

STRONG GROWTH, LOW POLLUTION

MODELLING A CARBON PRICE

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FOREWORD

The science of climate change is compelling, the threat is real and the economic and environmental benefits are tangible.

The need for action to prevent climate change is clear. This Government has put forward a comprehensive plan to introduce a carbon price for Australia.

The Treasury modelling has been prepared to inform policy design and public discussion about carbon pricing. Treasury modelled a range of scenarios which explore different environmental targets and design features in a carbon pricing scheme. The modelling provides important insights into the economic impacts of carbon pricing at global, national, sectoral and household levels.

The world is moving to act. At the Copenhagen and Cancun conferences, we saw the world step up with pledges to take action to put the world on a path to reduce the risks of dangerous climate change. Australia must contribute its fair share to this world action.

The Government is committed to taking action in a fair and effective way. Pricing carbon through a market mechanism provides incentives for emission reductions to occur where they are cheapest. As the Productivity Commission found, when firms and consumers make the decisions, rather than governments, the costs of reducing emissions are lower. A carbon price is the most economically responsible, fair and effective way to tackle climate change.

Building on modelling completed by the Treasury in 2008, this report presents one of the largest and most complex economic modelling projects undertaken in Australia. It provides a comprehensive analysis of the implications of carbon pricing on the economy, at a global, national, regional and sectoral level. The modelling draws on experts from within Treasury, across Australia and around the world, and represents a robust and comprehensive analysis of carbon pricing for Australia.

The Treasury modelling finds the costs are modest to cut pollution and transform our economy to cleaner energy sources. A carbon price will ensure the Australian economy continues to prosper while we cut emissions to reduce the risks of dangerous climate change. Incomes and jobs continue to grow under a carbon price, with the majority of the economy experiencing only a very modest slowing in growth.

The Treasury modelling also finds the world will face higher long-term costs if we defer action to reduce the risk of dangerous climate change. We must act now to protect our future economy, future environment and future generations.

This report will form an important part of the community debate over carbon pricing over the coming months. Given the long lead times in commissioning detailed modelling of the electricity generation and other sectors, it was necessary to settle on the broad architecture of the global scenarios in late 2010 and the starting prices for the economy-wide modelling analysis in early 2011.

As a consequence, the economy-wide modelling presents scenarios with starting carbon prices in 2012-13 of A\$20 and \$30 /t CO₂-e, growing at 5 per cent per year plus inflation before moving to a flexible price. The \$20 core policy scenario has a slightly lower carbon price path over the

first 3 years than agreed by the Multi-Party Climate Change Committee (MPCCC), which is for a \$23/t CO₂-e starting price, growing at 2 ½ per cent per year plus inflation. As it is a separate modelling exercise, with shorter lead times, the modelling of household impacts reflects the agreed starting carbon price of \$23/t CO₂-e in 2012-13.

The Government's plan has been negotiated with the MPCCC, which agreed on a comprehensive set of measures to tackle climate change. The Government is separately proposing additional transition and abatement measures, which are separately identified in the policy documentation and fiscal costings. These measures include support for jobs in the coal and steel industries and inclusion of heavy on-road transport in the carbon price coverage from 2014-15.

The economy-wide modelling contained in the modelling report does not include all elements of the final policy package as agreed by the MPCCC. For example, in addition to the slightly lower start price, the core policy scenario assumes unlimited international permits over the entire period, a binding 100 per cent facility allocation cap and applying an effective carbon price to heavy on-road vehicles from 2014-15.

Even so, it is expected that the outcome of any updated modelling would closely match the results of the core policy scenario.

Once again, this is one of the most comprehensive modelling exercises ever conducted in Australia. The report provides extensive details on the assumptions and frameworks used, with full details provided on the Treasury website.

A handwritten signature in black ink, appearing to read 'Wayne Swan' in a cursive style.

The Hon. Wayne Swan, MP
Deputy Prime Minister and Treasurer

A handwritten signature in black ink, appearing to read 'Greg Combet' in a cursive style.

The Hon. Greg Combet, MP
Minister for Climate Change and Energy Efficiency