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Market for carbon credits shows signs of recovery

A report says carbon projects in South-east Asia, like Rimba Raya (right) in Indonesia, could generate returns on investment of up to US$27.5 billion (S$36.7 billion) per year. PHOTO: INFINITEEARTH

Analysts note rising concern among firms to mitigate climate change risks on operations

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When Mr Todd Lemons first received the Indonesian government's green light to help set up the 64,000ha Rimba Raya reserve in Central Kalimantan in 2010, a carbon credit would fetch US$10 (S$13) a tonne.

Three years later, after a long tussle with a palm oil company that wanted the land, demand for carbon credits had collapsed to about US$3 a tonne as investors shied away and a long-promised mandatory, or formal, carbon trading market failed to materialise.

The reserve – a US$5 million investment to preserve a tropical peat swamp forest that covers an area nearly the size of Singapore – locks away as much carbon dioxide as nearly five coal-fired power plants can produce in a year.

Projects like Rimba Raya store huge amounts of carbon in the trees and deep peat. If cleared and drained, the project would release millions of tonnes of carbon dioxide and other greenhouse gases. Preserving them is a key weapon in fighting climate change.

To help pay the costs of managing the project and funding local livelihood projects, clients agree to buy carbon credits from the project, each representing a tonne of avoided carbon emissions. The customer is essentially paying to keep the carbon in place.

Rimba Raya says its project is the largest in terms of avoided emissions delivered to date – more than 130 million tonnes of carbon emissions. For now, sales of carbon offset transactions from Rimba Raya and other offset projects, such as efficient household cook stoves, occur in the voluntary carbon market, where firms buy carbon offsets as part of their green efforts.

The offsets are not valid for use in national, mandatory carbon markets, like the European Emissions Trading Scheme which covers Europe's industry and sets increasing emissions reduction targets for big polluters. The design of the scheme is quite different.

While Rimba Raya earns enough to cover its costs and pay for a floating clinic that serves the seven villages that dot the river adjoining the concession, it has not paid a return to its investors.

"We have investors who are investing for the right reasons," said Mr Lemons, chief executive officer of Hong Kong-based InfiniteEarth, which manages the project. "They are expecting a return at some point."

But a study published last week might give the investors cause for optimism. Written by Conservation International, DBS Bank, National University of Singapore and Temasek, the report says carbon projects in South-east Asia like Rimba Raya can potentially generate returns on investment of up to US$27.5 billion per year.

With roughly 15 per cent of the world's tropical forests, which are increasingly under threat, South-east Asia's carbon stores offer the world's highest rate of return, the report says.

This is based on a combination of the size of the carbon stores – the region's tropical forests store billions of tonnes of carbon – and the risks they face from deforestation for their timber and agriculture.

That makes the remaining intact, high-quality carbon even more valuable. For instance, between 1990 and this year, South-east Asia lost 376,000 sq km of forests or roughly one-sixth of its former expanse. Indonesia and Cambodia are the worst affected, according to the United Nations Food and Agriculture Organisation.

But even as carbon emissions shrink this year amid the Covid-19 pandemic which has tipped most economies into recession, high-profile promises to curb carbon emissions suggest a lasting recovery in the carbon market might at last be at hand.

In January, Microsoft said it plans to remove more carbon from the atmosphere than it puts there by the end of the decade, bettering a vow a year earlier by Amazon to be carbon neutral by 2040.

Earlier this month, former Bank of England governor Mark Carney said he would help establish a global carbon offset market. A pilot programme ought to be up and running next year.

A carbon exchange could go some way towards injecting more transparency into a market that gets criticised for being opaque with high operating costs.

In Singapore, the AirCarbon Exchange aims to bring much needed transparency to the market by trading carbon offsets like any other commodity. Fully verified offsets are held in a registry and are traded by the tonne of carbon in a transparent manner on the digital exchange between buyer and seller.

Although it is early days yet, the exchange already has a growing client base, from carbon project developers to investment funds.

In the voluntary market, carbon credits – generated according to rules set down by non-profits like Washington-based Verra – are, for now, mainly sold directly to clients, making it tough to keep tabs on what is a fair price.

Calculating those credits is expensive. Mr Lemons said regular audits of the Rimba Raya project take months and cost roughly US$250,000. The audits are meant to ensure carbon offset projects are locking away significant levels of carbon based on the strict methodologies set by Verra and other recognised standards.

While overall sales of carbon credits more than doubled to US$320 million last year from a year earlier, said climate non-profit Forest Trends, that is only half of where the market was a decade ago.

Professor Koh Lian Pin, director of the National University of Singapore's Centre for Nature-based Climate Solutions and one of the authors of the report, said the depressed market might indicate investors' wariness.

The report, the first to focus on South-east Asia, assumes a more modest price for carbon of less than US$6 a tonne – even as more buyers promise to pile into the market – and takes into account the regulatory and financial hurdles of setting up carbon projects, he said.

"Fifteen years ago, this thing was hyped," Prof Koh said, referring to carbon trading. "There's less hype now and more focus on the science and policy aspects."

Mr Lemons said that by 2022, Rimba Raya ought to finally find as many buyers for its carbon credits as it is permitted to sell – something that has not happened yet.

As firms become concerned with mitigating the risks that climate change poses to their operations, conditions for the carbon market will improve, Mr Lemons said.

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