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By Nick Main and Joseph Stanislaw

Copenhagen: Political realities to the fore, business leaders wait

Recent developments from the Asia Pacific Economic Cooperation meeting in Singapore—the agreement to delay the deadline for the agreement on carbon reduction targets previously set for the 15th Conference of the Parties (COP15) December meeting in Copenhagen, and the dramatic trip to Singapore (the last major leaders meeting before Copenhagen) by Danish Prime Minister Lars Lokke Rasmussen—may have left business leaders wondering what they should expect from the current round of climate negotiations. But these developments are not surprising.

Why a change of course?

The United Nations climate change conference in Bali, Indonesia, 2007, set the agenda for today's reality:

- The target date was generally viewed as too aggressive.
- More time was needed for that many countries and different interest groups to come to a conclusion.
- The matters to be resolved were too complex.
- There was no obvious strong political will for agreement.

But in the past year there has been much change in the political environment. The United States has voted in an administration with a different perspective on these issues. And, no less important, China is more engaged and is showing leadership.

For China and the United States, the new reality is clear. They are the largest emitters of greenhouse gasses and the largest users of coal in the world. They both have very large solar and wind energy plays. There will be an increasing focus on these two countries.

The framework evolves

So what is expected from Copenhagen and can Danish government's vision of "one Agreement—two purposes" be met? Here are some considerations:

- There will likely still be concerted action at a political level to set a broad framework for allocating load-sharing responsibilities among the developed, the developing, and the undeveloped world and between countries.
- There is also likely to be greater clarity about what those commitments would be at a country level. Remember that this commitment will be difficult to achieve, as there is competitive advantage to be gained, and the tendency exists to try to "game" the system.
- The miasma surrounding the negotiation by officials will likely be cleared, if there is strong instruction from the political leaders. The position today after two years of negotiation—where the "square brackets" of not-agreed clauses are so complex no one truly knows what they all mean, and they are reduced to producing non-papers—is not satisfactory.

So the two purposes—solid content for all the building blocks of the Bali agreement, which can be a foundation for the later legal agreement, and the provision for immediate action, mainly around capacity building, technology cooperation, early mitigation, and adaptation – can be met. The challenge will be to go from the framework to delivery.

The developing country voice

China is the lead voice for developing countries. It is coming on strong on alternatives, renewable, and efficiency—emphasizing its solar and wind programs (already, China has stricter Corporate Average Fuel Economy standards than the United States). Clearly, China sees this as an area of future global competitive advantage, and it will own the intellectual property as well as the low-cost manufacturing base when it exports these products.

However, China is unlikely to be able to reduce carbon in absolute terms for at least a decade. Rather, it will reduce carbon emissions relative to gross national product. That is not to say that it does not understand the role that markets can play in reducing emissions and that restrictions are needed to make markets work; it's just the nature of those restrictions is likely to be different. Expect to see a "grace period" for developing countries before they have to commit to absolute reductions. There is a precedent for such treatment in the Montreal Protocol on substances that deplete the ozone layer.

In other words, China is taking a muscular role in climate change but within more flexible criteria than the West. Other developing countries will probably follow China and, increasingly, India's lead.

The developed country dilemma

The main question for the United States is: Will the U.S. "walk the talk"? The Obama administration will likely say that "we are trying to pass legislation, and, in any case, we are deputizing the Environmental Protection Agency to deliver change in U.S. businesses."

The recent deferral of the U.S. Senate climate change bill, while reflecting the national reality, means the next steps in the process are not a single meeting but a round of meetings. It is unlikely that the United States will sign up to a commitment on which it does not think it can deliver, so the passage of that bill and any eventual passing of legislation will be a fundamental prerequisite to any agreement.

Interestingly, the United States and China—the new G2—will mirror each other when it comes to climate change policy.

Europe, for its part, will continue to play a strong hand and maintain a strident tone. The European view is that its countries lead in emissions reduction regulation, have been managing down their emissions profile, and will continue to do so. The stated intention is to continue this policy direction despite what happens at Copenhagen, with a constant threat of border adjustments and out-of-border policy encroachment (consider air travel).

The agenda for the developing world

Here are three areas for development at COP15:

- There will likely be considerable focus on the clean development mechanism as a method of both reducing the pain of transition for developed countries and benefiting developing and undeveloped countries on a different path to low carbon growth.
- Expect some considerable emphasis on this clean development paradigm and a reduction in the emphasis on immediate developed country reductions.
- Expect a significant emphasis on forestry issues and agricultural sequestration and emissions avoidance. Forestry credits have been in existence for some time but are not recognized in the European Emissions Trading Scheme, the major buyer of clean development mechanism credits. This may change with a focus on not just sequestration credits but also on REDD credits—credits from reduced emissions from deforestation and forest degradation. With 20 percent of global emissions arising from deforestation, this is expected to be an important conference debate.

Expected outcomes

So what will be the end result? The following is highly likely:

- Copenhagen attendees will structure a second round of talks and use Copenhagen as a mere starting point. There will be some high-level agreement on what burden different countries may bear.
- The conference will be declared a success if attendees can create a broad framework for managing climate change with general benchmarks—something similar to the way the International Energy Agency handled oil issues in the 1970s.
- China will emerge as the leader of the developing country voice with India not far behind. There will be a grace period before developing countries are required to meet absolute reduction targets similar to those of the developed world.
- There will be wide agreement on an extended clean development mechanism (or equivalent). Forestry and agriculture credits will play a strong role.
- There may also be a consensus on carbon pricing.

And for business?

The reality is that a price on carbon is being put into the equation. If COP15 *bis* gives rise to binding agreements on significant emissions reduction, then prepare for this to be reflected in country systems. It is likely that this will result in the following:

- The cost of emissions will go up.
- Investment decisions will be reappraised.
- Reducing carbon intensity will become a strategic imperative.
- Competitive advantage will need to be reconsidered.

It is a whole new framework of risk and opportunity.

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