E3G

BRIEFING PAPER October 2021

HALF-BAKED
THE NEED FOR THE NET ZERO REVIEW TO GO BACK IN THE OVEN

HEATHER MCKAY

With COP26 fast approaching, the UK must clarify how it will manage a fair economic transition to climate safety by 2050 – and set out a strategy to finance that transition. This must include a complete understanding of the costs and the benefits of the transition. This analysis is critical to capture the benefits and minimise the costs - creating real jobs, warmer homes and cheaper power to level up across the whole of the UK.

The Net Zero Review

The Net Zero Review is being written by Treasury and focuses on answering the question 'who pays', considering the up-front costs of the net zero transition. The Net Zero Review document should be seen as the definitive guide to the distributional costs of the transition, answering the 'who pays' question with a full assessment of both the costs and the benefits of net zero investment.

The Net Zero Review will be published alongside the Net Zero Strategy which will contain the plans and policies for sectoral level transition. It is essential that any decarbonisation strategy is accompanied by a complete understanding of the costs and benefits of the transition.

However, the benefits half of the equation is expected to be missing. Without this, the Net Zero Review is incomplete, and fails to assess the true economic impact of the net zero transition. This other half is crucial if the Government is to take the necessary steps to meet net zero while also protecting those most at risk and capturing the immense potential benefits.

Government has consistently articulated its aspiration for green finance leadership and a fair transition. The UK is also embarking on one of the largest public investment plans in history. A Net Zero Review which considers only the upfront capital investment costs and doesn't look at significant value that the investment will return, risks derailing the growing support for net zero investment by business and the public.

Gaps in the Net Zero Review

There are expected to be significant gaps in the Net Zero Review. Most critical of these is the failure to articulate the return on investment of net zero. This failure paints a highly unbalanced view of the economic impact of reaching net zero and is insufficient to inform government policy.

Upfront investment costs are an integral part of the equation. We therefore understand why the Government will include elements such as the changing tax base, as the energy industry transitions towards green. However, with climate change now recognised as an economy wide and macroeconomic issue by a number of high profile international and national bodies, including the Network for Greening the Financial System[1], the IMF, the G20, Bank of England and HMT, it makes no sense to just look at only the cost side of the equation and not the benefits.

It will be remarkable if the Net Zero Review does not look at the immense potential for value creation from the transition, such as the birth of new industries, cheaper power, and greener and cheaper transport. This is in addition to the numerous benefits to health and environment that will accompany new industry creation or co-benefits such as nature and health gains, and the catastrophic costs of unmitigated climate change[2]. Finally, a focus on costs and cuts will not address multiplicity of studies that demonstrate the transformative approach that investing, not cutting, can deliver.

Return on investment on Net Zero

The UK's net zero transition will require capital intensive investment upfront and will spark a changing UK economic landscape as industries transition away from fossil fuels and future-fit jobs are created. However, a managed and strategic approach to financing the transition can minimise the costs and maximise the benefits. Moreover, it is important that we recognise how significant the benefits will be to people across the whole of the UK.

[1] https://www.ngfs.net/en/executive-summary-call-action

[2] CCC Independent Assessment of UK Climate Risk

Recent analysis by Cambridge Econometrics, commissioned by CBI, Corporate Leaders Group UK and the Green Finance Institute, together with E3G and WWF[3], has outlined what value the net zero transition can bring to people and places across the UK:

> **Early investment in energy efficiency could save the average household over £500 per year in their energy bills** – through lower household spending on fossil fuels.[4]

> **Shield UK households from the effects of international gas price volatility**. Price rises and volatility on energy are hitting the poorest households hardest[5].

> **Save the NHS £1.4-2bn[6]** annually by mitigating the negative health impacts of fuel poverty.

> **217,000 additional jobs across the UK economy by 2025, rising to 370,000 by 2030.** The largest number of new jobs will be in the services and construction sectors. The largest impacts are expected across the East of Scotland, North of England and the M1/M40 corridor between London and Birmingham. In particular, support for **Boris Johnsons pledge to level up would come through supporting 190,000 energy efficiency related jobs to 2030** and channelling investment into communities in the North and Midlands where fuel poverty is highest[7].

> **Higher disposable income for low-income households from the transition to 2030**[8]. This impact could be higher with specific policies targeted at fairness.

> **Early investment would also reduce the overall cost of net zero.** According to the OBR, the fiscal cost of achieving net zero by 2050 will be twice as high for the UK if the Government delays acting until 2030[9]. Front-loading investment will maximise the net positive of the transition, including sustainable job creation[10] and biodiversity protection[11].

> The public investment needed to shift to net zero would pay for itself within the lifetime of the Spending Review - **boosting UK GDP by two percent, increasing**

---

[3] Cambridge Econometrics, 2021, 'Putting the UK on course for net zero – a fairer, stronger and greener economy'

[4] **https://www.e3g.org/publications/responding-to-uk-gas-crisis/**

[5] Reducing the dependence of UK households and industry on imported natural gas can reduce their exposure to volatile international gas prices – and thus provide more stable (and lower) prices for low-income households who are most exposed to volatility. As low-income households spend the money they save, there are also significant economic multipliers to be had from cutting their bills.

[6] **Cold homes and excess winter deaths: a preventable public health epidemic - E3G**

[7] **https://www.theeeig.co.uk/media/1099/eeig_report_turning_stimulus_into_recovery_pages_web.pdf**

[8] These Households typically spend more of their income on energy and thus are most exposed (through pre-payment meters) to rapid changes in energy costs.

[9] **The Office of Budget Responsibility highlighting the benefits of early action and investment, stating that the fiscal cost of achieving net zero by 2050 will be twice as high to the UK if the government delays acting until 2030**

[10] The IMF suggests that investing in "job-rich, highly productive, and greener activities", could generate a multiplier of 2.7 in additional output for economies

[11] **In line with the Government's recent commitment to 'nature-positive' future in response to Dasgupta review, UK Government (2021)**

E3G

employment by one percent, and reducing energy bills for all households. These gains hold both in the short and the long term.[12]

> Getting public investment on track to net zero would leverage in £106 billion in private finance for UK infrastructure by 2025, including green homes, transport, and nature.

> **Avoid the catastrophic costs of unmitigated climate change**. The CCC Independent assessment report shows that annual damage costs in the 4ºC scenario will cost at minimum tens of billions of pounds for the UK[13].

Government Action Required

In order to realise the value from their net zero investment, the government must:

> **Update the Net Zero Review in 2022 to include a full assessment of the economic benefits and the co-benefits**. This could land in the Green Finance Strategy Review and will allow the Treasury to extend its analysis to date and complete the Review.

> Announce a **strategy to deliver a net zero financial system[14] and set out a comprehensive UK Net Zero Finance Strategy[15] as part of the Green Finance Review in 2022.**

> **Include immediate and substantial commitments to green public spending for recovery and levelling up in the Spending Review** – at minimum doubling public investment levels in net zero[16] to overcome current shortages[17]. The CSR should include substantial public investment for refurbishing the UK's buildings.

> **Transition investment should focus on areas of the highest impact for net zero and levelling up – such as the decarbonisation of heat and buildings.** The National Infrastructure Bank should also be used to deliver investment to critical sectors such as nature restoration, low carbon transportation and agriculture, areas which are not included in the CCC's pathway[18].

[12] In the short-run, GDP would be 1.3% higher in 2025, and employment 0.6% greater. These benefits will persist into the future due to improved energy efficiency and the impacts of reduced consumer energy bills.

[13] **CCC Independent Assessment of UK Climate Risk**

[14] A recent letter from leading UK financial institutions, responsible for over $5 trillion in assets, called on the Prime Minister to develop a world-leading net zero financial system.

[15] For more information on what this would require, see '**Financing the Net Zero Transition, E3G, 2021**'

[16] The CCC recommends that additional investment scales up from £10bn per year in 2020, increasing to £50bn per year in 2030 through to 2050. However, changing technology curves are likely to lower the cost of investment over time, and there are cost curve savings to investing early.

[17] The Government is currently not delivering the required investment to put the UK on track to net zero, having delivered less than half of the public investment needed between 2020 and 2025. The gap to meet the CCC's Balanced Pathway is an estimated £16.9bn for this period.

[18] Given its dual mandate of net zero and levelling up, the upcoming levelling up whitepaper needs to provide a clear definition and understanding of the synergies between fairness and net zero.

Conclusion

With a changing world already affecting the domestic cost landscape[19], the case for Government action has never been clearer. COP26 is a crucial opportunity for the UK to demonstrate to the world that it is serious about building a climate-safe net zero economy. This can only be achieved if the full economic benefits of the net zero transition and how to maximise them are assessed. Only then can the Prime Minister's plan for a fair transition to net zero be realised.

About E3G

E3G is an independent climate change think tank accelerating the transition to a climate-safe world. E3G builds cross-sectoral coalitions to achieve carefully defined outcomes chosen for their capacity to leverage change. E3G works closely with like-minded partners in Government, politics, business, civil society, science, the media, public interest foundations and elsewhere. More information is available at **www.e3g.org**

[19] **https://www.e3g.org/publications/responding-to-uk-gas-crisis/**