At what cost carbon credits?

There is much confusion in the marketplace about the likely impacts of carbon trading schemes on the Australian economy. I suspect there are some uncomfortable effects for both business and consumers that policymakers aren't discussing. Indeed, the release of the Deutsche Bank report on emissions trading highlights some worrying aspects of the Federal Government's task group recommendations for some economic sectors. It also points out the winners in this new environment – most likely to be the banks and financial institutions involved in operating the carbon trading market itself.

So what don't we know? The first thing of note is that carbon trading involves something that doesn't actually exist. *The Economist* pointed out in its commentary on the European scheme (ETS) that, "The trade is not actually in carbon, but in non-carbon: in certificates that establish that so many tonnes of carbon dioxide have not been emitted by the seller, and may therefore be emitted by the buyer." This artificiality puts a much greater burden on market regulators and policymakers and raises some questions about their likely approach.

We also don't know how the initial allocation of credits will be undertaken? Surely those industry sectors with high energy consumption will get more credits – iron and steel, chemicals, plastics, paper and manufacturing to name a few, not small parts of the economy. Then there is the question of allocation of targets and the rate of reduction if targets are set. Will there be some system for estimating how easy it is for certain industries to reduce their emissions? What about new entrants to the market. Does this mean carbon-based protection?

Then there is the carbon price or in other words the price at which the initial non-carbon permits are set? If the objective is to reduce overall emissions, then the cost of reducing emissions must logically be less than the cost of a credit. In Europe most large-scale emitters plan to buy credits rather than reduce emissions simply because they are cheaper than investing in new processes. Thus, customers are paying twice for lack of investment.

Maybe I'm completely wrong or maybe the economics of carbon trading are more complex, but until we all know what we are talking about, business and customers will remain highly suspicious of how this new market will allocate its benefits.

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