ECONOMY AND ECOLOGY 28.08.2023 | Justin Talbot Zorn

Beyond the climate tech arms race

The Inflation Reduction Act raised tensions between the EU and the US. But the allies have more in common than at odds in the net-zero transition

One year ago, the US Senate surprised the world by reaching an eleventh-hour deal to pass the largest-scale climate legislation in history. While the Inflation Reduction Act (IRA) was initially greeted as promising news globally, concerns about 'Buy American' provisions and domestic tax incentives soon led policymakers in Brussels to criticise the law for creating market distortions, violating WTO treaty commitments and promoting a 'global subsidy race to the bottom'.

Today, a year into the IRA implementation, tensions persist. But there's evidence of a softening. A new transatlantic Task Force on the Inflation Reduction Act has coordinated concessions to Europe, including allowing some EU-made battery components to count towards domestic production requirements for IRA tax credits. As the EU deliberates over its own green industrial strategy, the US and European allies have expanded collaboration on some research initiatives and technology standards. At their decidedly friendly meeting in March, US President Joe Biden and European Commission President Ursula von der Leyen jointly declared that: 'We are working against zero-sum competition so that our incentives maximise clean energy deployment and jobs – and do not lead to windfalls for private interests.'

The importance of the transatlantic partnership

Still, beyond the rhetoric, the question remains: is it even possible for the US and Europe to get beyond 'zero-sum competition' on clean industry? At a time when the world needs massive new investments in climate tech – and when the US and Europe need to diversify supply chains and deploy new technologies – the answer needs to be 'yes.' While competition over subsidies and tax incentives will continue, there's a growing necessity for transatlantic allies to build a substantial partnership on climate innovation and industry.

The US and Europe also need to deepen their partnership to guard against looming challenges to the transatlantic relationship.

Consider the need for new investment. In early 2023, a media narrative emerged that new government incentives and a wave of VC funding would make climate tech 'recession proof' – and perhaps give the world a fighting chance to avoid catastrophic warming. Analysts now expect that the IRA's roughly $400 bn in climate investments will result in $1.7 tn of public and private spending. Still, the current government incentives and private financing are only a fraction of what's necessary for meeting the technology requirements of achieving the Paris climate goals. In the US and Europe, there's a major financing gap for climate-focused companies, particularly with respect to the 'valley' that runs from early-stage to profitability. The Bloomberg New Economy Climate Technology Coalition estimates that investment in climate technologies needs to triple from 2021 levels by 2025 – and then double yet again by 2030. All of this is to say nothing of the actual work of deploying new technologies – including financing energy and infrastructure projects and training workers.

The US and Europe also need to deepen their partnership to guard against looming challenges to the transatlantic relationship. Europe recently inaugurated a first-of-its-kind Carbon Border Adjustment Mechanism – a tax on specific imported products based on the carbon emissions associated with their production. The Biden administration has proposed a different model – a 'green steel club' of countries that levy tariffs on high-emission imports of industrial materials. While either strategy will have important emissions-reduction benefits, the US and EU need to coordinate their approaches – or else risk more serious trade tensions that could ultimately benefit higher-emissions industrial producers in China and elsewhere.

While it's good news that the US and Europe now have platforms for dialogue on these issues, the transatlantic allies need a bolder agenda for how to join forces in support of the green transition.

Expanding collaboration

One important way to move beyond zero-sum competition is through the practice that's come to be known as 'friendshoring' – rerouting

supply chains to encompass countries with common values and interests. Willy Shih, a professor at Harvard Business School and expert on supply chains, describes the logic as 'a recognition that we can't do everything ourselves'. There are ongoing dialogues between the US and Europe as well as other partners on how to expand friendshoring. Yet, the work is just beginning. Countries need to systematically track which allies can provide which critical minerals and other materials and products to enable the clean energy transition – and then, based on these analyses, explore how to selectively extend subsidies and other incentives to build supply chains. This is a way to speed up the clean energy transition – and deepen alliances at the same time.

Technology is another place to start. While the EU-US Trade and Technology Council – a coordinating body founded in 2021 – is working to expand some shared climate technology research between the continents, policymakers can go further, establishing joint research laboratories to address the major technological challenges for the net-zero transition. For example, the transatlantic allies could create new joint centres of excellence focused on solving the grand challenges in climate tech, including green hydrogen, battery storage, grid flexibility, carbon utilisation, climate modelling and others. These new centres can leverage countries' diverse tools and expertise to advance research and de-risk private investment. Similar international partnerships on science and technology have a proven track record in strengthening alliances and accelerating progress on technical challenges. The US and EU countries, along with other world powers, jointly fund and operate the International Thermonuclear Experimental Reactor (ITER), a fusion research and engineering megaproject based in France. A range of projects – from the CERN laboratory to the International Space Station to the Human Genome Project – have followed similar models over recent decades.

An expanded transatlantic partnership on innovation and industry could go a long way towards accelerating private investment, solving technical challenges and forging a sense of trust and shared mission for the work ahead.

Partnership on innovation can be an entry point for broader collaboration. The EU-US Trade and Technology Council is beginning work on how to create common standards for green government procurement and expanding electric vehicle charging. But, once again, governments should go further. For example, the US and Europe can learn from each other on pressing questions of how to deploy clean technologies – including workforce development strategies like apprenticeships, financing strategies like green banks and other issues like permitting, utility regulation and

economic redevelopment for regions transitioning away from the fossil fuel economy. Beyond new centres of excellence on addressing grand challenges in climate tech, the US and Europe can create new platforms for sharing best practices in public policy and offering mutual technical assistance – including at the local and regional levels of government.

Domestic politics on both continents will, of course, continue to limit budgets and policy options. But new collaborations can – where possible – draw on existing facilities and funding while leveraging new private financing. Even as climate debates remain polarised, there's growing interest across ideological divides in investments in low-carbon technology – even if only motivated by business enthusiasm around EVs or security considerations *vis-à-vis* China.

In the age of the IRA, competition is inevitable. Countries across the Atlantic will continue to vie for corporate investment, and companies will keep pushing for subsidies. Issues such as carbon border taxes will continue to be a challenge because the US hasn't put a national price on carbon as the EU has. Still, an expanded transatlantic partnership on innovation and industry could go a long way towards accelerating private investment, solving technical challenges and forging a sense of trust and shared mission for the work ahead. The transatlantic allies have more in common than at odds in the net-zero transition.



Justin Talbot Zorn
Santa Fe

Justin Talbot Zorn is Senior Adviser at the Center for Economic and Policy Research, a Truman National Security Fellow and an adviser to climate-focused coalitions and startups. He served as Legislator Director for three members of the US Congress.