ROUND TABLE
ON SUSTAINABLE DEVELOPMENT

Foot on the Gas? Maintaining momentum for net zero while responding to the war in Ukraine

Summary of the 43rd Round Table on Sustainable Development[1]
21 October 2022
OECD Headquarters, Paris

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The 43rd Round Table on Sustainable Development (RTSD) focused on how recent world developments, and particularly Russia's large-scale war of aggression against Ukraine, are affecting policies and progress towards tackling climate change, and what can be done to maintain momentum on climate action while responding to the social and economic consequences of the war.

The meeting, which was the first in-person gathering of the RTSD since February 2020, assembled 25 prominent leaders and thinkers including government ministers, private sector CEOs and heads of international organisations. It was preceded by an informal dinner the evening before, for which Ms. Jennifer Morgan, German State Secretary and Special Envoy for International Climate Action, was the dinner speaker.

The effects of Russia's war in Ukraine, and of the resulting far-reaching sanctions imposed on Russia, have been rapid and severe. Coming on top of an already fragile and heterogeneous recovery from COVID-19, extremely high and volatile energy prices are driving mounting inflation in many countries, creating a strong renewed focus on securing energy supplies and managing affordability. Rising food prices due to inflation and export disruptions are also contributing to escalating costs of living around the world, threatening to push millions more into poverty. Governments are taking immediate and urgent measures to shore up near-term energy security and protect consumers from these cost-of-living and inflationary pressures.

At the same time, two longer-term, interlinked challenges also require urgent action from governments: climate change and reducing dependence on fossil fuels. The climate crisis is becoming ever more acute, with global emissions still rising in 2021 and the world being far from the needed trajectory towards net-zero emissions, even as severe climate impacts are being felt. To improve longer-term energy security, immediate action is necessary to make the structural economic changes needed to reduce and ultimately eliminate dependency on fossil fuels. These two objectives are fundamentally aligned; policies can and should be designed to exploit this.

This RTSD meeting sought to understand how governments can continue to make progress on these aligned goals while still meeting the urgent social needs of the current cost-of-living crisis. The discussion was steered by the following questions:

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[1] This Chair's Summary reflects views heard at the RTSD discussion, which was held under the Chatham House rule. It does not necessarily reflect the views of the OECD Secretariat nor its member countries. The RTSD is chaired by Connie Hedegaard, former European Commissioner for Climate Action and former Danish minister, and is managed by Andrew Prag, Senior Advisor in the OECD Environment Directorate. The RTSD is grateful to the European Climate Foundation for financial support.

1. To what extent are countries' policy responses to the current crisis taking us further off-track from longer-term objectives on climate change? What can be done in particular areas to avoid this?
2. What can be done to limit impacts of the costs of the net-zero transition on households and businesses, especially given current high energy prices and rising costs of financing? Who should pay for these measures?
3. Given that private sector investment is essential for the net-zero transition, what can policy makers do to keep investment flowing in the current economic climate, with rising costs of capital and heightened uncertainty?

A background paper that supported the discussion is available here.

Main messages from the discussion

- While the crisis caused by the war in Ukraine can be a strong driver for accelerating the transition towards net-zero emissions, it is up to government policies to ensure that this actually occurs. Governments have maintained a strong focus on climate change despite the war in Ukraine, with most countries maintaining or increasing their stated ambitions. There is, however, a continued shortfall in implementation, and measures put in place by countries to respond to the economic and social implications of the war have generally not been well aligned with climate objectives. Such measures create conflicting incentives within countries, for example through lowering consumer energy prices, sending mixed signals to investors and prioritising natural gas infrastructure. They also send mixed signals internationally, whereby developing countries may perceive OECD members as pursuing fossil-fuel interests at home while continuing to avoid financing them abroad, leading to downgraded trust in climate commitments and threatening essential international cooperation on climate change.
- Today's policies need to focus more on building longer-term societal resilience. Beyond anticipating and building resilience to climate change impacts, policies promoting energy and political security must take a longer-term view by improving systemic resilience to future global disruptive events. This means investing in infrastructure that reduces reliance on fossil fuels while also anticipating potential future supply chain fragilities and dependencies related to supply and manufacturing of clean energy technologies. Resilience also means moving from a culture of "just in time" to one of "just in case".
- A widely held view is that the crisis triggered by the war in Ukraine has made very clear that natural gas does not have a role as a "transition" or "bridge" fuel in the rapid transformation required to move our economies towards net-zero emissions this decade. Investments in new natural gas infrastructure will not alleviate the immediate crisis due to the lead time of project development, and risk locking in both producing and selling countries with long-term contracts that will either derail the net-zero transition or create stranded assets. It is important that the political push to reduce European dependence on Russian gas extends to *all* fossil gas, regardless of origin or mode of delivery.
- Maintaining positive public opinion for policies related to climate and energy is essential to delivering a resilient transition and realising global climate change objectives. Democratically elected governments need to implement ambitious policies in line with climate science but must do so in a way that maintains public support for their actions, to avoid being voted out in favour of regressive governments who might roll back progress. This requires cementing a "social licence" for net zero, including by avoiding that blame for current prices be pinned on the clean energy transition. An unerring focus on communicating on the benefits of decarbonisation, while also addressing the distributional effects of climate and energy policies, is essential. This is especially true in times of economic fragility, inflation and high energy prices for consumers.
- Protecting vulnerable citizens and communities is necessary but should not come at the expense of international co-operation on security, energy transition and action on climate change. There is a risk that a rise in nationalism caused by the economic consequences of the war in Ukraine could extend to energy and industrial policies, which would ultimately be detrimental both to energy security in

Europe and for international progress on decarbonisation. The benefits of open, co-ordinated and inter-connected energy markets need to be made clear to consumers and politicians, including to highlight that renewable resources can be exploited more effectively through interconnections across borders.

- Policymakers need to strike a balance between maintaining an appropriate price signal to drive the net-zero transition while protecting vulnerable consumers and businesses from extreme prices and volatility. For consumers, governments should avoid blanket, unfocused relief policies, such as reducing excise duty on fuels, and instead pursue targeted support measures to the most vulnerable, with a focus on income support rather than price relief measures. Further guidance to governments in this area would be valuable. For businesses, artificially low prices can reduce both the incentive to invest in the transition and attention to energy efficiency. Achieving a balance through targeted policies is essential to address the real risk that energy intensive industries could relocate due to prolonged high energy prices, leading to both industrial and carbon leakage.
- A successful net-zero transition requires a relentless focus on managing inevitable employment shifts. This has grown even more important in light of the economic and social ramifications of the war in Ukraine, as well as changes in the workplace observed since the COVID-19 pandemic. Governments need to be proactive in providing current and future workers the means to develop the new skills needed as different technologies, behaviours and business models gain importance. Opportunities for repurposing subsidies to support job transitions and skills development should be explored, including fossil fuel subsidies.
- A repeat of the emergency measures enacted in 2022 in response to the war in Ukraine will not be feasible in many countries due to the public cost of limiting consumer prices and the implications for fiscal deficits and future debt burdens. Despite success in filling up EU gas storage capacity this year, high gas prices are already likely to be prolonged into 2023, in part due to the price at which stored gas was purchased, and refilling stocks may be challenging. This reinforces the urgency of both energy market reforms and a step change in measures to improve energy efficiency.
- Urgent energy market reforms are needed to weather the current crisis while allowing an accelerated transition to net-zero and making energy systems more resilient.
    - The RTSD first explored electricity market reform in Europe in 2013, and changes have now become urgent in light of the current crisis and the speed of energy transition. Shares of renewable energy in the energy mix are increasing, but market prices are still often driven by marginal pricing, which means that fossil-based generation tends to set the price, especially natural gas. This contributes to volatile prices and prevents the benefits of more affordable renewable energy from reaching consumers.
    - Political support for a form of price cap on natural gas in Europe is growing, given the substantial sums still flowing to Russia through fossil fuel purchases, as well as the need to protect consumers and businesses from high prices. However, the design and implementation of a price cap is complex and the consequences need to be carefully and urgently thought through. While some participants maintained that price signals in the gas market are still a valid signal for investment and behaviour even in the current crisis, others stressed that the complexity of the market means that prices are no longer reflecting real scarcity. Different types of price cap are possible with different implications (for example on retail or wholesale prices; permanently or as a “circuit-breaker”; universal or targeted to different forms of natural gas, such as pipeline vs. LNG). Rigid price caps can also have implications for a potential subsidy war, which would further distort international competition, including related to clean energy.
- Energy efficiency has long been recognised as the “first fuel” and as an essential element of any cost-effective pathway towards net-zero emissions. While the push to net-zero emissions in recent years has not seen the needed boost in energy efficiency, the economic and energy security challenges posed by the war have seen a redoubling of political momentum for efficiency: “if not now,

when"? This requires governments to be clear on the benefits while recognising the challenges of implementation. Barriers to efficiency are often due to lack of access to capital rather than price incentives – this needs to be addressed through supportive public policies that go beyond regulation and address financing for energy efficiency at all scales.

- The current financial climate points to a forthcoming investment crunch, with inflation and rising costs leading to a loss of investment appetite as investors take stock of a new higher-risk environment. Governments need to focus on insulating, as much as possible, "green" investment from any such downturn, including through improving financial market regulation as well as policy incentives for investment. A focus on maintaining investment flows in developing countries is particularly important where mitigation is cheaper but finance is expensive and at risk of further aggravation due to the current financial situation.
- The surge in clean energy investment needed, both to reduce dependency on fossil fuels and to transition towards net zero, requires the rapid removal of barriers to deployment as well as anticipating and avoiding future bottlenecks and vulnerabilities. Streamlining permitting procedures for clean energy is an important near-term step in many countries, but needs to be accompanied by policies to ensure availability of materials to fulfil that investment. This means developing strategic and sustainable value chains for essential materials for the clean energy transition and electrification in particular, including critical minerals. Other key bottlenecks to address include investment in electricity transmission and distribution grids, as well as a concerted effort to support and provide direction to innovation. Focussing on developing the necessary skills for the transition, which are currently lacking, is also important.

Suggestions for next steps

A number of policy-relevant issues and priorities emerged from the discussion that could be taken forward as further work through OECD committees, governments and other organisations seeking to create space for better-informed decision making as governments grapple with the "polycrisis":

- Further analysis of how policymaking across policy domains can be designed to contribute to longer-term societal resilience in the face of interconnected and overlapping global crises and disruptions, including integrating resilience to the overarching impacts of worsening climate change.
- Deeper understanding of the distributional effects of climate policies in the current energy-price context, leading to evidence-based guidance to governments on how to better calibrate and target support measures aiming to protect consumers from high and volatile price rises, as well as measures to alleviate high energy costs on businesses while avoiding direct compensation.
- Analysis of the most effective options to remove barriers to deployment of technologies needed for net zero, while identifying, anticipating and relieving future bottlenecks related to supply of materials. This could include identifying how to develop strategic, sustainable supply chains for key materials.
- Analysis to better inform how policy makers can act to maintain and scale up private-sector investment flows for the net-zero transition, including for energy efficiency, despite the deteriorating financial situation, with higher risks and rising costs of capital.
- Develop inventory of current and projected shortfalls in the skills needed to accelerate a just transition towards net-zero emissions, and provide guidance on how governments can act to provide appropriate skills development to overcome those bottlenecks, as part of a comprehensive jobs-oriented approach to making sure the transition is just and fair.
- Identifying concrete steps to advance energy market reform, including creating an electricity market fit for high proportions of renewable electricity and which passes through the benefits of cheap renewables, as well as providing detailed analysis on the implications of different forms of energy price caps.