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Can Bali successfully replace Kyoto?

At Bali, the question will be by how much China should reduce greenhouse gas emissions

By IVAN PNG

OVER 10,000 delegates from all over the world are converging on Bali, Indonesia, for the United Nations Climate Change Conference. For twelve days, representatives of over 180 countries will negotiate a greenhouse gas policy to succeed the Kyoto Protocol.

By the Kyoto Protocol, most developed countries have committed to reduce greenhouse gas emissions by at least 5 per cent relative to 1990 levels. The commitment period lasts from 2008 to 2012. The Protocol exempted less developed countries, including the world's second-largest emitter of greenhouse gases - China - from target reductions. Among developed countries, two holdouts - Australia and the United States - refused to ratify the Kyoto Protocol.

US President Bush was long hostile to the Kyoto Protocol. He seems to have adjusted his position, perhaps responding to a popular groundswell, driven in part by Al Gore's movie, *An Inconvenient Truth*. The United States appears to have, grudgingly, agreed to negotiations over new targets for greenhouse gas emissions.

In last week's general elections, John Howard, prime minister of Australia since 1996, was trounced by the Labour Party. To add insult to injury, Mr Howard even lost his own seat. Labour made climate change a key issue in the election. Incoming prime minister, Kevin Rudd, has initiated the process to ratify the Kyoto Protocol. He will attend the Bali conference.

So, in Bali, all eyes will be on China and other developing countries. On current trends, China will soon surpass the United States as the world's top emitter of greenhouse gases.

China is aware of the spotlight. In June, prior to President Hu Jintao's meeting with the G-8 leaders, China unveiled its climate-change plan. The plan aims to reduce the energy intensity of economic production by 4 per cent annually between 2005 and 2010.

However, China's government stressed that its top priority remained 'sustainable development and poverty eradication'. This is not surprising considering the widening urban-rural gap and when over 100 million people struggle on less than US\$1 per day.

Moreover, China considers that, as a developing country, it is not obliged to cut emissions. Rather, the responsibility rests with the developed countries.

Nevertheless, China is making some progress on climate change. In 2006, energy intensity fell by 1.2 per cent, far short of the 4 per cent target. However, in the first nine months of this year, energy intensity fell by 3 per cent.

At Bali, the question will be by how much China should reduce greenhouse gas emissions. Critics emphasise that China's emissions will soon be the world's highest. However, Chinese officials respond that, on a per-capita basis, emissions are low.

The simplest answer would be a market solution - to establish a global price for emissions. The acceptable level of greenhouse gas emissions is just like the consumption of any scarce resource, whether it be alumina, iron, soybeans, or wheat.

China, India, and other developing countries pay international market prices for minerals and grains. They should do the same for greenhouse gas emissions.

Multi-lateral government negotiations over China's emissions would make no more sense than multi-lateral government negotiations over China's consumption of iron ore or soybeans.

There are no multi-lateral government negotiations to allocate scarce resources of iron ore or soybeans. Rather, China buys minerals, grains, and other primary products on global markets. Free market forces ensure that all countries - developing and developed - use the appropriate quantities of these resources.

What if some countries - whether developing or developed - refuse to implement pricing of greenhouse gas emissions? Under such circumstances, it would be appropriate to levy a countervailing tariff on imports from such countries to compensate for the unpriced emissions. This would ensure a level playing field in international trade.

President Nicolas Sarkozy of France visited Beijing last week. He warned that Europe might impose a greenhouse gas emissions tariff if China did not adopt an acceptable emissions policy.

Would such a 'carbon tariff' be an unwarranted interference with free trade? That free trade increases overall welfare is one of the most celebrated propositions in economics.

However, the free trade proposition assumes that there are no externalities. Greenhouse gas emissions are a negative externality.

Emissions from China and other developing countries affect the worldwide climate. They cause global warming, not local warming.

Almost as celebrated a proposition in economics is that externalities must be corrected, or else, they would be excessive. Accordingly, it is entirely reasonable to correct the international externality through a countervailing import tariff.

Incidentally, I will not travel to Bali, and by doing so, I make my contribution to reducing greenhouse gas emissions. The convenors of the Bali conference are making their contribution as well - to save on air-conditioning, all delegates are encouraged to dress casually. Every gram counts.

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