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INQUIRER

Public deserves better than Treasury's failure on Labor energy 'fantasy'

By STEPHEN ANTHONY

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Last month Jim Chalmers committed to easing the performance protections that restrict how superannuation funds can invest members' hard-earned contributions. The stated reason is to facilitate greater inflows into renewables and other public utility activities, including potentially the Tomago aluminium smelter.

The announcement followed hot on the heels of the Treasurer's backdown on taxing unrealised gains in superannuation. This policy was so bad that it would have made Australia a laughing-stock on global capital markets.

So it is clear by now that the Treasurer has no economic bona fides when it comes to robust policy formation.

What about the Treasury itself in 2025? Does it demonstrate in its analysis and reporting that it can take an issue and work from first principles to identify optimal policy solutions implementable in the real world?

Further, is it still the famed agency of yesteryear literally "drawing the line" by injecting economic rigour and fiscal discipline on its minister and through central agency deliberation into federal cabinet policy processes?

Well, not based on the Treasury's latest climate report: Australia's Net Zero Transformation, released in mid-September, which we have taken our time to analyse.

The report provides political cover for the minister and the government's policy misadventures in the energy space, but not much more.

The report also reveals the Treasury's inability to rise above the current political mediocrity to make a useful first principles policy contribution to one of the nation's most pressing policy challenges.

Worse, the report is misleading and fails to meet minimal standards in economics.

The public deserves better. But does Treasury know better? Does it understand energy economics and how to think through the net-zero transition?

Australia is attempting to reduce emissions by substituting intermittent solar and wind for fossil fuels in electricity generation. This is a fraught process. Our decision to swap dispatchable for intermittent technologies is uniquely risky among advanced industrial countries. Unlike in Europe and the US, there is no backup system just across the border to bail Australia out. Australia's supposed insurance policy is a massive, expensive and wasteful overbuild of renewables capacity intended to provide redundancy to back up intermittent power.

However, as Europe and the US have shown, inevitably there must be backup provided by alternative sources: gas; coal; even better, zero emissions-based nuclear load or perhaps long-term thermal storage. The reality is that renewable energy and fossil fuels are complements, not substitutes, in production.

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Our nation is already stuck with the consequences of our renewables inefficiency: higher energy prices, lower per capita living standards, less economic resilience, over-reliance on foreign manufactures (as domestic industry is uncompetitive) and much greater vulnerability for the poor.

So, Treasury's report and related modelling appendixes should be a welcome move in this direction. We had hoped for a high standard of assessment from the Treasury. Certainly, the report claims in the foreword that it is meeting best international practice. Unfortunately, the report fails the critical test as a serious international level analysis to determine the best adjustment trajectory for the Australian economy.

The report is called a scenario analysis. It takes as a given the Albanese government's solar and wind-based policies. It takes dubious technology-based engineering inputs from the CSIRO and the Australian Energy Market Operator and uses those to calibrate macro-model projections of the economy-wide impacts of different scenarios.

This is not in itself wrong. What is wrong or misleading is the assumption that the Albanese government's policy is the best pathway forward. It is presented as the baseline scenario. See sentences such as: "Australia's ambitious and achievable plan to reduce emissions will support continued economic growth, higher living standards and employment (p7)"; "The modelling finds that expanding the supply of renewable energy continues to be the most cost-efficient abatement opportunity (p6)"; and "long-term investment in new renewable generation and storage underpins a cost-efficient net-zero pathway for the whole economy (p40)".

The report assumes the Albanese government's policy stance is optimal, and later implicitly and explicitly treats it so as a finding.

Whereas what a best-practice international report (or even low-level academic report) should say is: "The government's policy stance is assumed to be optimal and, without endorsing this assumption, we model the economic impact via different approaches to implementation."

It is not clear whether the Treasury is confused or being intentionally misleading. Either way, treating a fragile and contested program that assumes the approach of most of the rest of the world is wrong, without acknowledgment or justification, seems to deprive the Australian public of much-needed context.

The report says following the government's program in an orderly manner will give investor certainty. This is not only a trivial statement. It certainly confuses smoothness with predictability, or the state of the road with the destination. Paradoxically, a smooth transition in the wrong direction may do more economic damage than a disorderly one in the right direction – if it is even possible.

Spain's renewables-reliant grid went down in April affecting Portugal and parts of France; their transition has been neither smooth nor fit for purpose. Regardless, we advocate neither, as we consider it is possible to better identify the feasible pathways for Australia's energy transition.

A section of the Treasury's report covers export and manufacturing opportunities, which appear to be significant. Again, there is no analysis. It is simply assumed Australia has a comparative advantage in energy and can meet a significant portion of the supposed global demand for green manufacturing and green steel. This seems like a rerun of the somewhat discredited energy superpower rhetoric that had been quietly dropped.

The report contains no mention of artificial intelligence, or of why companies such as Google, Microsoft, Amazon and Meta are investing heavily in energy technologies. Singapore is raising its baseload dispatchable power capability by 50 per cent to accommodate AI. Microsoft recommissioned the Three Mile Island nuclear facility in the US.

Is AI not important for the future economy? Does Treasury know something these companies do not?

Essentially Treasury's modelling entirely misses the roughly linear relationship between Australia's measured productivity performance and the intensity of energy use. To a first approximation, GDP is energy converted into useful work. To paraphrase the brilliant Australian economist Steve Keen, without energy, labour is a corpse while capital is a sculpture.

That same relationship implies that the global renewables transition is a key contributor to the slowdown in Australia's (and global) productivity since the mid-2010s; again, because of the high degree of substitutability between renewables and dispatchable generation in production.

A logical process the Treasury should have followed in its report is to assess all the technical feasible pathways to net zero on a cost-equivalent basis and then decide which was optimal.

It could do this via the following process: First define a policy endpoint – say a net-zero goal by some realistic end point such as 2065 or 2075 – and then work back from then to the present day with realistic policy options and engineering solutions.

Next, assess all feasible existing and potential technology options available to replace existing dispatchable generation capacity and establish which of those are cost comparable on an apples-for-apples basis.

A good example of this type of analysis is a report prepared by Industry Super Australia in 2019, signed off by various luminaries from many of Australia's leading superannuation funds.

Next, assess all the value created by retaining our existing major power stations such as Yallourn, Gladstone and Eraring. This is vital. An electricity grid powered by centralised generation is far more productive than one fuelled by many hundreds of small plants powered by intermittent technologies with low-energy densities.

A good example is a report by Macroeconomics Advisory that estimated the existing value embodied in the infrastructure (the existing transmission grid and thermal power plant equipment such as boilers and steam turbines) conservatively estimated at $500bn in 2022 dollars.

After that, develop alternative transition pathway scenarios from the engineering and sector-based economic cost estimates listed above to determine the most feasible/optimal way forward. Then simulate the gains from this baseline approach in an appropriate dynamic macroeconomic model to determine the relative welfare impacts for the public of pursuing this approach.

Then, rinse and repeat. Update the modelling and planning process each year until the net-zero transition is completed.

Our suggested reporting process provides an up-to-date, independent and rigorous technical baseline to inform the right combination of storage, production and transmission capacity.

We believe it is a critical missing input for private investor decision-makers who are charged with deploying institutional capital but have no firm policy benchmark to work with in Australia.

Finally, further to the last point, governments must also stop meddling in energy markets but provide a consistent long-term planning framework.

Stop shovelling public subsidies into inefficient technologies and paying energy rebates to middle-class and wealthy householders.

Start imposing effective economic regulation on grid-incumbent businesses to allow entry of innovative technologies such as long-term thermal storage.

Ignoring all these policy deficiencies comes with a warning for all Australian governments. The approach will condemn working Australians and especially the poor to higher energy prices and lower living standards.

Under current policy settings the Australian economy will hurtle towards fully administered energy markets, something like the National Disability Insurance Scheme of energy. The energy sector is already uninvestable for big institutions unless projects are underwritten by governments. Energy already is rationed for industrial users and soon will be for home heating and cooling, too.

The adverse economic and environmental consequences of Australia's current net zero policy is depressingly predictable. But they will never be broadly accepted across the community unless Australia's bureaucratic elites step up and demonstrate integrity and courage by truth telling about the full costs of the transition.

No wonder the federal opposition is having such a hard time calibrating its policy position. Perhaps it would do better adopting something like President Donald Trump's Operation Warp Speed. This creates a technology race to transition. But tie that race to our annual feasible options assessment – outlined above. Then just replace the Net Zero tagline with Best Zero, that is, explicitly acknowledging that the transition must be more “balanced”. Going full throttle and scorched earth to 2050 just leaves the elderly, poor and industry without reliable and cheap power, while degrading our bushland and farmland for no net environmental gain whatsoever.

As for the Treasury, all that was honestly required from its net zero analysis was a book report that peered over the fence to see how other nations were handling this issue.

For example, examine the spectacular collapse of wind power investment flows in Europe as subsidies are removed. Or the policy shift in Germany to firming technologies.

If the Treasury is politically hamstrung to do this, we sympathise. But if the Treasury knows better and is simplify comfortable propagating influence through misleading the public, then we are appalled.

This is the same “rot” that applies in the Victorian and ACT bureaucracies that have gone rogue with their political leadership.

Either way, if the Treasury can no longer demonstrate economic rigour or impose some fiscal discipline on the political classes, let alone the public service, then what good is it anyway?

Stephen Anthony is a director of Macroeconomics Advisory and an adjunct professor at the University of Canberra.

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