Investor Group on Climate Change

IGCC POLICY BRIEFING

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US election and net zero Asia re-shape the 2021 policy agenda

"At this moment of profound crisis, we have the opportunity to build a more resilient, sustainable economy — one that will put the United States on an irreversible path to achieve net zero emissions, economy-wide, by no later than 2050."
US President-Elect Joe Biden

Summary

This brief provides an overview of the climate policy implications of the United States (US) election. It outlines how the impact of a Biden Presidency on climate change policy will be felt through two main channels - diplomatically and through an acceleration of domestic emissions reductions in the US. This will have significant implications for Australia and will support existing New Zealand policy commitments.

Key points include:

1. Climate change will now be one of the US' top foreign policy objectives. This not only impacts on the Paris Agreement negotiations but on all outcomes of other major global political meetings such as the G20.
2. Net zero emissions by 2050 is now the global benchmark against which to judge the credibility of long-term commitments to address climate change.
3. Australia will increasingly be seen as an outlier, as countries increasingly re-examine national 2030 emissions targets and others set net zero targets. The US currently has a 2025 target under Paris and will need to set one for 2030 before COP26 next year. The optics of major allies strengthening their 2030 targets will be difficult on Australia, especially as the Federal Government remains committed to use Kyoto carry-over credits to achieve its 2030 target.
4. The Biden-Harris platform includes a US$2 trillion economic recovery plan focused on clean energy investments and the creation of green jobs. Many of the policies outlined can be implemented through executive orders or appointing new administrators and do not require support from Congress. However, measures such as an enforcement mechanism to reduce emissions in the electricity sector and tax measures will require the Biden Administration's engagement with Congress to pass.
5. Finally, the sheer scale and size of the US economy means even small changes in direction can have global implications. Major investments by the US Government and other major economies into existing and emerging clean technologies may create further challenges for investment in Australia as capital flows to markets with supportive policy frameworks delivering better long-term rates of return.

Coupled with recent policy commitments for net zero targets across China, Japan and South Korea, it is clear that 2021 is shaping up to be a very different year for the climate change policy landscape.

About Us

The Investor Group on Climate Change (IGCC) is a collaboration of Australian and New Zealand investors focused on the impact that climate change has on the financial value of investments. IGCC represents institutional investors with total funds under management of over $2 trillion, and others in the investment community interested in the impact of climate change. IGCC members cover over 7.5 million people in Australia and New Zealand.

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Building pressure ahead of COP26

Australia the outlier?

The Obama presidency was central to the delivery of the Paris Agreement in 2015. At that time, climate change was the US' top foreign policy objective. This not only impacted on the Paris Agreement negotiations but also on all other major global political moments (e.g. G20 meetings) and interventions on other international agreements to ensure consistency with Paris outcomes (e.g. emergence of the Task Force on Climate-releated Financial Disclosures, limiting of coal power financing under OECD export credit agency agreements).

The Biden-Harris platform states, "[Biden-Harris] *will not only recommit the United States to the Paris Agreement on climate change – he will go much further than that. He is working to lead an effort to get every major country to ramp up the ambition of their domestic climate targets.*"

The election of President Trump and the withdrawal of the US from the Paris Agreement has created cover for other recalcitrant governments. The US will now re-enter the Paris Agreement. The Investor Agenda, of which IGCC is a convening partner, issued a joint statement on the formal withdrawal of the US in early November (available here).

On the back of recent announcements in Asia (see section below) and the EU, significant momentum is building towards COP26, even amidst the ongoing global challenge of COVID-19. The Biden-Harris presidency will strengthen and accelerate this momentum and leave Australia increasingly isolated diplomatically unless it shifts its current position. For example, over 70 per cent of Australia's two-way trade will be with countries that have net zero targets around 2050 (Table 1). Specific international actions that President-Elect Biden has flagged they will undertake include the following:

- Convene a world climate summit in early 2021 to directly engage the leaders to set more ambitious national targets, above and beyond commitments already made.
- Make future bilateral US-China agreements on climate contingent on China eliminating unjustified export subsidies for coal and other high-emissions technologies, and making verifiable progress in reducing the carbon footprint of projects connected to the Belt and Road Initiative.
- Seek a G20 commitment to end all export finance subsidies of high-carbon projects.
- "Name and shame global climate outlaws": The US Department of State will publish rankings of the country's track records on climate change.

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Table 1: Net zero emission economy is the destination for a growing number of Australia's major trading partners.[1] See section 'Momentum building in Asia: China, Japan, South Korea in race to net zero' for more.

	Top ten major trading partners (% trade)	AUD Sustainable Recovery (% of total fiscal stimulus spending)	On track to meet 2025/30 target	Mid century net zero target
Australia		$3.7bn (1.1%)	N	N
Top trading partners in G20				
China	**1st** (24.4%)	$12.38bn (0.7%)	Y	Y
EU	**2nd** (13.3%)	>$400bn (30%)	Y	Y
France		*~$54.4bn (6.6%)*		
Germany		*~$50.34bn (3.6%)*		
Italy		*$1.25bn (<0.1%)*		
Japan	**3rd** (9.7%)	$0bn	Y	Y
USA	**4th** (8.8%)	<$1bn (<0.1%)	N	Y
Republic of Korea	**5th** (6.5%)	~$37bn (5%)	N	Y
India	**6th** (3.6%)	$0bn	Y	N
UK	**8th** (3.5%)	~$43bn (7.3%)	Y	Y
Other selected G20 and major trading partners				
Canada		$4bn (2.8%)	N	Y
Brazil		$0.4bn (0.2%)	N	N
Indonesia		$0.3bn (0.2%)	Y	N
Singapore	**9th** (3.5%)	$0bn	Y	N (in 2nd half of the century)
New Zealand	**7th** (3.5%)	No data	Y	Y (all gases ex. farm methane)

1 See Hepburn and O'Callaghan at Centre for Policy Development (2020): https://cpd.org.au/wp-content/uploads/2020/09/COVID-19-fiscal-recovery-stimulus-to-win-on-economics-and-climate-Hepburn-and-OCallaghan-1.pdf. For background on national emissions targets see Climate Action Tracker (2020): https://climateactiontracker.org. Trade data from DFAT (2020): https://www.dfat.gov.au/about-us/publications/trade-investment/trade-at-a-glance/Pages/trade-at-a-glance

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2030 targets back in the picture

The US was one of the few countries to set a 2025 emissions target under the Paris Agreement. Most countries set 2030 targets. When the US joined the Paris Agreement it set a target of 26-28 per cent on 2005 levels by 2025. Australia has the same per cent reduction target but five years later in 2030.

The Paris process was designed to address the inconsistency between 2025 and 2030 targets by providing an opportunity for the US and other countries with 2025 targets to set 2030 targets before COP26. The US would not accept them doing this alone so all countries are expected to revisit their short-term targets at this time as well. This process has begun with the EU, China, Japan and South Korea, in addition to setting net zero emissions targets, are also agreeing to revise their 2030 goals.

This will impact on the Australian policy landscapes by adding pressure on the Federal Government to revisit its current 2030 target.

Under the Paris Agreement rules, the US' 2030 target must be stronger than its existing 2025 target. The optics of major allies like the US, UK, and EU updating and strengthening their 2030 targets will be difficult on Australia, especially as the Federal Government remains committed to use Kyoto carry-over credits to achieve its 2030 target. No other nation is proposing this approach.

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Delivering domestic US emissions reductions

The Biden-Harris domestic emissions reductions platform is comprehensive and covers emissions reductions and resilience measures across the economy. In July 2020, the Biden-Harris campaign announced a US$2 trillion economic recovery plan focused on clean energy investments and the creation of green jobs as a vehicle to pull the country out of the economic crisis caused by the pandemic. This includes:

1. 'Ensure the US achieves a 100 per cent clean energy economy and reaches net-zero emissions no later than 2050': President Biden will sign a series of executive orders toward the above-stated end as well as demand that Congress establish an enforcement mechanism, invest in energy and climate research and innovation, and incentivise the rapid deployment of clean energy innovations. For example, implementing new fuel economy standards for vehicles, establishing new appliance- and building-efficiency standards, and setting aggressive limits on methane pollution for oil and gas producers. The plan aims to achieve an emissions-free electricity sector by 2035.

2. 'Build a stronger, more resilient nation': The plan aims to make infrastructure investments to rebuild the nation and to ensure that our buildings, water, transportation, and energy infrastructure can withstand the impacts of climate change. For example, new zoning and building codes for communities to adapt to climate change will be implemented.

3. 'Stand up to the abuse of power by polluters who disproportionately harm communities of color and low-income communities': For example, direct the Environmental Protection Agency (EPA) and Justice Department to more aggressively pursue criminal anti-pollution cases.

4. 'Fulfill our obligation to workers and communities who powered our industrial revolution and subsequent decades of economic growth': Biden-Harris platform includes policies to help protect workers affected by the transition to cleaner energy sources. For example, by ensuring that miners receive the pensions and health benefits they have been promised. The Biden-Harris platform also vows to "make the largest-ever investment in clean energy research and innovation," at an estimated cost of US$400 billion over 10 years. This investment is aimed at developing new technological breakthroughs that will create jobs and reduce emissions.

5. Engagement with financial regulators: Finally, a Biden-Harris Administration will engage with financial regulators on climate change in the US. For example, options include using Treasury's Financial Stability Oversight Council (FSOC), to perform a thorough analysis of transition and physical risks. Regulators, including the Office of the Comptroller of Currency (OCC), the Federal Deposit Insurance Corporation (FDIC), the Securities and Exchange Commission (SEC) and the Federal Reserve, could also stress tests financial institutions and the FSOC can also coordinate with financial regulators to require mandatory climate-related financial disclosures. See also for example, Commodity Futures Trading Commission's (CFTC) Climate-Related Market Risk Subcommittee report on managing climate risk in the US financial system.

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The Biden-Harris presidency's ability to deliver on all of these policies is currently uncertain. Many of the policies outlined can be implemented through executive orders that do not require support from Congress. However, measures such as an enforcement mechanism to reduce emissions in the electricity sector and tax measures will require the Administration's engagement with Congress to pass. The two principal uncertainties are:

- **The Senate results are not yet clear.** The Administration will need at least 50 Senate votes to gain congressional support for legislative mechanisms.
- **The posture of the Republican party on climate change over the next four years is also uncertain.** Many Republicans also strongly support renewable energy because of the job creation opportunities and the benefits to national and energy security.
- **The impact of current subnational actions, such as California emission trading scheme, are already projected to reduce emissions 25 per cent below 2005 levels by 2030.** Scaling up current subnational actions could reduce emissions 37 per cent by 2030 and combined with strong federal climate policy could reduce emissions nearly 50 per cent by 2030.

Momentum building in Asia: China, Japan, South Korea in race to net zero

East Asia's three biggest economies have set ambitious deadlines for rapidly decarbonising their economies broadly in line with the Paris Agreement.

In September, President Xi Jinping announced that China would aim for carbon neutrality by 2060. This was closely followed by announcements from Japan and South Korea to achieve net zero emissions goals by 2050. Proposed climate policies under the Biden-Harris presidency will likely strengthen and accelerate policy action to achieve net zero targets.

The implications of this shift will be felt acutely in the region and especially in Australia. Meeting these pledges will mean rapid structural changes in energy production, manufacturing, transportation and infrastructure development. Many of these sectors will need to meet new standards on emissions, which will have a knock-on effect on the suppliers of the fossil fuels, raw materials and technologies that will move towards net zero carbon solutions.

Notwithstanding the optimism with which these announcements were greeted, there is the need for greater detail from each country to give confidence that these longer-term goals will be implemented in the short-to-medium term.

China

Specific domestic policies to achieve China's long-term goal will emerge as i develops and agrees its 14th Five-Year Plan to define government policy over the coming years. This will be approved in March 2021 during the fourth session of the 13th National People's Congress. Since announcing the net zero target, China's ministries have already begun to follow up with guidelines for specific sectors, including:

- **Green finance** - five government ministries have issued a set of guiding opinions to encourage private investment and foreign capital to back green bonds and fund climate-friendly projects.
- **Electric vehicles** - the Ministry of Industry and Information Technology (MIIT) has released the Technical Roadmap 2.0 which calls for electric vehicles to account for 50 per cent of new sales by 2035.
- **Electricity sector** - China's power sector is likely to be one of the most affected sectors as coal-fired power plants account for two-thirds of China's electricity output. Policymakers will need to reverse course from their previous position of supporting new coal-fired power plants as a means of driving an economic recovery that had resulted in a project pipeline of 300GW. Government researchers have recommended China needs to stop the building and financing of all new coal-fired power plants, cap emissions and double wind and solar capacity to 500GW each by 2050.

Japan

Central to Japan's transition to net zero will be concrete measures in the near-term to transform the nation's heavy reliance on imported fossil fuels, with energy-related emissions accounting for 85 per cent of the national total.

Japan's current energy policy envisages a modest 22-24 per cent of electricity from renewable sources by 2030, together with 26 per cent from coal and 27 per cent from LNG. These targets are currently under review, with Japan's 2030 energy mix likely to be revised in favour of renewable energy. A detailed roadmap for energy is due by the end of December for approval in 2021.

In addition to earlier commitments to phase out inefficient coal plants by 2030, a key enabler will be upgrades to electricity distribution networks throughout the country to cater for new renewable energy access to the market, which has been resisted by incumbent regional power companies. With 17 new coal-fired power plants in the planning or early construction stages, and significant emissions intensive assets on balance sheets, negotiations with the major power companies and heavy industry will be crucial in securing bold reforms to unlock new investment, stimulate new demand for zero carbon energy and adequately incentivise the structural shifts required.

South Korea

Korea's Green New Deal aims to transition to green infrastructure, to expand low carbon, decentralised energy and to establish a green industry innovation ecosystem, for which the Moon Administration has pledged US$65 billion over the next five years. From the 2021 fiscal budget plan, US$7 billion is allocated for the Green New Deal. US$2 billion will be invested in the green transition for public infrastructure, and US$3.7 billion on the construction of charging stations along with expansion of electric and hydrogen vehicles.

Considering that 40 per cent of its electricity is generated from coal power and less than 6 per cent from renewables, South Korea will have to drastically curtail coal-fired power plants and increase renewable energy generation to become carbon neutral by 2050. With seven coal power plants still under construction, the Moon Administration has earlier announced that it would halve the total of 60 coal-fired power plants by 2034.

On renewable energy, the Green New Deal policy plans to triple solar and wind power facilities to 42.7GW by 2025 compared to last year of 12.7GW. This would make a significant contribution to achieving the Renewable Energy 3020 Plan which aims for 20 per cent renewable energy by 2030 (or 63.8GW of supply).

Legislations on green finance facilitation, net zero society transition, green pricing, and the introduction of Power Purchase Agreements (PPA) are also currently under review by National Assembly committees.

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Implications for investors

The election of a Biden-Harris presidency has significant implications for investors.

Firstly, commitments from investors, companies and nations to net zero emissions by 2050 have snowballed in recent months. The re-engagement of the US, with its own net zero emissions target, will only accelerate and bolster this process internationally. If it was not already, net zero emissions by 2050 is now the global benchmark by which to judge the credibility of a long-term commitment to address climate change.

Australia is due to submit its own long-term strategy by November 2021. IGCC will continue to engage with other influential stakeholders to ensure an investable and credible long-term policy framework is agreed before COP26.

Secondly, the international conversation over the next 12 months will now shift to more explicitly focus on increasing the ambition of national 2030 targets. This five-year review process to 'ratchet up' ambition is an intentional and important element of the agreements made in Paris and this process will begin again in a few years time. Governments will not be able to dodge additional and stronger commitments to reduce emissions indefinitely.

New Zealand has agreed to update its 2030 target next year. Australia's stance on 2030 targets will be in focus as they are considered weak by international standards and the Federal Government plans to weaken them further through the use of Kyoto carry over credits. IGCC research indicates a stronger 2030 emissions target would open up multi-billion dollar investment opportunities in Australia.

Thirdly, the sheer scale and size of the US economy means even small changes in direction can have global implications.

For example, the engagement of US financial regulators to embed climate-related risks and opportunities into regulatory approaches would have global implications. Also, major investments by the US Government and other major economies into existing and emerging clean technologies may create further challenges for investment in Australia. Technology costs and state-based policies in the US already make it an attractive investment opportunity such as renewables and carbon sequestration. Additional policy intervention in the US will only exacerbate the challenges Australian investors will have in choosing domestic projects over more competitive investments in other countries.

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