14.3.23

Bloomberg
The US is forcing Europe to up its green game

It looked like the start of a transatlantic trade war over climate policy.

As US President Joe Biden hosted his French counterpart in Washington on Dec. 1, not long after finalizing a $369 billion green tax-break bonanza, there was a rupture in the usual diplomatic cooperation on global warming. Just a day earlier, and in front of US lawmakers, French President Emmanuel Macron criticized protectionist features of the Inflation Reduction Act that would be

Some of those European companies — first in private and later in public — have since then started making noise about the wave of American money. German chemicals giant BASF SE and steelmaker ArcelorMittal threatened to shrink their presence in Europe, where they're grappling with soaring energy prices, in favor of the newly incentive-rich US. Swedish battery maker Northvolt AB put an estimated $8 billion total on the tax credits that would come by the end of the decade from moving production to the land of the IRA. The world's biggest ball-bearings maker, Sweden's SKF AB, decided to put its new facility in North America.

If this was what Europe's political leaders feared, then its policymakers this week appear far from alarmed.

Eight months after passage of the lavish US climate law, the European Union is considering a policy response that marginally improves on the three-year-old Green Deal roadmap for tackling climate change over a decade. The measures set to be proposed by the European Commission on Tuesday don't suggest a Washington-vs.-Brussels arms race for the green future. New policies in the Net-Zero Industry Act would accelerate permitting and set production targets for technologies including solar panels, wind turbines, heat pumps, batteries and electrolyzers, according to a draft document reviewed by Bloomberg.

This is stay-the-course stuff rather than dramatic moves to counteract a sudden shift by the world's biggest economy into much more heavily incentivizing clean energy and climate technology. No one has reached for the panic button, even as companies shift their postures in response to competing incentives.

Unlike the EU's policies, which have focused on subsidies to boost the adoption of green products and technologies, the IRA is aimed at enticing manufacturers who can bring jobs to the US. It worked on Roeland Baan, chief executive officer of green-hydrogen producer Topsoe A/S based in Denmark. His company is now considering adding a second plant in the US following construction of a 500-megawatt plant in Denmark using next-generation electrolyzers that split water in hydrogen and oxygen.

"Look at the amount of money. The EU, with all its schemes together, is not so much different in scale," he said. "But it's more accessible in the US. There's much more clarity and certainty on what you get and how."

Baan sees growing demand for green hydrogen on both sides of the Atlantic, so the simpler incentives in the US open up additional avenues for growth. This may be the conclusion other businesses come to as well: It's not time to shut down production in Europe, but rather increase investments in North America.

The EU's green programs will add up to $1 trillion in spending this decade, according to projections from researchers at BloombergNEF. From a certain point of view the US is playing catchup with its $369 billion green spending measure — and because some of the American tax incentives are uncapped, the final total could be far higher.

For European companies, getting access to existing funding has become increasingly cumbersome as new funding programs with different climate requirements and goals were launched, often forcing companies to employ additional staff just to go through tedious administration and paperwork.

That's where the IRA's appeal lies: using the simple and well-understood incentive of tax breaks to boost sales of electric cars, deployment of vehicle chargers, domestic manufacturing of heat pumps, and production of futuristic fuels such as green hydrogen.

“I would rather have a positive competition with the US on climate than to complain that the Americans are doing nothing,” said Pascal Canfin, a French lawmaker who heads the European Parliament’s environment committee and Macron’s trusted man in Brussels. He sees the EU’s long-running embrace of carbon pricing and stricter rules on green investments, alongside established financial incentives for clean technologies, giving the bloc an advantage in the shared push to curb greenhouse gas.

If anything, Canfin said, the IRA has prodded the EU to improve its policy framework. “And like in any race,” he added, “it’s now on us Europeans to be on the winning side.”

The real risk for European industrial production — and what really irked EU officials — is the IRA’s domestic-content requirements. One provision would provide tax credits for vehicles at least partly manufactured and assembled in North America, a direct blow to European car manufacturers that could contravene global trade rules. Volkswagen AG has already reacted by accelerating its investments in the US, spending $2 billion on an electric-vehicle plant in South Carolina.

In order to fix flaws in the business side of the EU’s climate strategy, the European Commission in February put forward the Green Industrial Plan with the aim to simplify regulations, speed up access to finance, develop skills for green industries, and create a “more supportive environment” for manufacturing. The commission, as the bloc's regulatory arm, is set to take this a step further on Tuesday by introducing a package of measures including the Net-Zero Industry Act.

While formal approval may take about a year, the act could deliver a boost for some industries. The slow permitting process has been the “overriding biggest challenge” in Europe, Henrik Anderson, chief executive officer of Vestas Wind Systems A/S, one of the biggest wind turbine manufacturers, told Bloomberg in November.

It’s become clear that the EU is not seeking to adopt a carbon copy of the IRA. For starters, the bloc can’t follow suit because it doesn't have a unified corporate tax system. One way the EU is trying to directly counter the threat is to allow countries to give subsidies for production of green technologies that would “match” those provided outside Europe, according to a plan unveiled last week by European Commission President Ursula von der Leyen. Though no money-figure was attached to the plan, which will have to go through the months to years long EU process before it can become reality.

Until then, however, Europe benefits from a more united stance against global warming. Unlike Democrats in the US, who must contend with Republicans uniformly opposed to climate legislation, European lawmakers don't have to worry as much about marketing a clean-energy support package as anything other than a climate bill.

“The optimal policy mix is carbon pricing, investments and regulation,” said Simone Tagliapetra, a research fellow at Bruegel, a think tank in Brussels. That’s Europe’s approach. “But politically that's a no-go” in the US.

The EU’s headline climate goals have unanimous support across its 27 member countries, even if there’s differences on implementation. That level of agreement allows for tariffs on carbon-intensive goods imports and using environmental, social and governance (ESG) rules to align the financial system with climate targets. These measures have long been seen as non-feasible in US politics, although, in a sign of changing winds, the idea of taxing carbon imports is gaining traction among some Republicans.

The IRA may not end up being the boon that some manufacturers are expecting. An analysis from the Rhodium Group shows domestic manufacturing of green technologies may only get 10% of total subsidy dollars. The vast majority will go toward deployment of solar panels, wind turbines, and electric cars.

As time goes on, calmer minds on both sides are likely to see the bigger picture. Both the US and the EU need to find ways to create meaningful competition to the world’s clean-tech manufacturing leader: China. The two Western powers announced last week they’re working on a preliminary agreement around critical EV materials which could allow EU companies access to some of the IRA’s benefits.

“The moment you start thinking that China might use clean tech the same way Russia used gas, then you start to see it’s not good to be overexposed to one country,” Tagliapetra said.
The two economic superpowers also bring different strengths to the clean energy transition. The US still has a long way to go to gain the EU’s credibility and sway in international climate negotiations. The EU, for its part, will need to get more business savvy as it competes with a big, green industrial machine across the Atlantic.
“Having a competition to drive things faster, and bigger scale, is not a bad thing,” said Jennifer Morgan, Germany’s climate envoy. “It’s kind of like, game on. Let’s go.”
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