Cutting emissions will hit growth, but costs of inaction much higher, says IMF

IMF says taking swift action to achieve 25% cut in greenhouse gases by end of decade will cost less than failing to act

The IMF said decades of procrastination meant what could have been a smooth transition to decarbonised economies would now be more challenging. Photograph: Michael Sohn/AP

Larry Elliott *Economics editor*
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Vital steps to reduce greenhouse gases by 25% by the end of the decade will lead to lower growth and higher inflation but the costs of inaction would be far greater, the International Monetary Fund has said.

The IMF said decades of procrastination meant what could have been a smooth transition to decarbonised economies would now be more challenging, and the world had to cut fossil fuel use by a quarter in eight years to have a chance of hitting the global climate crisis goals set in Paris in 2015.

“Because the energy transition needed to accomplish this has to be rapid, it is bound to involve some costs in the next few years,” the Washington-based fund said in a chapter from its forthcoming half-yearly World Economic Outlook.

IMF officials have estimated growth will be reduced by between 0.15 and 0.25 percentage points a year between now and 2030 while inflation will be between 0.1 and 0.4 points higher.

But the IMF said its central message was “that if the right measures are implemented immediately and phased in gradually over the next eight years, the costs will remain manageable and are dwarfed by the innumerable long-term costs of inaction”.

Under the Paris deal, nations vowed to prevent the world’s average temperature rising 1.5C above pre-industrial times in order to avoid dangerous climate breakdown, and the IMF said more effort was needed if there was to be a “fighting chance” of achieving the goal.

China, the US and the European Union would experience less of a growth hit – ranging between 0.05 points and 0.20 points a year on average – while the impact on the rest of the world – including fossil-fuel exporting countries and energy-intensive emerging market countries – would be higher.

The IMF said governments should resist the temptation to postpone action until inflation was lower and their economies were growing faster. The costs would be higher if governments adopted a stop-go approach or delayed further on the grounds that “now is not the time” to act. If climate and anti-inflation policies were not credible, the toll would be greater.

“If climate policies are only partially credible, firms and households will not consider future tax increases when planning investment decisions,” the fund said. “This will slow the transition (less investment in thermal insulation and heating, low-emitting technologies, etc), requiring more stringent policies to reach the same decarbonisation goal.

“Inflation would be higher and gross domestic product growth lower by the end of the decade as a result. We estimate that only partially credible policies could almost double the cost of transitioning to renewables by 2030.”

Two IMF staff members, Benjamin Carton and Jean-Marc Natal, said in a blog that estimates of the growth and inflation impact of more rapid decarbonisation assumed each region introduced budget-neutral policies that included greenhouse gas taxes. These would be increased gradually to achieve a 25% reduction in emissions by 2030, alongside transfers to households, subsidies to low-emitting technologies, and reduction in taxes on labour.

"Better understanding the near-term macroeconomic implications of climate policies and their interaction with other policies is crucial to enhance their design," they said. "Transitioning to a cleaner economy entails short-term costs, but delaying will be far costlier."