

Transcript: Economics

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Thank you. In every transition, every industrial and agricultural revolution, new technologies replace the old, societies change, you get innovation and productivity leaps, and there are winners and losers - and the losers lobby the government. But the change happens.

Transitions are uncomfortable. They can make the status quo seem attractive when it's actually a very dangerous place to be, as we've heard. People who are worried about the cost of living and their future need real solutions, and they will come from going forwards, not backwards.

They will come from greening our economy faster even when others are slowing down and sowing division. There are two big things that are slowing us down. The market rules are not driving the right outcomes, and the old world is not making way for the new. Let's start with the market rules. Net zero and nature-positive solutions will not win in markets which take for granted a stable climate, clean air, fresh water, pollinators.

We currently produce and consume in a way that doesn't factor in our impact on the planet. And that is an economy wide problem, and we fix it by setting new rules of the game.

We have done some of that already, we have not done enough and we are actually in danger of rolling back. We need to consistently reward the businesses that are doing the work to be competitive in a new world where success includes: lowering carbon, restoring soils, keeping forests standing, circular use of resources and less waste - all things that add to our resilience.

We know that there's a positive link between environmental reporting and a company's returns, but the companies who disclose their carbon are already the ones who are doing relatively well, and even they experience a dip in financial performance - a hump before they see positive effects in the long term.

And that disjoint - that hump - is getting in the way of the transition.

Plus, those companies are doing all this extra work to lower their environmental footprint, restore what we've lost, they have to invest, they have to pay extra, they have to pay for certification. And then they either have to beat the competition on price, or they have to find the 5 or 10% of the market that will pay a premium - all while those who are doing nothing, who are profiting from putting us at risk, get the same financial terms, get the same market access, get the same profit.

That tells you that our rules aren't working and it's Government's job... [applause]... it's Government's job to change the rules when there are obvious market failures like this.

The second thing that's slowing us down: the old guard are fighting not to be replaced. There are businesses that lose in any transition, but some could avoid it. Fossil fuel companies and big agricultural companies - they could diversify and they could clean up their act.

Ørsted was a fossil fuel company that decided to become a renewables business, and that was in 2009, and ten years later, it was the largest offshore wind producer in the world, consistently outperforming the FTSE 100 and outperforming fossil fuel companies that hadn't made that switch, like Shell.

But the picture for the next Ørsted doesn't look so good. Spikes in the oil and gas prices since Russia invaded Ukraine have made fossil fuels very profitable again. And unless you have an automatic windfall tax, you can see why staying in that old world might be a very good strategy.

And unfortunately, too many companies are making that choice, and they have deep pockets, and they can buy lobbyists, they can buy media space, they can even buy politicians to sow doubt and sow distrust.

We have seen - we have seen this before. We saw it with the tobacco industry lobbying against the science. And it is happening here too. It is always Government's job to distinguish between the overall economic interests and the interests of those it is hearing from most.

But changes in industry take a long time to reflect in the voices that Government hears.

That will fix itself eventually. But it's a feature of these transitions that the companies that will be the industries of tomorrow - they get frustrated and outvoted, and they often end up leaving the trade bodies that are supposed to represent them as the old guard dig in and protect their interests.

So independent voices - academics, civil society - are really important right now.

And another thing it's important to say is that people and places should not be the winners and losers in this transition. Support for places and a safety net, and retraining for people is absolutely essential. We need to build confidence in this shared mission if we want a dynamic culture where ideas can come and go, but people can find better jobs in more successful, more productive firms, and places can find their new niche.

So I've said that the economics can tell us when we should be acting, and it tells us how to navigate this transition, but there's also bad economic arguments getting in the way. So let's deal with those too.

First I'll say why we should transition, but this has been said before - [Lord] Nick Stern said it in 2006. He said it again in his new book. The costs of inaction are massively outweighed by the cost of action.

The case is overwhelming - even the most cautious estimates of cost and benefits. Proving that was so important, because our economic models were not flashing red in the face of the climate and nature crisis.

Models are simplifications. They help us answer particular questions, but they don't include everything that our economy depends on. And they did not include the environment. They didn't include a functioning finance system, if you remember that. Those things are just assumed to be there.

So changes or failures are a major blindspot. Now, the OBR, the Bank of England, the Green Finance Institute, they're all correcting that now. They're all aware that climate and nature is a major systemic risk for the economic and financial system. So why are we still not acting? Why is it so hard?

Let's deal with the bad arguments. First one: "we can't afford net zero". Yes, debt levels are high because of the financial crisis and because of Covid. And that's true that lots of things that we need in this transition have got upfront costs and long term benefits. But the economics does not change because of the fiscal situation we're in.

The investment the UK needs to make to stay on the CCC's balanced pathway is equivalent to about £4 billion a year. That's 0.2% of GDP. And we can start seeing that pay back from 2041.

Even if other countries don't act, that will generate returns for the UK.

The majority of that investment would be paid by the private sector. With the right incentives and policy, they would cover 40% to 90% of what is needed, and the public sector share could be funded by national banks and asset backed lending, where the economics stack up like they do here.

Plus delaying until you can afford it assumes that costs won't increase or that it will be cheaper later. And that isn't true. Learning by doing delivers major savings. The Oxford Martin School and the Smith School have been looking at this in the context of the energy transition. They compared a fast, a slow and no transition - and faster is cheaper. The faster transition saves \$12 trillion compared to staying on fossil fuels. That is more than twice the saving of a slow transition.

Bad argument two: "the UK can't do this by itself". The UK can't do this by itself. It's true. The UK can't solve the whole climate and nature crisis by itself. But that's not what is happening. Others are acting. In the last ten years, we have seen a seven fold increase in national climate policy around the world. Plus, the best way to get others to act is to act yourself.

Leaders drive innovation and make it easier for others to follow. Just let's look at the last ten years. Globally, wind is being built out three times the pace we thought it would be in 2015. Solar installations are 15 times faster than we thought they would be. EVs were expected to have 20% of the market in 2030, have hit that last year, and they're now expected to double market share by 2030.

And because faster is cheaper, the cost of the whole UK transition is now 73% cheaper than we thought it would be just five years ago. So I'm not going to promise you the UK will have a leading role in every single part of the green transition, but we will increase our chance of being a designer, a high value component producer, a project developer if we're involved at the start and if we're working with other countries bilaterally and plurilaterally, so we can create the scale necessary for those positive tipping points that Tim talked about in key areas like energy, transport and agriculture.

Last bad argument: "we can't do this without raising the cost of living" - which is code for "we can't do this in ways that ordinary households will vote for at the ballot box". The issue of upfront costs and long term benefits for households is a really good problem to crack, and we will not crack it by sitting on our hands.

Inflation would have been 7% lower if we had decarbonised the power sector ahead of Russia invading Ukraine. It would have been a further 9% lower if our food system wasn't linked to fossil fuels through fertiliser prices, which went up 400% at that same time, and it would have been 11% lower if we'd have switched to heat pumps earlier.

Think of all the good people we could have helped if we had acted earlier. And we can't go back, but we can avoid making the same mistake twice by acting now. And those customers are a major asset in this transition. Businesses want to develop their products and their business models, where there are people - ideally informed and enthusiastic supporters of action like we have in the UK - so they can test their offer in the real world and build to scale.

Trusted companies that can insulate our homes, install energy efficient appliances, home renewables with a guarantee to save consumers money - they've got a rock solid investment. Ideas that enable people who don't have cash upfront to start saving on their bills are the ones that the Government and the finance sector could back.

How do we navigate this transition well? We need to do all the obvious things. We need patient outcome-focused strategy because it gives room for innovation and surprising answers that you don't get if you only work within sector boundaries or you only focus on your pet projects. We need to align incentives so standards, taxes, subsidies, procurement all back the businesses that are investing and innovating to reduce risk. We need to think internationally.

Most of the sectors we now need to transition - industrial goods, agricultural goods - are globally traded. So we need carbon border adjustments and we need minimum standards so

that our efforts in the UK are effective and we're building the secure supply chains with partners overseas who are solving the same problems that we are. We need to use Government money and regulations sparingly and smartly.

Evidence supports subsidies that are time limited, taxes that ratchet up over time and can be avoided - I don't mean avoided in the Cayman Islands way - I mean avoid them by doing the right actions.

And when those clean alternatives have been developed, we need the old technologies to be just phased out.

We need to highlight risks but not eliminate them. Risk moves people. So Government should speed up the process of businesses seeing what risks they face. But it should get ready for some failures.

And I want to end with what might be an unusual test of our transition. But it has to work for low and middle income households. They are key to public acceptance and they are key to building really leading businesses.

There's going to be a loss of jobs. There will be a lot of jobs created in this transition, but governments being overly jobs-focused can increase the risk of expensive mistakes. And these are filtered out if our test is: "how does this action help consumers, how efficiently are we improving people's lives?"

The jobs that are built on that strategy will be around for a long time. And I would argue so is the government that makes that their focus.

So some people are making bad choices in this transition. But the economics is clear. We should choose the rules that make businesses stronger and more resilient, the investments that will pay us back for decades, and a future where households are better off.

Thank you.