Policy Contribution
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A whole-economy carbon price for Europe and how to get there

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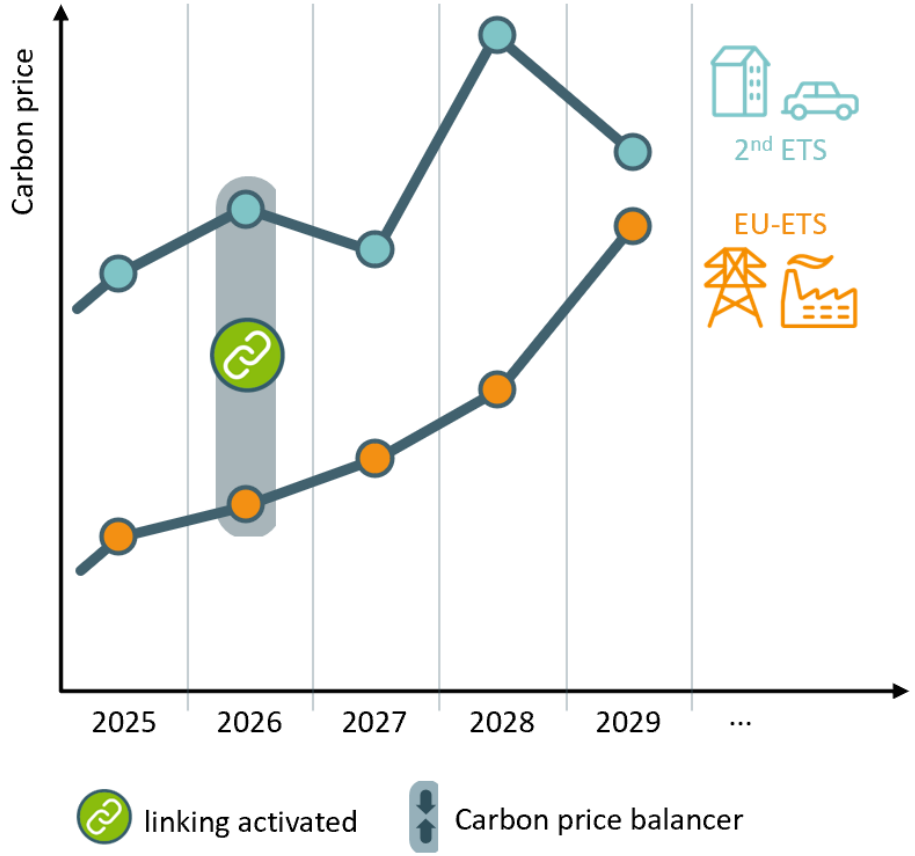
Motivation

- More ambitious targets
- Current architecture insufficient
  - No/very low carbon prices in important sectors
  - High political uncertainty on future pricing
    - Interaction with complementary policies not addressed
  - ESR-targets not sure to deliver
  - Higher and more uncertain marginal abatement cost -> regulation and subsidies will get expensive
- A whole economy carbon-price

First best (universal, credible) carbon price required, but four considerations

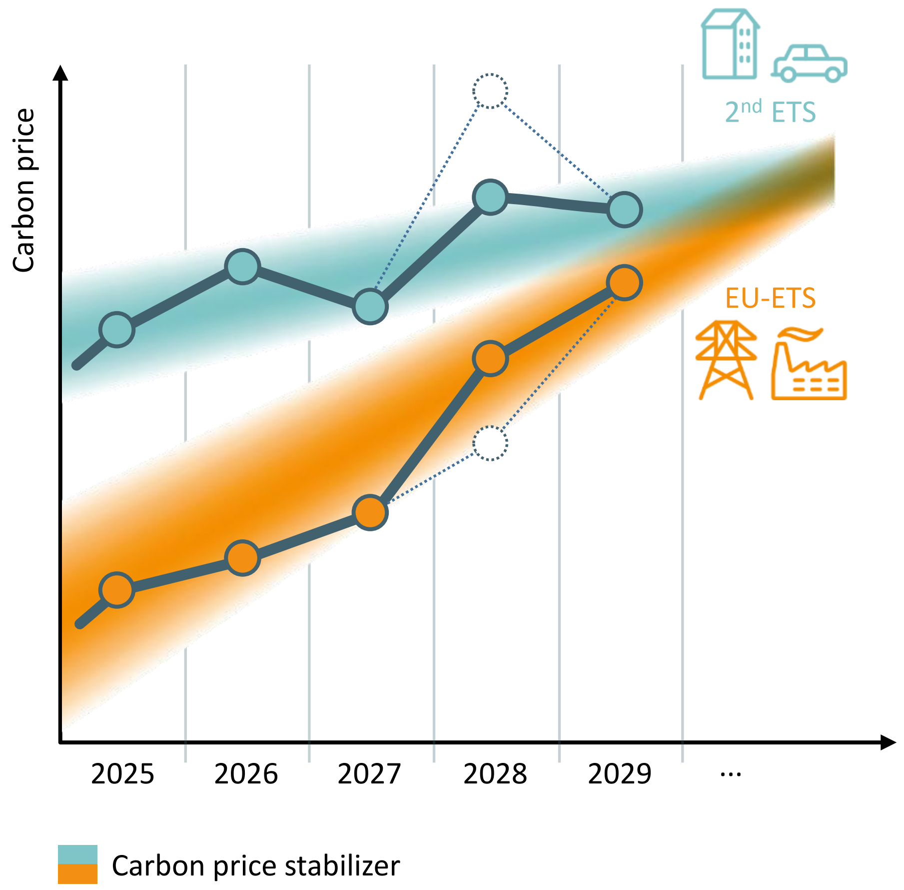
Market readiness	EXISTING ETS took two years of trial phase and continous adjustments since 2007 to mature **->** carbon pricing in very different sectors will also require up to 5 years to be resilient
Competitiveness and social equity concerns	CARBON prices will impact competitiveness of companies and welfare of households -> revenues should be used to help both, but mixing these two issues will be politically difficult
Commitment problem	TODAYS governments cannot credibly commit, that future governments let carbon markets play out irrespective of possibly very low/high prices -> markets *politcally* discount future carbon prices
Other externalities	ONLY based on carbon prices, markets underinvest in new technologies and assets needed for decarbonisation (renovation, green cement, …) due to split-incentives and market barriers

Two ETS with carbon price balancer



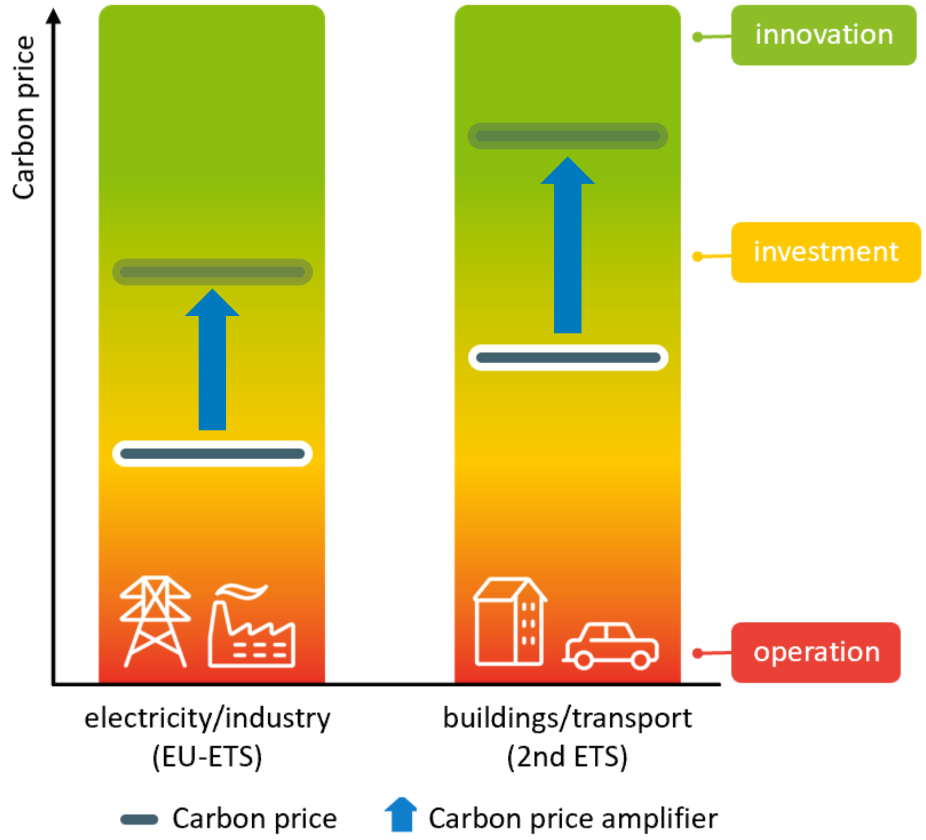
- Start with **two separate ETS**
- Use **carbon price balancer** (linking) to manage price differences between the two systems in the short run

Carbon price stabilizer



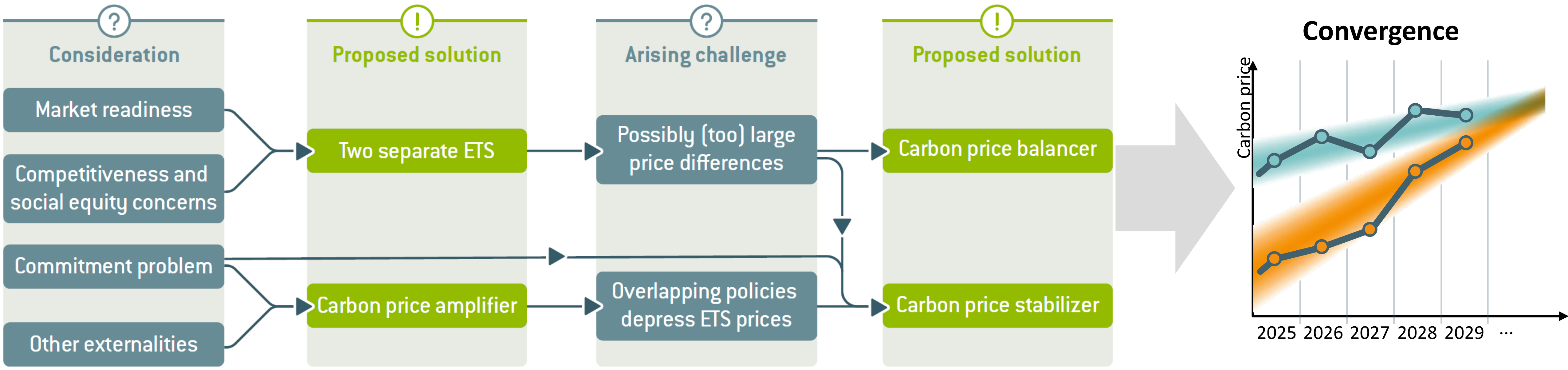
- Build in long-term **convergence**
- Use **carbon price stabilizers** (price collar) to address the commitment problem and ensure price convergence

Carbon price amplifier



- ➢ Trigger fast investment and innovation
- ➢ Use **carbon price amplifiers** (additional policies) to address the commitment problem and other externalities

An architecture to firmly move to a whole-economy carbon price for the EU



Cross-country distributional questions

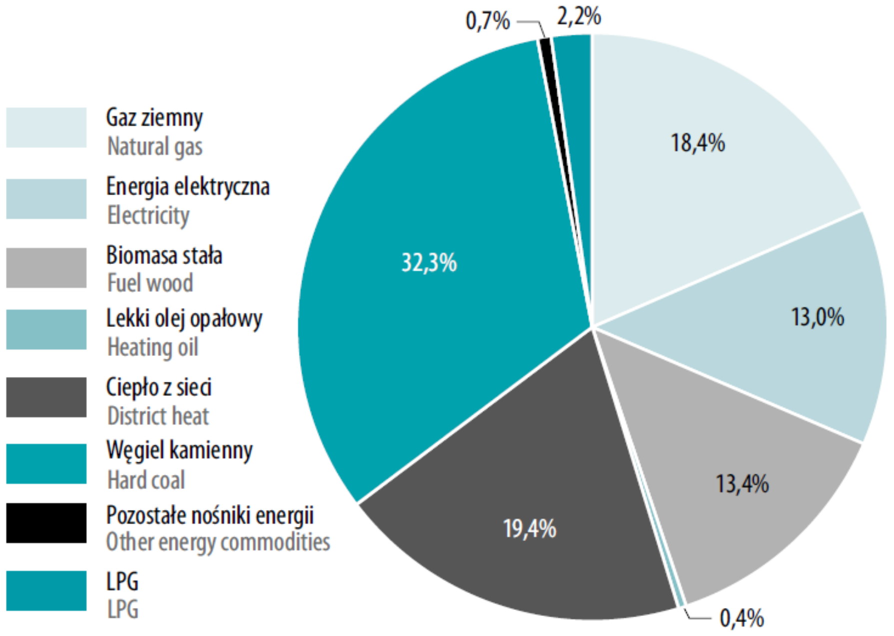
(1) When discussing a reform of the carbon pricing architecture, cross-country distributional effects - such as the one mentioned by Minister Kurtyka – will be key for finding a compromise.

(2) All stakeholders will have strong positions, but there are many different levers that can be used to hammer out a compromise (initial allocation of allowances in both ETS by country; size and structure of EU different funds)

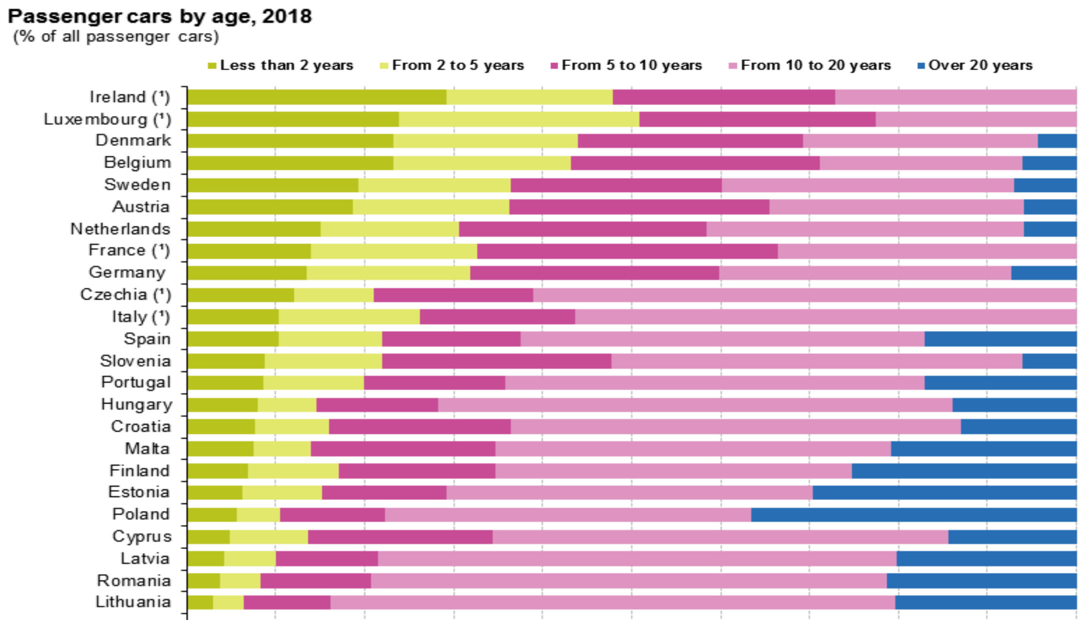
(3) This will possibly need to happen at the highest political level, but needs to be informed by analysis.

Polish transport & heating (buildings) particularly carbon-intensive

Roughly one third of household energy use from hard coal



Highest share of passenger cars over 20 years old in Poland



Principles for fair allocation of allowances?

	Population [Million]	Mean income [1000 EUR]	Emissions Transport [Mt]	Emissions Residential and Commercial [Mt]
Poland	38	7	64	42
Germany	83	23	162	115
France	67	23	131	70

Thank you

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bruegel