

The Australia Institute

Research that matters.

TITLE: Carbon policy sinks to symbolism

AUTHOR: Richard Denniss

PUBLICATION: Australian Financial Review

PUBLICATION DATE: 5/07/14

LINK: <http://www.afr.com>

Just as introducing the carbon tax didn't really drive the cost of a leg of lamb to \$100, removing it isn't really going to have any noticeable impact on the cost of living.

Supermarkets are adamant they didn't increase prices when the carbon price came in, and they are just as adamant they won't cut prices when it is scrapped.

In rich countries with strong economies, politics revolves around symbolic issues. Asylum seekers account for a tiny fraction of our rapid population growth but are the focus of all our debate about population.

Our public debt is tiny, but the political furore around it prevents meaningful debate about the kind of infrastructure and human capital we should invest in. The carbon price was never really a "wrecking ball" through the economy, but the polemic around it prevented meaningful debate about shifting the burden of tax away from labour and towards pollution.

If not repealed, the carbon price introduced by Labor is set to fall from \$25.40 today to about \$8 next June, when the fixed-price period ends and the floating-price period begins.

Doing nothing would deliver 60 per cent of the carbon price reduction that comes with Tony Abbott's repeal. And let's not forget that, under the current scheme, the so-called "emissions-intensive trade-exposed" industries get about 90 per cent of their pollution permits for free.

Leaving economic reality aside, repealing the carbon price is a huge symbolic victory for big polluters and the Abbott government. It's proof that the Labor-Green government has been deposed. It also helps reassure business that any future increases in tax revenue will fall on households, via the goods and services tax, rather than on polluters, via efficient Pigouvian taxes.

But it is not just the Abbott government that is interested in symbolism. Many environmentalists have been pushing hard for a zero-price emissions-trading scheme to supposedly show that Australia is committed to tackling climate change.

The Palmer United Party has resisted calls to insert a zero price into the existing carbon pricing regime. It has agreed to push for a new emissions-trading scheme after voting down the current one, albeit one which does not commence until other countries introduce similar schemes.

SCIENCE HARDENS, PRICE FALLS

While there is no doubt that political symbols matter, especially at a diplomatic level, there is also no doubt that price signals matter more, especially when it comes to making long-lived investments in energy generation. Regardless of whether the Labor-Green carbon price or the Abbott government's Direct Action plan is in place, the fact is, a big fall in the Australian carbon price was inevitable.

At a time when the science of climate change is hardening, it seems remarkable that the carbon price would be falling.

While economic theory has been almost entirely absent from the design of the Labor-Green and Coalition climate policies, it seems economists and business people can probably agree about the need for certainty.

There is a simple alternative to the political instability of on-again, off-again carbon pricing schemes, and the economic volatility of the roller-coaster carbon prices that come with an emissions-trading scheme. It's called a carbon tax.

Imagine if Australia introduced a small carbon tax of \$5 per tonne, with no exemptions, and used all of the funds to reduce corporate and personal income taxes. The tax could be scheduled to rise slowly and steadily by \$1 per year.

If Kevin Rudd had introduced such a scheme in 2008, the price would still only be \$11 per tonne, far less than the \$23 Julia Gillard's scheme started with, and a bit more than the floating price would soon to collapse to if not repealed.

Economic modelling would confirm what common sense suggests. A small but slowly rising carbon price would slowly speed up the rate at which emission-intensive capital equipment was phased out, while increasing the post-tax returns to capital and labour. It would also provide certainty to business.

In a rich country where political symbolism trumps efficient policy design, such a reform is unlikely. Indeed, even the environment movement seems more interested in the political symbolism of zero-price emissions-trading schemes than pushing for an actual price on pollution.

