

Discussion of:

New Climate Club
by Hitoshi Matsushima

Catherine Wolfram, MIT Sloan

Hugely important topic

The UNFCCC process has many positive elements

- Inclusive
- Focuses attention on climate for 2-3 weeks per year

But it has also been roundly criticized

- Glasgow 2021: debate about “phasing down” versus “phasing out” unabated coal and fossil fuel subsidies
- Dubai 2023: “transitioning away” from fossil fuels
- Unmet pledges (e.g., U.S.)
- Cheap talk?

Harvard – MIT Global Climate Policy Project



Carbon Border Adjustment Mechanism (CBAM)

Climate change: Prisoner's Dilemma

Rest of world
climate mitigation









A little

A lot

A little

U.S.
climate
mitigation

A lot

Climate change is trapping the world in a major Prisoner's Dilemma

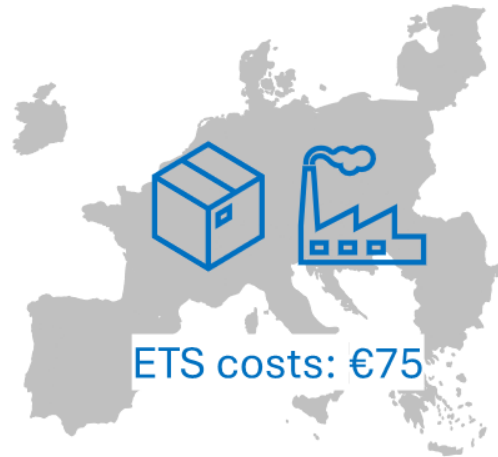
- Most countries would like other countries to take aggressive steps to mitigate climate change
→ Free-rider problem

The carbon border adjustment mechanism (CBAM) helps flip the script by changing incentives

How does the CBAM work?

- If a jurisdiction has a domestic carbon price (e.g., EU Emissions Trading Scheme), then
- ... a CBAM **adjusts** at the **border** so that imports also pay the same **carbon** price
 - For example, if a Malaysian steel producer exporting to the EU uses 2 tons of CO₂ per ton of steel and the current EU carbon price is €75/ton CO₂, the CBAM assesses €150/ton steel on exports to the EU from the Malaysian steel producer
 - Credits for any carbon price paid in Malaysia
 - Only applies to certain sectors to start

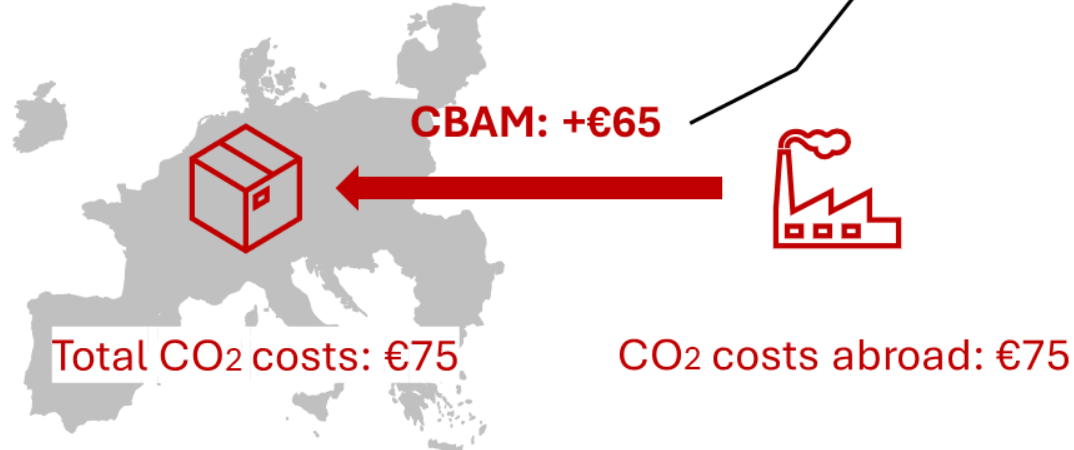
Production in EU



The CBAM applies to products in these sectors:

- Steel
- Aluminium
- Electricity
- Fertilizer
- Cement

Production abroad



With CBAM

Rest of world
climate mitigation

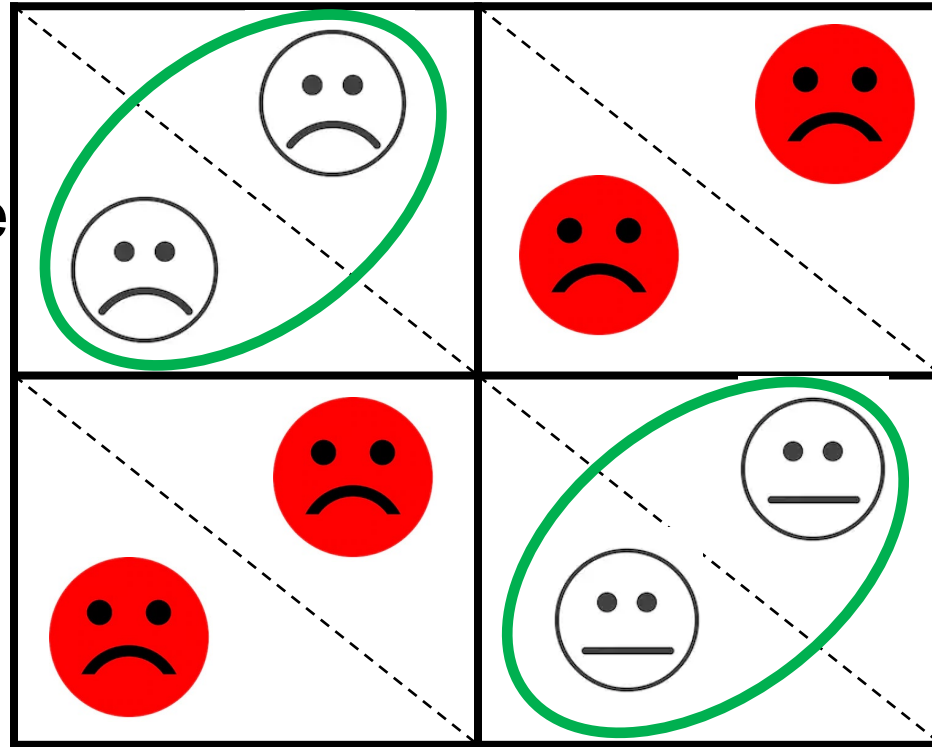
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Notes on CBAM

- EU CBAM in place, tariffs become effective in 2026
- UK CBAM to begin in 2027
- Other countries considering: Australia, Canada
- Generating increased interest in carbon pricing
- Theoretically, possible to have a **graduated CBAM**
 - Lower income countries credited for lower carbon prices

New Climate Club

CBAM + New Climate Club

CBAM: Punishes free-riding

New Climate Club (NCC): Rewards cooperation

How does the NCC work?

- Regions/countries decide whether to join club
- Club members decide on carbon price target (500)
- Club members decide on adjustment process (M)
- Members announce their own upper limits
- Reduction to *all countries* required carbon price as a function of number of members + non-members below the target (X+1)
- Adjustments continue in second stage → final carbon price function of total number of countries, M and original upper limit

Detailed questions/comments

- Social cost of carbon is more like ¥30,000
- Elaborate on countries' incentives to set initial parameters (carbon price target, M)
- Level of countries' carbon price doesn't matter, as long as it's below target
- In what forum would the NCC come together, if not UN?

THANK YOU!