

Questions and answers

1. Kyoto

What are New Zealand's commitments under Kyoto?

New Zealand, like the other signatories to the protocol has signed up to reducing its Greenhouse Gas Emissions (GHGs) to below 1990 emission levels on average for the years 2008-2012.

Countries who have signed the protocol have agreed to pay a fee on a per mega tonne basis for emissions to the UN if they fall short of that target. New Zealand is expected to be well short of its target and on current estimate will owe somewhere around \$375 million in 2012.

Is everyone in the same position as New Zealand?

No. Some countries will meet or are much closer than New Zealand to meeting their targets.

How did they manage that?

In many cases their targets were easier to achieve than New Zealand's. For example Germany and the UK were able to make significant gains by simply switching electricity production from coal to gas. There are significantly less emissions from gas than there are from coal so it was a bit like picking fruit from the low hanging tree. New Zealand was something like 60% reliant on renewables in 1990 so we didn't have the same easily available options in the energy sector.

Are all countries signed up to Kyoto?

No. Among others, America (25% of total global emissions), the world's second largest source of GHGs has not signed up while China(26%), the world's largest emitter, has developing nation status and is not subject to the same strict regimes. Australia has also only recently decided to join.

What happens after 2012?

After the first Kyoto period in 2012 all the signatory countries renegotiate their commitments to reduce or maintain GHGs for a second commitment period.

So in less than four years there is a new system?

Yes. There are likely to be revised targets.

2. Allocations

What are these free allocations that you mentioned?

Again based on agreed targets in agreed sectors each signatory country to Kyoto has been granted a certain number of allocated (free) carbon units. It is up to individual governments how they then allocate those units to certain businesses or sectors within their economies.

Does New Zealand have an allocation?

Yes it does.

What are the allocations used for?

Most Governments are using them for industries that they recognise cannot make rapid reductions in their emissions or for industries that are seen as vital to economic well being.

Is the New Zealand Government making similar allocations?

It has made provisions for some sectors in New Zealand but the last of those, agriculture, is phased out by the end of 2025. Most other countries have opted not to completely phase out their allocations until they are due to expire.

As far as we know New Zealand is also unique in removing its allocations for agriculture and including agriculture and forestry in its ETS.

3. The numbers

Where has NZIER got its figures from?

We have been working with a number of industry and interest groups who have provided us with detailed information for their sectors and we have also used commonly available data provided by Government organisations such as Stats NZ, MfE and others.

Why are your figures different from Government's?

Our model is a similar model to that used in Infometrics work for the government. Our view of how the economy adjusts over the short and long term is different however. We think wages are sticky in the short term, while capital stocks can adjust in the longer term. Under this view, we are more likely to capture the impacts of the ETS on the productive side of the economy.

Why are NZIER predictions different to other commentators?

We are surprised at the lack of quantitative analysis on such an important policy decision.

Our results arise out of many months of work on this topic, the development of a sophisticated model capable of assessing economy-wide impacts, and the gathering of a great deal of information and analysis.

We have not set out to build a case. We also feel we have leaned to the conservative rather than the worst case scenario.

It should also be noted that our results aren't in fact different from all other commentators. The government-commissioned peer review of the ETS by Dr Suzi Kerr highlighted qualitatively the issues that we quantitatively assess.

Why are the costs of the ETS high?

It's a combination of costs to business, contraction in the domestic economy, loss of competitiveness internationally, reduction in wages, contraction in household spending, and some increase in prices.

Can you quantify the sectors where prices will increase?

They will come across the board. Energy costs will increase because we do generate from sources such as coal and gas and the emissions costs will almost certainly be passed on to both domestic consumers and business customers.

Higher energy prices will impact on manufacturing and processing industries and those increases will again be reflected in the costs of goods passed on to consumers.

The horticulture and dairy sectors are huge consumers of electricity, their costs will be passed on to domestic consumers.

New Zealand is also heavily reliant on road transport for moving goods around the country. Higher diesel and petrol costs will be factored into the costs of consumer goods, and reduce the profitability of exports.

4. Buying overseas credits

How do we benefit from paying for offshore projects?

It is simply cheaper for NZ to pay for credits earned by a project overseas that, say converts electricity generation from coal to gas, than it is for us to impose costs on our businesses here.

But aren't we just transferring the problem?

If the goal is to reduce global emissions, then no. There are many easier options overseas that will benefit the planet sooner than trying to extract further gains from an already efficient producer like New Zealand.

Our agricultural sector comes under constant pressure for its emissions, the bulk of which are methane from livestock. Short of slaughtering vast numbers of livestock there are no rapid gains to be made in a sector which makes up ~50% of our emissions.

The research already underway into methane reduction biotechnology may take years to come to fruition. Nitrogen inhibitors are possibly a more immediate solution, but these emissions are less than a third of agricultural emissions.

We are internationally recognised as one of the most efficient agricultural producers in the world but New Zealand is contemplating penalising our farmers while allowing other, inefficient farming systems overseas to continue unchecked. That doesn't make sense.

Are you suggesting abandoning the ETS?

No, not at all. We are suggesting that the Government take a breath and properly consider the full impacts of an ETS, whether it's this one or some modified versions.

We can meet our current Kyoto obligations at much less cost to the economy than the proposed ETS. We don't need to lead the charge in crucial sectors such as agriculture when that's clearly to our detriment, especially as emissions leakage means we won't actually reduce global emissions.

The phase-out of free allocation is key design feature of the ETS. We suggest some form of 'best practice' intensity-based free allocation to firms facing international competition.