

On the rebound

The easing of the global recession has helped to stabilise the voluntary carbon market while regulatory developments, most notably in California, have prompted an uptick in interest.

Charlotte Dudley reports

Activity in the voluntary market dropped in 2009 as the global financial crisis put pressure on corporate budgets. But with economic fortunes slowly turning around and the business case for broader climate initiatives strengthening, market participants report an upswing in voluntary demand for carbon credits, in both the 'pure' voluntary and pre-compliance markets.

Lenny Hochschild, managing director at White Plains, New York-based Evolution Markets, voted Best Broker in *Environmental Finance's* Voluntary Carbon Market Survey, says there's been a "gradual pick-up" in pure voluntary activity – where organisations buy carbon credits to offset their emissions or those of their customers – in direct response to improved economic conditions.

While volumes in this section of the market aren't exactly robust, he says, buyers are slowly coming back into play, with the bulk of demand coming from companies in the US and Europe. Meanwhile, there has been

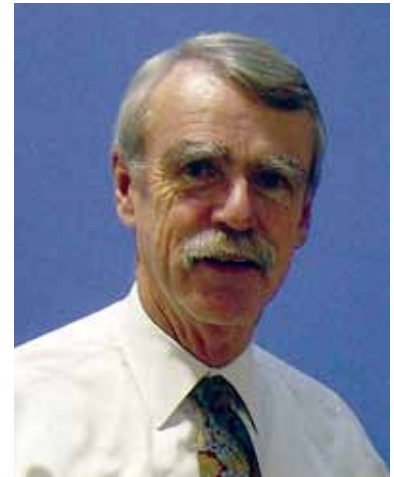
clear growth in the US pre-compliance market, in anticipation of a Californian cap-and-trade programme, he adds.

In addition to economic pressures easing, Richard Gledhill, a London-based partner at PwC, named runner-up in advisory/consultancy, says the relatively positive outcome at the UN climate talks in Cancún should boost the global voluntary market.

"It's been a difficult year, but it ended on a positive note with the Cancún Agreement which, in particular, has given new impetus to the forest carbon market with REDD+" he says, referring to projects that reduce emissions from deforestation, where tangible progress was made at the Mexican talks (see pages 14–15).

Stephen Killeen, chief executive of the UK-based CarbonNeutral Company, named Best Offset Retailer, says voluntary market participants started to take action in 2010, after a wait-and-see year in 2009.

"In 2009, you had people waiting for Copenhagen, you had [the] Waxman-Markey [climate bill] in the United



Tod Delaney, First Environment: California plans bode well for WCI

States, and then, the third component, you had the whole economic meltdown, so there was a tremendous amount of uncertainty.

"By 2010, though, people had spent so much time planning in 2009, that they started to act," he says, pointing to a rise in carbon offsetting and corporate carbon neutral product offerings.

Kathy Benini, New York-based head of environmental markets at Markit, voted Best Registry Provider, says while 2010 started slowly for the voluntary carbon market, she points to a growing take-charge attitude, with companies saying: 'If governments [are] not taking action then we'll do it anyway'.

But not everyone reported growth in 2010.

Luca Bertali, London-based global manager for Joint Implementation and the Clean Development Mechanism at TFS Green, runner-up in the broker category, says the voluntary carbon market showed a "steady decline" in 2010, dragged down by falling demand and a "huge supply" of voluntary emission reductions, in particular pre-2008 vintages. The disparity between supply and demand has "flipped" the pricing structure, Bertali explains, adding that in tough economic times, buyers are reluctant to pay the asking price of specific types of credits.

Exact figures are difficult to ascertain in such an opaque market, but market participants report sales of voluntary credits in the past 12 months as low as 50c a tonne, from some of the less attractive project types, through to €16 (\$21.80) a tonne, for credits generated by more 'charismatic' African projects.



	Winner	Runner-up
Best Broker	Evolution Markets	TFS Green
Best Trading Company	Vitol	First Climate
Best Advisory/Consultancy	ICF International	PwC
Best Law Firm	Baker & McKenzie	Van Ness Feldman
Best Verification Company	First Environment	DNV
Best Project Developer	South Pole Carbon Asset Management	Blue Source
Best Offset Retailer	The CarbonNeutral Company	Terrapass
Best Registry Provider	Markit	= American Carbon Registry = APX

"But I am absolutely positive that things will change on the voluntary side," Bertali adds, confident that environmental concerns will rise up the agenda when purse strings are relaxed.

And most market players forecast growth in 2011.

Mary Grady, California-based marketing director of the American Carbon Registry (ACR), runner-up in the registry provider category, believes the voluntary market has "a lot of room for growth," particularly in the US market as new methodologies, the essential first step for new project types, present additional opportunities.

Meanwhile, Markit's Benini expects further growth this year, boosted by rising interest in forestry projects, increasing corporate awareness of sustainability issues and domestic policy initiatives around the world such as Australia's government-backed National Carbon Offset Standard, introduced last July.

For those looking at the voluntary market as a way of gaining experience or hedging against a future regulatory regime, the pre-compliance side of the market took a hit in the past

12 months, particularly in the US following the collapse of federal climate legislation.

Kyle Danish, a Washington, DC-based partner at Van Ness Feldman, named runner-up in the law firm category, says interest in the voluntary market has remained steady among the firm's more internationally-oriented clients. However, for many US-focused players, he says the Senate's kibosh of climate legislation was "an incredible blow to their plans".

Craig Ebert, Los Angeles-based managing director of ICF International, named best advisory/consultancy firm, says slow recovery from the recession combined with a lack of climate action at the federal level has prompted many voluntary market players in the US to re-examine their carbon strategies. "It doesn't mean they're backtracking, although some of them are," he says. "They're re-evaluating their positions."

For others, the legislative failure may trigger greater interest in the voluntary market, notes Erin Craig, San Francisco-based chief executive of offset retailer Terrapass.



Luca Bertali, TFS Green: supply-demand disparity 'flipped' pricing

"Since the legislation failed we have had more businesses interested in offsets. I don't know if that's because the federal legislation failed and they figure they're going to make a contribution to [addressing] climate change ... or if it's because the economy's picking up. It's hard to aggregate the causes," says Craig, whose company was named runner-up in the offset retailer category.

But the development that's been making the biggest noise in the vol-

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Sascha Lafeld,
First Climate:
companies
shaping carbon
strategies around
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Stein Bjørnar
Jensen, DNV:
validation
process speeding
up reductions

untary camp in recent months, and is largely credited with reinvigorating pre-compliance activity, is California, with its plans for a cap-and-trade programme.

In November, voters rejected a ballot initiative that could have indefinitely delayed California's trading system. The next month, regulators unveiled its draft rules (see pages 18–19).

Christoph Sutter, Zurich-based chief executive of South Pole Carbon Asset Management, voted best project developer, points to a "big rush" among pre-compliance forestry buyers, in direct response to the Californian developments.

Rick Saines, a Chicago-based partner at Baker & McKenzie, voted Best Law Firm, says the pre-compliance market has rallied around those protocols that "were hinted at as being recognised for early-action credit under the proposed federal legislation".

In addition, he notes that some sellers aiming previously at the pure voluntary market now view California as an opportunity to parlay their reductions into early action credits that may meet future compliance liabilities.

But legislation can also pose a threat to the voluntary market.

"The legislative actions are like a two-edged sword," says Craig at Terrapass, noting that while legislation drives demand, the time lag between agreeing to and then enacting a planned regime creates a window of uncertainty in relation to what types of projects will qualify and how the programme will operate.

"It puts the pre-compliance market a bit on ice. Everyone knows that some things will qualify and others things won't, and you don't know which is which, so everybody just waits," she says, adding that Terrapass is "very fo-

cused" on opportunities both in California and the wider emerging emissions trading programme proposed for the Western Climate Initiative (WCI). The latter brings together California and a number of other US states and Canadian provinces.

Tod Delaney, New Jersey-based chief executive of First Environment, named Best Verification Company, says developments in California bode well for WCI.

"California putting in cap-and-trade really assures that the Western Climate Initiative is going take off, which then brings in British Columbia, Ontario and Québec and all the offsets there, so that they can then be sold into the Californian market," he says.

Market participants say voluntary carbon trading is increasingly forming part of corporations' broader business strategies, despite the challenges of recession, pricing, and supply and demand.

Gledhill at PwC says companies are becoming more strategic in their offset purchases, for example looking for credits that have an association with their company's supply chain or key markets. Others, such as Sascha Lafeld, Frankfurt-based executive board member of First Climate,

named runner-up in the trading company category, notes the trend toward companies shaping their carbon commitment around a specific product offering.

On the buyers' front, there is continued demand for high-quality credits from charismatic projects, as increasingly sophisticated customers look for credits under recognised standards, such as the Voluntary Carbon Standard (VCS) and the Gold Standard. Sutter at South Pole said his company is increasingly applying the Social Carbon Standard in combination with other standards such as the VCS, to meet growing demand for projects that demonstrate a broader social impact.

Meanwhile, Stein Bjørnar Jensen, head of the climate change unit at Oslo-based DNV, voted runner-up verification company, says major standards such as the VCS play a key role in the validation of new methodologies – a process he says is becoming more efficient.

"We do not see any reason why a methodology validation should take more than three to four months to validate," he said.

In the US, the number of methodologies has risen in the past 12 months, with emerging methodologies for agriculture, forestry and land-use projects. Grady at ACR expects this year will lead to the approval of methodologies covering wetland restoration and rice production. Internationally, the market is watching standards such as China's Panda Standard, launched in 2009, she adds.

As with other elements of the voluntary market, registries are becoming increasingly sophisticated. Sutter points to the trend toward real-time transactions, while other market participants say improved accountability has largely eliminated the scandals of past years, when so-called 'carbon cowboys' were accused of sharp practice in selling bogus offsets.

Looking ahead, market commentators anticipate 2011 will see a greater focus on REDD and African projects. Meantime, all eyes will be on California. However, a number of significant unknowns – about future compliance requirements, about pricing and about project criteria – leave many questions remaining.

"Over the next year I think the market will continue to bump along," says Ebert at ICF International. "I don't expect it will heat up, there's too much uncertainty about where it's going."

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How the survey was conducted

Companies were e-mailed in December and asked to nominate the leading service providers active in the voluntary carbon markets, via an online survey.

Voters were asked to make their judgments on the basis of: efficiency and speed of transaction; reliability; innovation; quality of service provided and influence on the market, not just the volume of transactions handled. Around 500 completed responses were received.