Southeast Asia Carbon Markets Will Find an Equilibrium: ACT Commodities

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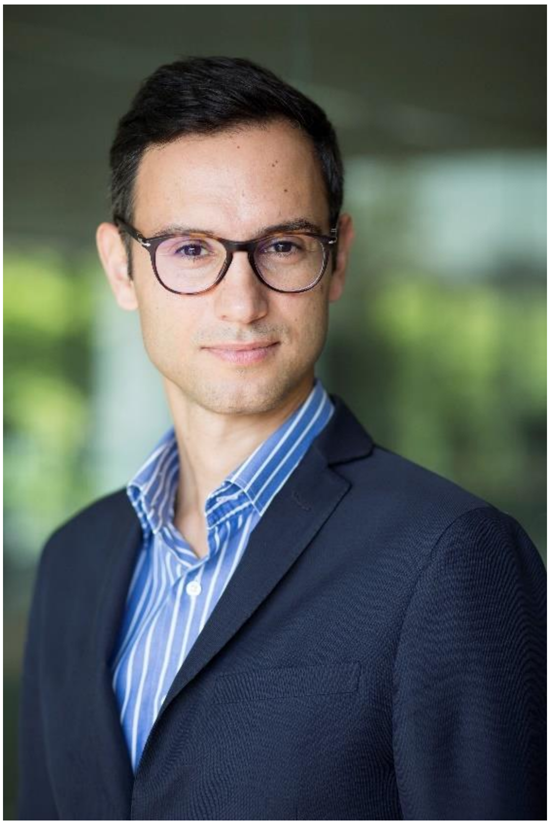
Stability in more mature carbon markets, such as in the European Union, with its emissions trading system (ETS) took over a decade to cultivate. Budding Southeast Asian carbon markets should leverage the lessons learned from these countries in order to make a system that works for the region's unique attributes – ACT Commodities' Federico Di Credico shared in an interview with BloombergNEF.

Di Credico said there is an equilibrium point that countries can achieve with a mix of voluntary carbon emissions reduction and compliance intervention. In Southeast Asia, markets are adopting a blended approach to carbon markets, starting with voluntary markets that could – in some way – lead to eventual compliance systems. Asked if there were any drawbacks to going down the voluntary route rather than compliance first, Di Credico said, "If a nation is willing to transition through voluntary mechanisms first, and if this provides the economic stability needed while encouraging climate action, then I would say there are no drawbacks." Additionally, he shared, "Be it voluntary or compliance, what needs to be achieved is economic and overall stability of the business environment within a nation that enables the ability to foster investments."

The following Q&A has been edited for length and clarity.

Q: What is your outlook on carbon markets in Asia Pacific?

A: After the signing of the Paris Agreement and the Glasgow Climate Pact last year at COP26, things are changing fast. We see conversations on climate action happening in all sectors and geographies.



***Federico Di Credico**, Managing Director (Asia Pacific) – ACT Commodities. Photo courtesy of ACT Commodities.*

Asia Pacific is definitely not an exception – a lot of different initiatives are happening here. After all, this is a fast-growing region in terms of economy and urbanization. These are leading to environmental issues such as depletion of resources, biodiversity loss and pollution, which is creating a lot of pressure.

Carbon markets in Asia are being influenced by a few different macro trends:

One is this macro, Paris Agreement-led trend, with countries having made promises for climate action through their own nationally determined contributions (NDCs). For this, countries will need to think about how to implement these promises – carbon pricing is inevitably part of this discussion.

In parallel, there is growing interest from corporates to take voluntary action. There are more stakeholders in the ecosystem which are exerting additional pressure to act. Extensive supply chains are also located in the region, so not only are corporates here feeling pressure from their stakeholders, but their customers are also creating this pressure upstream.

These result in a nice blend of globally driven carbon pricing, with local governments starting to think about how to implement their promises, and local corporates taking climate action. Against this backdrop, the growth trajectory and models of carbon markets differ across the region as Asia Pacific is so diverse.

The carbon markets in early movers, like South Korea and New Zealand, have been around for a while, with the compliance ETSs leading the way domestically.

Japan has been going down a unique path by adopting a hybrid model that involves voluntary action that is also supported by the government. You can also find this model in Malaysia. Here again we see this mix – the voluntary, corporate-led action combined with national priorities, which find a way to work together.

I should also mention the supply of carbon credits too - there are some nature-based and technology-based solutions that can be readily implemented, which can make a substantial change in terms of emissions reduction, while providing income for local communities.

Q: If we zoom into Southeast Asia specifically, in your opinion, how do you see compliance carbon markets developing across the region?

A: Compliance systems are in the making in the region, partly driven by their role to help companies achieve their NDCs. The type of system differs depending on the country.

In Singapore, the country introduced the region's first carbon tax in 2019. Compared with the ETS, it does not fix the volume but the price of carbon. This year, the government raised the ambition to S$50-80 [$36-57] by 2030, and for a small percentage of the carbon tax liability, is allowing companies to surrender eligible high-quality carbon credits instead.

In other parts of Southeast Asia, such as Indonesia, Vietnam, Philippines, Thailand and Malaysia, the local governments have indicated plans to roll out mandatory ETSs in the future.

At the same time, corporates are not typically keen on compliance schemes – they prefer voluntary, self-determined targets and are also often the fastest to implement. Hence, we see that in Southeast Asia, voluntary carbon markets have preceded that of compliance.

In a theoretical world, if all the corporates were active voluntarily to achieve their goals, there is no need for a compliance market as long as those are consistent with NDCs. Of course, that is an ideal world. It might be true at the beginning, but with the pressure piling up to reach net zero, there is a stronger role for compliance schemes to play in accelerating climate action. With the NDCs and voluntary corporate targets, we see both the compliance and voluntary carbon markets growing concurrently and finding an equilibrium over time.

Q: What are the benefits of going with voluntary first, rather than straight into compliance? Are there any pros or cons for Southeast Asia doing it this way?

A: Southeast Asia possesses immense potential for carbon sequestration due to the rich natural resources in the region. Therefore, it is in a strong position to supply the voluntary market. To many this will be an economic investment or growth potential, which also helps the nation achieve new economic gains.

As for a mature, post-industrialized nation, a compliance market might make more sense. The reason being is that developing nations would have a broader role to play, to grow and develop as a nation on one hand, and on the other, to do it in the most sustainable way. It would make it more complex to have the compliance market in a pre-mature market.

Be it a voluntary or compliance market, what needs to be achieved is economic and overall stability of the business environment within a nation that enables the ability to foster investments.

For example, parts of Southeast Asia are still in an industrialization phase, so compliance markets may restrict their growth. Therefore, if a nation is willing to transition through voluntary mechanisms first, and if this provides the economic stability needed while encouraging climate action, then I would say there are no drawbacks. [Countries can] apply this until adaptation is achieved and gradually progress toward a more controlled environment.

Even for the EU ETS at the beginning, the rules of the game were changing every other day. At one point, prices were dependent on tweets of people in the European parliament – is that really a much better system?

If voluntary mechanisms and international best practices can lead to a more stable future, it may not be a bad idea. At the end of the day investments are the drivers of this whole story and that can be interesting from a scalability point of view.

Q: Since the compliance schemes in Southeast Asia are still under development, are there best practices that the region can adopt from more well-established schemes such as the EU ETS?

There are things that we do not need to copy from the early days of the EU ETS – for example, there was significant grandfathering in the beginning, which delayed action. Now, there are aspects about the EU ETS that I appreciate, despite the challenges such as the energy crisis and ongoing debate on some of the fundamentals of the system.

What is nice about the EU ETS is that it serves as a building block of the union. With its geopolitical significance, having the EU ETS as a foundation for multi-country agreements is something that is really important nowadays.

If you think about Southeast Asia and the various cross-country discussions, this could broaden the spectrum for a pricing pool which would benefit the region. Pricing pools imply that a portion of the efforts to reduce carbon emissions is shared, to a certain extent, among nations. This way, the most efficient solutions can be implemented regardless of the geographical location. This can be achieved by having a common carbon pricing that can be accessed by any actor of that pool of nations. This also has the benefit of reducing policy uncertainty, since the policies are negotiated among different nations, this allows for consistency thus creating a more stable climate for investments.

Having “carbon clubs” or a pool of countries that start thinking together on how they can share some of these initiatives can create common benefits such as pricing stability. Right now, it is only partially happening. Countries can collaborate and gain some lessons on how Europe addressed challenges such as the east, west, south divisions in order to maintain a common carbon pricing. I would even favor, at some point in time, regional – or sub-regional – initiatives to create better carbon pricing and solutions to address the differences among countries.

Another lesson to consider would be investing in technologies and creating investment funds to support less developed countries. Especially in Southeast Asia, we have a lot of potential for emissions reduction, for example, to sequester carbon, conserve forests and mangroves, accelerate renewable energy – pooling together funds to develop innovative carbon projects will be beneficial not only for the environment but also economic development.

Q: So maybe there is hope of an ASEAN carbon hub?

Why not?

But of course, there is the elephant in the room, which is still the discussion on corresponding adjustments under Article 6 of the Paris Agreement.

For Article 6 between countries – we go back to the "carbon club" concept and having agreements and MOUs [memorandums of understanding], which are already happening. Let's start with mutual goals, robust infrastructure such as national greenhouse gas inventories and carbon credit registries. Ideally that would be the seeds for ASEAN carbon pricing. Why not, right?

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