CLIMATE ENERGY FINANCE

Submission on Safeguard Mechanism reform: consultation on a proposed design

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Tim Buckley, director, Climate Energy Finance (CEF)

BACKGROUND

Firstly, CEF acknowledges the energy and climate momentum established over the last 8 months in Australia, since the election of the Albanese government. Federally, and in cooperation with the states, Australia has come a long way, and CEF is encouraged about the shifting narrative and policy landscape in Australia. This is not in isolation; internationally, the federal government's action sits in the context of the US IRA, the REPowerEU and EU Net-Zero Industry Act, China's 14th FYP, India's PLI and most recently, the Japanese GX Roadmap. Momentum at the state level is also building the national narrative. The re-election of the Andrews Government in Victoria brings huge momentum on electrifying everything, a Gas Substitution Roadmap and 95% RE by 2035, and the NSW EPA is tasked with regulating carbon emissions across all businesses to align with the 70% emissions reduction by 2035 target Minister Kean announced pre-Xmas.

In the federal policy context, the safeguard mechanism (SGM) and Chubb review of Australian Carbon Credit Units (ACCU) sit alongside the Climate Act, the 82% RE by 2030, the $15bn Reindustrialising Australia Fund, and the progress in critical minerals and EVs. SGM deals with scope 1 emissions, 82% RE by 2030 pertains to scope 2, and these are separate to dealing with our still expanding fossil fuel export industry (scope 3).

It is CEF's view that Australia can leverage and build domestic voter support in middle Australia by showing decarbonisation is good for our economy, regional jobs and exports, and that this narrative shift is well underway.

THE PROPOSED SGM REFORMS

The proposed SGM reforms put industrial emissions (scope 1) on a rapid declining path (although CEF strong recommends the scheme be expanded beyond the top 215 facilities by lowering the threshold to 25,000tpa). Scope 3 exported emissions remains the huge elephant in the room. The Russian war on Ukraine and resulting longer term sanctions presents unique and unprecedented conditions for fossil fuel exports. A priority should be appropriately taxing fossil fuel export war-profits to ensure a meaningful return to Australians from multinationals exploiting our public assets for private profit and to help fund some relief from the energy poverty this war-profiteering inflicts on average Australians; see CEF's August 2022 report on this issue.

The foundational premise of Climate Energy Finance is that financial markets are phenomenally powerful, but they need an explicit, high, permanent price on carbon to drive the rapid decarbonisation pathway required to ensure alignment with a 1.5°C trajectory under the Paris Agreement, which was made politically toxic by the previous government. It is CEF's view that the SGM reforms create a credible framework to re-establish a price on carbon emissions in Australia.

For finance, the direction of policy is key and the SGM reforms set that direction well.

We applaud energy minister Chris Bowen's action to change the landscape by capping the carbon pricing at *just* A$75/t, double where we are today. We further commend the decision to subject the cap to aggressive indexation (CPI +2% annually). The $75/t cap becomes ~$100/t by FY2030. Longer term international linkage to emissions trading schemes (ETS) of integrity would see it go to the EU ETS price today of [€88/t](#) (A$138/t), giving our price another huge boost, again creating the confidence for finance and corporates in Australia that the $75/t price cap is an interim promise, with the long term price likely double that. We support longer term international scheme linkages, if the international schemes have clear and credible integrity, transparency and alignment with the SBTi

We make the following observations on the indexation of the cap (developing David Leitch's work in [Renew Economy](#).

Table 1: The Safeguard Mechanism - A Path to Formal, High Emissions Pricing

	Baseline Mt CO2	Reduction Factor	Annual Reduction %	Reduction Mt CO2 pa	Cummulative Reduction Mt CO2 pa	$m cost Accumulated pa	Annual Increase in total carbon costs	CO2 Price A$/t	Inflation pa	Inflation +2% pa
FY2023	143	100.0%		Nil						
FY2024	136	95.1%	-4.9%	7.0	7	525		75.00		
FY2025	129	90.2%	-5.1%	7.0	14	1,103	110%	78.75	3.0%	5.0%
FY2026	122	85.3%	-5.4%	7.0	21	1,736	58%	82.69	3.0%	5.0%
FY2027	115	80.4%	-5.7%	7.0	28	2,431	40%	86.82	3.0%	5.0%
FY2028	108	75.5%	-6.1%	7.0	35	3,191	31%	91.16	3.0%	5.0%
FY2029	101	70.6%	-6.5%	7.0	42	4,020	26%	95.72	3.0%	5.0%
FY2030	94	65.7%	-6.9%	7.0	49	4,925	23%	100.51	3.0%	5.0%
FY2031	87	62.4%	-5.0%	4.3	53	5,630	14%	105.53	3.0%	5.0%
FY2032	80	59.2%	-5.3%	4.2	58	6,378	13%	110.81	3.0%	5.0%
FY2033	73	55.9%	-5.6%	4.1	62	7,168	12%	116.35	3.0%	5.0%
FY2034	66	52.6%	-5.9%	3.9	65	8,001	12%	122.17	3.0%	5.0%
FY2035	59	49.3%	-6.2%	3.7	69	8,873	11%	128.28	3.0%	5.0%
FY2036	52	46.0%	-6.7%	3.5	73	9,784	10%	134.69	3.0%	5.0%

** CEF assumes long term inflation is 3.0% pa.*

Firstly, our reading is the -4.9% pa is a FY2024 impact. The SGM reform proposes a 7Mtpa reduction which is -4.9% in FY2024, but this is not a fixed % off a reducing base. We estimate a **CAGR of -5.8%** from FY2024 to FY2030.

Secondly, depending upon inflation (CEF assumes a reversion to 3% pa) the power of compounding means **$75/t becomes $100/t by 2030 and $128 by 2035**. That is a seriously positive trajectory that finance can now bank on, particularly relative to the uncertain ~$30-35/t we had just a month ago. Finance will extrapolate this rate of change, and won't wait a decade to act. This will get built into decisions immediately, with growing confidence as the legislation and regulations solidify. We strongly endorse the CPI +2% pa framework, that is excellent to see.

Thirdly, we acknowledge the 215 facilities will use offsets initially; from a standing start, they can't move collectively that quickly after a decade of going backwards. But if they all use offsets and do nothing, by 2030 the annual cost of collectively doing so will be **$4.9bn**. Annually, because the emission reduction of 7Mtpa is cumulative, and the price goes up each year. Working in conjunction with the public funding support of the Powering the Regions Fund (which we endorse, but we also note the clear need for real time transparency on this significant use of taxpayer funds), this provides a massive positive incentive for industry to acknowledge the massive cost to Australians and our environment of excessive carbon emissions, and act to sustainably reduce their scope 1 emissions permanently at the necessary speed, in alignment with the SBTi.

Fourth, getting an **Australian CBAM** proposal into discussion is a really important new step forward to encourage global action and to show Australia will now belatedly play a constructive leadership role. It is also in the context of the accelerating climate and energy decarbonisation trends globally.

Fifth, we are strongly encouraged by the cumulative budget for total emissions of no more than 1,233Mt of CO2-e in total between 2021 and 2030, and the 100Mtpa target for FY2030. We need real time transparency on how we are tracking on these key national targets.

We note it is important that this be clearly mandated and enforced, and ideally legislated.

CEF suggests that the optimum timing for a review would be in 2026 with implementation effective 1 July 2027, so the SGM isn't a political football going into the next election. Our hope is that the next election presents the government with an even stronger climate mandate, consistent with climate science and underpinned by the progress by our trade partners.

CONCLUSION

The proof of the SGM will be in the delivery and integrity, as with the implementation of the outcomes of the ACCU review.

We note that interplay of the SGM with ACCUs is critical. On that front, CEF argues that we should have a retrospective review of phantom ACCUs issued without substance, and more public disclosure and transparency of how we effectively address the key issues raised by Professor Andrew Macintosh. Trust and credibility need to be earned.

While the ACCU review might understate the distrust and abuses of ACCUs enabled by the Coalition, we applaud the fact that it does recommend strong improvements in transparency and integrity, e.g. an independent integrity review committee, and the abolition of new credits for "avoided deforestation", where bogus credits were applied to land which would not have been cleared.

In conclusion, the SGM could be significantly stronger, but it does deliver a number of positive steps Australia urgently needs, given the lost decade of chaos and inaction of the previous government. CEF's view is that Australia needs to move forward. We see the complementary SGM and ACCU reforms as a very important step, one of many the Federal government is taking in concert with the States – real actions which together build a stronger community consensus.

After a decade of going backwards, strong corporate momentum needs to be built, and this won't happen overnight. Climate Energy Finance considers the proposed SGM reforms a key driver of that momentum.

Note: please refer also to our previous submission on the SGM reforms.

ABOUT CEF AND TIM BUCKLEY

Climate Energy Finance (CEF) is an Australian based, Australian funded think tank established in 2022 that works pro-bono in the public interest on mobilising capital at the scale needed to accelerate decarbonisation consistent with the climate science. We conduct research and analyses on global financial issues related to the global energy transition, as well as the implications for the Australian economy, with a key focus on the threats and opportunities for Australian investment, regional employment and value-added exports. Beyond Australia, CEF's geographic focus is the greater Asian region as the priority destination for Australian exports, particularly India and China. CEF also examines convergence of technology trends in power, transport, mining and industry in accelerating decarbonisation. CEF is independent, non-partisan, works with partners in the corporate and finance sector, NGOs, government, and progressive social and climate movement organisations in Australia, and is philanthropically funded.

Tim Buckley, CEF's founder and director, has 35 years of financial market experience covering the Australian, Asian and global equity markets. Tim founded the Australia and Asian arms of the Institute for Energy Economics and Financial Analysis in 2013 and worked as the Australasian Director on the global energy transition for eight years till the start of 2022.

Prior to this, Tim was a top-rated Equity Research Analyst, including Head of Equity Research in Singapore at Deutsche Bank, Managing Director, Head of Equity Research at Citigroup for 17 years, Head of Institutional Equities at Shaw & Partners and co-Managing Director of Arkx Investment Management P/L, a global listed clean energy investment start-up jointly owned with Westpac Banking Group.

Contact: Tim Buckley, director, CEF. tim@climateenergyfinance.org