Global Spillovers of Climate Policy Shocks*

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Abstract

Slow implementation of climate change mitigation policies is partly due to concerns about their potential impact on economic growth and firm profitability. The European Union (EU) has been leading the global efforts on carbon pricing through its Emissions Trading Scheme (ETS). How do global stock markets react to innovations in this policy? We analyze responses of global stock returns to **?** carbon shocks at the country-industry level. We find that global markets react negatively to positive innovations in carbon prices, but the reaction is small in magnitude. While in the EU all sectors are affected directly to some extent, global spillovers are limited to the sectors that are linked to the targeted EU sectors through trade in intermediate goods. There do not appear to be spillovers outside such trade linkages. This suggests that unintended consequences of climate mitigation policies in the EU have so far been immaterial, and negative effects on targeted industries' stock returns remained small in magnitudes.

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