Europe's Economic Recovery – Climate Neutral, Fair and Innovative

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Key messages

The Corona crisis offers three important lessons for climate policies and Europe's economic recovery. First, systemic shocks – like the Corona pandemic or climate change – affect the foundations of modern societies, exposing in a drastic way their vulnerability and unpreparedness. Second, resiliency, preparedness and time are existential factors in addressing systemic crises. To respond to climate change in a resilient and prepared way, all countries, including the EU, must accelerate their emission reductions drastically – in the near term until 2030 as well as in the long term until 2050. At the same time, they need to be better prepared for the consequences of climate change, which are partly already unavoidable. Third, the world's economic recovery must help build efficient, innovative and climate neutral economies, while supporting the poor and protecting the vulnerable. Calls to delay climate policies draw the wrong lessons from the current crisis and undermine Europe's economic recovery.

About this paper

This paper is part of the project "Building bridges — High Trust Network with Conservative Groups for Ambitious Climate Action", funded by the European Climate Initiative (EUKI).[1] The project aims at facilitating dialogues on climate policies between conservative and other groups from Hungary, Poland and Germany.

The role of climate policy in Europe's economic recovery

In the matter of a few weeks, the coronavirus has upended the world's operating assumptions. The virus forced us into a world that was unthinkable only a few months ago; it showed drastically that even the basics of societies are not for granted. The fabric of human societies – schools, work places, transportation and day-to-day human interactions – is now under severe stress. The virus interrupted global supply chains with serious knock-on effects across the world. Tourism came to a complete standstill. In consequence, the world is possibly looking at the biggest economic crisis since the great depression. The European Commission expects that the EU's GDP will decrease by more than 7 % in 2020, the biggest drop in its history.

In the face of the looming economic crisis, there are calls to delay climate policies. Cash-strapped companies are claimed not to be able to afford the investments required to make their operations climate neutral. These calls, however, draw the wrong lessons from the current crisis and

[1] Opinions expressed in this paper represent the views of the authors and do not necessarily represent the position of the European Climate Initiative. For further information, please contact nils.meyer-ohlendorf@ecologic.eu.

undermine Europe's economic recovery. Instead of delays, building efficient, innovative and climate neutral economies offers crucial opportunities for Europe's economic recovery[2], which should take center stage in the EU's economic recovery – for the following reasons:

1. **Resiliency, preparedness and – correspondingly – time**. In a drastic way, the Corona crisis made clear the existential importance of resiliency, preparedness and time. In the face of the pandemic, countries that were well prepared and acted swiftly have fared better than those that were unprepared and/or delayed action.

   The same lesson holds for the climate crisis – resiliency against climate change entails necessary immediate and drastic emission reductions and robust adaptation. Like in any exponential crises, time is an existential factor. Underlining the importance of time, UNEP estimated that if serious global emission reductions to meet the projected emission levels for the 2°C and 1.5°C would only have been 0.7 % and 3.3 % annually if serious emission reductions had begun in 2010. As this did not happen, required annual reductions increased drastically to 2.7 % in 2020 for the 2°C goal and 7.6 % on average for the 1.5°C goal. Crucially, further delays will require even greater cuts.[3]

2. **Vulnerability**. The Corona virus revealed the vulnerability of societies and economies to systemic shocks, i.e. shocks that hit a society's very foundation. The climate crisis is a similar systemic shock in that it affects the basic living conditions – weather, water, soil or biodiversity and – as a consequence – habitable land, food production or health.[4] Both crises affect disproportionally vulnerable groups – the poor and the sick. In this regard, the current pandemic is a foretaste of what a full-fledged climate crisis could entail.[5]

3. **Economic autonomy**. The EU's roadmap for recovery states that the Covid-19 pandemic has shown the "pressing need to produce critical goods in Europe, to invest in strategic value chains and to reduce over-dependency on third countries in these areas."[6] A circular economy – a key element of effective climate policies – will help make Europe more resilient and less dependent on imports. The decarbonization of European economies will also help to reduce Europe's dependency on coal, oil and gas imports. Increasing Europe's economic autonomy in this way does not, in any sense, mean scaling back global trade and globalization significantly but primarily to make Europe more resilient to systemic shocks.

4. **Financial resiliency:** The Corona crisis has shown that Environmental, Social and Governance stocks (ESG stocks) are particularly resilient. In the midst of the crisis, ESG-linked indexes outperform regular stock indexes, including S&P 500 or MSCI World Stock

[2] Along similar lines, the EU's "Roadmap for recovery", which the Presidents of the European Council and the European Council drafted and the European Council welcomed on 21 April 2020: "The Green transition and the Digital transformation will play a central and priority role in relaunching and modernising our economy"; https://www.consilium.europa.eu/media/43384/roadmap-for-recovery-final-21-04-2020.pdf, p. 3.

[3] UNEP, Emissions Gap Report 2019, 26 November 2019, https://www.unenvironment.org/resources/emissions-gap-report-2019.

[4] The impacts of the climate crisis on human society has many facets – ranging from increased frequency of extreme weather events to raising sea levels– but it also a health crisis. Infectious diseases such as West Nile, Dengue and Chikungunya fever could spread. Higher temperatures favor the spread of the hantaviruses. In the 2003 heat wave, an estimated 70,000 people died in Europe alone. In 2015, 8.8 million people worldwide (790.000 in Europe) died prematurely due to high air pollution - primarily caused by the combustion of coal, oil and gas (https://www.sciencedaily.com/releases/2019/03/190312075933.htm).

[5] McKinsey (2020), Addressing climate change in a post-pandemic world, https://www.mckinsey.com/business-functions/sustainability/our-insights/addressing-climate-change-in-a-post-pandemic-world [07.05.2020].

[6] Recovery roadmap (see footnote 1), p.3.

index[7]. In consequence, it is in investors' own interests to continue investing into companies that are swiftly making their operations climate neutral, while policy-makers should strengthen incentives and regulatory frameworks. The Commission's 'Sustainable Finance' package[8] is one of the priorities in this field.

5. **Competitiveness**. With accelerating climate change and a growing number of businesses depending on efforts to decarbonize economies, it is clear that the energy supply of the future will be efficient and renewable. This trend will continue, regardless of the Corona crisis. To maintain first-mover advantages and to secure one of the most important markets of the future, investments in clean and digital technologies, capacities as well as in the circular economy should be at the heart of Europe's economic recovery.[9] It is noteworthy that renewables are expected to be the only energy source that will grow in 2020, thanks to its low operating costs and priority grid access, while fossil fuel consumption is set to decrease drastically.[10]

Against this backdrop, the EU is discussing reforms of its climate policies and targets, as contained in the communication for a European Green Deal (EGD) and the proposal for a European Climate Law (ECL).[11] While the agreed target of achieving climate neutrality by 2050 remains largely uncontested among Member States, discussions on increasing the EU's 2030 target are ongoing. Partly in view of the Corona crisis, ministers of environment from 18 Member States support a higher target of 50 – 55 %[12], while other Member States call for maintaining the current target. The rapporteur of the European Parliament on the European Climate Law proposes reductions of 65 % by 2030.

Depending on various assumptions, the IPCC estimates that keeping the average increase of global temperatures below 1.5°C would require limiting all future net emissions of carbon dioxide from 2018 onward to around 570 Gt globally.[13] With current emission levels, the world would exceed the 570-Gt in 2031.[14] In light of this scientific evidence, Nationally Determined Contributions (NDC) submitted by countries are insufficient to implement the Paris Agreement. Although higher than other countries, the EU's current target for 2030 also constitutes an insufficient contribution. The exact increase of the current target will be agreed during the legislative process on the European Climate Law and the NDC update.

Agreeing on ambitious targets now is even more important as some of the consequences of the current economic crisis could weaken climate action in the long-term. Oversupply of oil resulting in

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[7] FT, *ESG funds continue to outperform wider market*, https://www.ft.com/content/46bb05a9-23b2-4958-888a-c3e614d75199; Bloomberg, *ESG Stock Resilience is Paving the Way for a Surge in the Popularity*, https://www.bloomberg.com/news/articles/2020-03-31/esg-stock-resilance-is-paving-the-way-for-a-surge-in-popularity?sref=nQW7ZNrq.

[8] https://ec.europa.eu/info/business-economy-euro/banking-and-finance/sustainable-finance_pl.

[9] Recovery roadmap, p. 3.

[10] International Energy Agency, Global Energy Review 2020 The impacts of the COVID-19 crisis on global energy demand and CO2 emissionshttps://www.iea.org/reports/global-energy-review-2020, https://www.iea.org/reports/global-energy-review-2020

[11] Communication from the European Commission Brussels, The European Green Deal,11.12.2019, COM(2019) 640 final and Proposal for a Regulation establishing the framework for achieving climate neutrality and amending Regulation (EU) 2018/1999 (European Climate Law), Brussels, 4.3.2020 COM(2020) 80 final2020/0036 (COD).

[12] https://www.climatechangenews.com/2020/04/09/european-green-deal-must-central-resilient-recovery-covid-19/.

[13] IPCC, Special Report: Global Warming of 1.5 ºC, Summary for Policymakers, https://www.ipcc.ch/sr15/chapter/spm/.

[14] McKinsey Quarterly: Climate math: What a 1.5-degree pathway would take https://www.mckinsey.com/business-functions/sustainability/our-insights/climate-math-what-a-1-point-5-degree-pathway-would-take?cid=climate-eml-alt-mcq-mck&hlkid=75cd74e4c36b4fbc8ee4f50d808bbc96&hctky=11929502&hdpid=f93fd3a0-3585-44b1-be49-c0ece38169e3.

low prices may hinder the shift to renewable energy as has already been the case in the 1980s and early 2000s. The fall in industrial production leaves more emissions allowances in the market, weakening incentives to reduce emissions. Finally, ECB's corporate asset purchases have been recently reported to target mainly 'brown bonds' which can negatively affect the competitiveness of greener companies.[15] ECB's monetary policy strategy review should address this problem.

Funding the green recovery and investments

It is a great challenge to fund the required investments in the midst of a deep economic crisis, where many companies struggle to survive and public budgets will very soon be strained. However, this challenge can be overcome. In fact, it can be turned into an opportunity for advancing climate protection while building a more competitive and resilient economy:

- **Private investments:** As climate protection is already integrated into the business model of many companies, they will continue to be engaged in building a climate neutral economy. Zero interest rates for the foreseeable future will continue to support this engagement. The Institutional Investors Group on Climate Change (IIGCC) – a group of global investors responsible for the management of trillions of dollars in assets – stated that institutional investors will continue to stay engaged because of their long-term view of value and returns.[16]
- **Economic stimulus programs:** EU Member States have wide discretion in designing their stimulus packages but recovery packages should devote large portions to climate change, resiliency and innovation. EU funding mechanisms, in particular the new Multiannual Financial Framework and the forthcoming EU Recovery Facility, should forcefully support this focus of investment. The Energy Transitions Commission – a coalition of leaders from global organizations across the energy, industry, finance and civil society sectors[17] – recommended economic stimulus packages that
  - invest massively in renewable power systems,
  - boost the construction sector via green buildings and green infrastructure,
  - support the automotive sector while pursuing clean air,
  - provide government support to businesses conditional to climate commitments,
  - targeted support to innovative low-carbon activities,
  - accelerate the transition of the fossil fuels industry and
  - avoid spiraling down carbon pricing and regulations.[18]
- **Not regressive:** Energy transition support mechanisms that mitigate climate change and support the EU economy should not contribute to another serious problem - growing economic

[15] https://www.bloomberg.com/news/articles/2020-05-17/ecb-s-brown-bonds-draw-criticism-once-again-amid-stimulus-boost?cmpid=BBD051820_GREENDAILY&utm_medium=email&utm_source=newsletter&utm_term=200518&utm_campaign=greendaily.
[16]https://www.iigcc.org/download/ia-a-sustainable-recovery-from-the-covid-19-pandemic/?wpdmdl=3289&masterkey=5eac65344452a.
[17] http://www.energy-transitions.org/sites/default/files/COVID-Recovery-Response.pdf.
[18] http://www.energy-transitions.org/sites/default/files/COVID-Recovery-Response.pdf.

inequality. The number of European citizens at risk of poverty or social exclusion will dramatically rise due to the economic crisis. Differences in real GDP per capita between Member States and post-communist fossil fuel dependent energy mix in Central and Eastern Europe should be taken into consideration when designing specific EU financial support packages. The increase of the EU's current climate targets must be fairly distributed among Member States taking into account, inter alia, the fundamental goals of the EU Cohesion Policy.

- **No-harm principle:** Government support for investments and the economic recovery should be climate neutral and should not entrench carbon intensive sectors. To this end, future government measures to recover the economy should not provide funding to gas, oil and coal infrastructures, applying the criteria for the Just Transition Fund. For the same reasons, subsidies for fossil fuels can more easily be cut at low energy prices.
- **EU's diplomatic role and support for third countries.** In addition to leading by example, the EU should pay particular attention to facilitate the world's green recovery efforts by reinforcing its climate diplomacy networks. At the same time, the EU should enhance targeted climate-related support for the most vulnerable countries and reconsider all of its current and future trade agreements by incorporating stringent climate change related conditionalities.

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