, but it's unlikely that many share his view. No doubt some economists and shareholders in coal-fired power stations agree with him. But they probably know it's best not to say it out loud.