

29 February 2008

Secretariat  
Finance and Expenditure Committee  
Parliament House  
Wellington

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Dear Madam

## **Submission on the Climate Change (Emissions Trading and Renewable Preference) Bill**

### **Background**

The New Zealand Manufacturers and Exporters Association (NZMEA) represents the interests of manufacturers and exporters throughout New Zealand.

The NZMEA is New Zealand's only focused, independent voice for manufacturers and exporters. NZMEA members make over \$2.0 billion in sales and have an export value of around \$1.0 billion. The Association can trace its beginning to the early history of New Zealand. As a legacy of the hard work and careful financial management of the past, we have a significant asset base that enables our independence and extends our activity.

The NZMEA is independent; we do not seek or receive funding from local or central government. We are not associated to any other business group.

The health of the elaborately transformed manufactures, particularly, and exporters generally, acts as the "canary in the coalmine", indicating the long-term prospects for our whole economy. In a similar way, the health and development of our smaller companies has a major role to play in the development of the New Zealand economy.

Elaborately transformed manufactures comprise over 30% of New Zealand tradeable exports, with sector sales totaling over \$30 billion, and total national employment numbers of around 170,000. New Zealand manufacturers face the ever-increasing onslaught of the cost of local regulation and global competition from low cost countries, without any real support from the policy framework.

The historical reliance that New Zealand has placed in the primary sector and basic manufactured goods has seen New Zealand slip down the rankings of the Organisation of Economic Co-operation and Development (OECD) from 5<sup>th</sup> in 1950 to 21<sup>st</sup> in 2005, between Spain and Greece, well into the lower middle bracket of global income per capita. New Zealand has grown more slowly than other countries due to the dependence on the primary sector. The manufactured goods sector of the internationally traded economy has grown much faster.

**The NZMEA does wish to speak on this Bill at a Select Committee hearing.**

## **General Comment**

The NZMEA recognises the need to address carbon issues. However if an NZ ETS adds to the loss of activity overseas sources that discharge a higher level of carbon emission than our local practice, Green House Gas (GHG) emissions in New Zealand will be replaced by higher emissions elsewhere. Such a process, of course, does nothing to reduce GHG emissions and any consequential global warming.

The key issue is trade. Done well, and that probably means done second, the NZ ETS will not erode the competitive position of the tradable sector in New Zealand. The total GHG loading of our economy has two components; those emissions generated by activity in New Zealand, and those “embedded” in tradeable imports.

Unless both are addressed in an equitable manner, all that will happen is that the NZ ETS will disadvantage local producers to the advantage of our international competitors and potentially greater GHG emissions.

The sustainability of New Zealand's elaborately transformed manufacturing sector is already on a knife-edge. The ETS has the potential to make things much worse, and there is little or no capacity to absorb additional cost increases that our competitors avoid.

Large economies with falling populations, a high dependence on fossil fuel for electricity generation, and a committed and growing nuclear generation programme will carry the advantage of the “global” emissions trading as currently envisioned. At the loser end of the spectrum will be small economies, with growing populations, the one with a complete ban on nuclear development, and an existing high level of renewable electricity generation. When the two are combined in the same ETS, the economic benefit transfers are obvious, and far from neutral. We believe this is something best avoided if New Zealand is to remain a developed economy.

## **Aspects of the Bill that need to be changed:**

**New Zealand does not need to try and win the race for the most ambitious ETS in the world.**

If trade is not to be damaged and emissions simply moved offshore, we must follow our trade competitors, not lead them. Tradeables compete on a daily basis with the most competitive and capable competitors in regard to better design, scale economies and lower costs. New Zealand manufacturers and exporters struggle against scale and cost economies now; adding a carbon differential will simply make this worse. New Zealand should avoid ETS until:

- Competitiveness issues must be balanced for our tradable sector, including disincentives for the import of “embedded” carbon.
- All New Zealand's trading competitors face similar costs.
- An effective global market has matured and stabilised.

**Energy intensive industries are likely to be disproportionately affected by the price of carbon, making them less competitive in international markets, and encouraging emission transfers to other countries, potentially with an increase of carbon emissions.**

- New Zealand's trade exposed industry should be evaluated on emissions intensity measured against 'world's best practice', for firms or products, when it comes to the free allocation of credits. Much of the work has already been done with New Zealand's largest firms to establish Worlds Best Practice under the previous NGA policy and this work should be revived.
- Free allocation of credits should not be phased out in a linear fashion, despite what other countries are doing, but should be reduced as trading competitors take similar action in pricing carbon emissions.
- At a minimum, legislation should ensure all trade-exposed industry is on a level playing field with the same sectors anywhere in the world. This requires a cautious approach to exposing tradeables to a price of carbon ahead of countries they compete with.
- Any ETS regulation should not disincentivise new investment in New Zealand, so there needs to be provision of free allocation of NZU's for new entrants.

**The price of carbon is high and volatile.**

The tradable sector in New Zealand battles with the volatility of exchange rates driven by local policy and global speculation. An infant, politically driven ETS, has the prospect of adding another uncertainty that could cause significant economic harm. Having a local "safety valve" to limit the price and price fluctuation of carbon is necessary to protect the competitiveness of New Zealand tradeables.

**Proposals in the Bill beyond 2012 are inadequate.**

The provision (Part 1 Clause 43, section 146) that says if there is no future in the Kyoto Protocol agreement, or successor agreement to the Kyoto Protocol, then the NZ ETS will continue regardless of what other countries are doing, seems pointless. New Zealand's emissions are a small part of the global carbon loading, what practical purpose is served by going it alone?

- This default provision should be removed from the Bill. Future negotiations regarding the post 2012 position will produce a clearer direction, again, there is no need to rush, we need only keep pace with, or follow our trading competitors.

**Too much of importance is being left to regulation.**

The changes proposed have the potential to severely impact the tradable sector, equal to that of the World Trade Organisation (WTO) agreements. These tariff, quota and technical access matters have taken years to develop and remain far from balanced and equitable from the view of many firms in New Zealand. Firms that are likely to face the full costs of emissions trading should have the right to make submissions to a full Parliamentary Select Committee on the impacts the NZU allocation plans will have on their business. That cannot be done at the moment.

- Defer the passage of the Bill until such time as the detailed work has been done to move all the substantive issues into the Bill.

## **Drafting of the Bill.**

The Bill, as published, is hard to read, and continuity and flow are compromised by use of extensive cross-referencing to other Acts. As already mentioned, done badly, a NZ ETS has the capacity to severely impact the New Zealand tradable sector without doing much to reduce global carbon emissions – the worst of both worlds.

Public debate and discussion on ETS is vitally important, a higher clarity of drafting would better support effective discussion and debate.

## **Members' comments.**

A number of other comments were made by our members that were more general in nature:

- Why does the NZ ETS envisage rejecting credits created by nuclear generation? We cannot seek to impose local nuclear free policy on others. A carbon credit is a carbon credit; if others adopt such idiosyncratic local exceptions the international ETS will be meaningless.
- If we try to lead the world in an ETS we will do next to nothing to influence global GHG emissions; we will however inflict yet more competitive disadvantage on our tradable sector.
- There are worries about global warming, but whatever New Zealand does will make no material difference one way or the other.
- It is hard enough to be competitive today with an overvalued exchange rate and the highest cost of capital in the developed world; this is likely to be just another nail in the coffin of our competitiveness.
- Manufactured goods increasingly flow from the developed world, and unless their emissions of carbon fall, then shifting production from New Zealand to the developing world will increase total carbon emissions. That would be a perverse outcome of any policy aimed at GHG emissions.

In summary, we do not need to rush. If an international ETS is established, and it is effective, New Zealand can join at that point, and if GHG really is driving climate change then that change will be ameliorated to our benefit. If, on the other hand, an international ETS fails, and GHG is really driving climate change, we would be better to spend on the mitigation of climate change effects and not sacrifice competitiveness or waste resources on a failed scheme.

Yours sincerely



**John Walley**  
**Chief Executive**