Transcript from CMI's Carbon Conversations event: International Carbon Trade & Market Mechanisms
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Panel: Rebecca Mikula-Wright | CEO – Investor Group on Climate Change, Scott Wyatt | Advisor – Delegation of the European Union to Australia, Adrian King | Partner in Charge, Climate Change & Sustainability – KPMG Australia
Hosted by John Connor, CEO, Carbon Market Institute

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John Connor:

Good afternoon and welcome once again to our Carbon Conversations. I'd like to acknowledge the traditional owners of the country from wherever you are, I'm joining you from Gadigal country, locked down for another month or so it seems. I'd like to pay respects to our elders past, present and emerging.

We have a great panel today, lots of interest in this subject. I'm looking forward to the presentations and discussions. In today's discussion, I'll ask Scott Wyatt his advice to the EU delegation here in Australia, about the 'Fit For 55', CBAM and other initiatives.

Rebecca Mikula-Wright, the newly appointed CEO of the Investor Group on Climate Change Australia, who is also maintaining her role as Managing Director of the Asian Investor Group on Climate Change, will provide viewpoints on the investor perspective on these matters.

Adrian King, from KPMG, one of our more recent CMI members, will then give us a perspective on what's happening in the corporate world. We'll then throw to all of you with questions. Scott, can I ask you to share with us insights and reactions to the EU announcements?

Scott Wyatt:

Thanks John, I'm going to run through a bunch of things very quickly, giving a sense of the state of play, then we can drill down into specific issues. By way of a quick introduction, with the EU we're talking about 27 member states and 446 million people. The EU produces about 8% of global emissions, and that figure has been declining. Since 1990 the EU has reduced emissions by 24%, while growing its economy by 62%. As you can see, there's a decoupling of emissions growth from economic growth. Many of you will have heard or be familiar with the term, the European Green Deal. This was a growth strategy put forward by the European Commission, the EU's executive arm, it was one of six major priorities put forward along with other things like digitalisation.

The European Green Deal was put forward in December 2019. Climate change and achieving carbon neutrality is a major pillar of that exercise, but there have since been a number of other interrelated things, developments have happened. For example, there's a circular economy action plan, there's a biodiversity strategy, there's a farm to fork strategy. These things put forward various targets, such as protected areas for biodiversity, reducing fertiliser and pesticide use for the farm to fork strategy, etc. As I said, climate change is a major pillar of the European Green Deal, but not the sole one, and these things are all interrelated. What's happened since then? The European Union has now enshrined in legislation a target to achieve carbon neutrality by 2050 and has also increased the targets for achieving emissions reductions by 2030, from 1990 levels, to at least 55%. The previous target was 40%.

That's a significant step up in ambition, and both of the things I've alluded to: climate neutrality and the 2030 target, have been submitted to the UNFCCC. So that then begs the question in respect to the increased targets of 55%, how are you going to get there? The European Commission has put forward a very comprehensive package of proposals, legislative proposals, targets and policies, to realise this significant emissions reduction goal of 55%, hence the term 'Fit for 55'. These proposals, they will have to go through the EU usual legislative process, which entails passing through the co legislators, the European Parliament and the European Council, I can speak to that later if you want. In terms of the detail, there are 13 legislative amendments, eight of these are revisions to existing legislation, there are five brand new pieces of legislation in there as well.

Just to give you a quick flavor, there is now, an existing renewable energy target for gross final energy consumption that's going to be increased, the sustainability criteria and their new renewable energy directive will be increased, assuming it passes. There's an energy efficiency directive, and the target for energy efficiency is increased, no surprises. Now sitting alongside the EU ETS, which I'm going to discuss briefly in a second, we have the what's called the effort sharing regulation, which sets out binding targets for each member state, and in fact, complements the EU ETS. The EU ETS covers around 41% of EU emissions, and so, there are several other policies that deal with the rest, and sitting alongside that is the effort sharing regulation, which sets out binding targets for each of the member states.

On the EU ETS, probably something of particular interest for this audience, there are several quite significant proposals put forward. The most important one is an increase in the overall level of ambition. What we call a 'linear reduction factor' is increasing, that term doesn't necessarily have to resonate, what it means is this is a cap-and-trade scheme, and the steepness of the cap is going to increase so that the ETS plays its proportional part in realising EU objectives.

Sitting alongside that, there's a proposal to phase out free allocation for the aviation sector, to introduce or to implement CORSIA here, that's the carbon offsets and reduction scheme for international aviation. Again, I can speak to that later. The European Commission is proposing that maritime emissions will be included in the EU ETS. This is a new thing. So that's voyages within the EU, and 50% of the voyages to third countries.

Another element of the ETS package is a proposal to develop a new emissions trading scheme that will cover transport and buildings fuels. So obviously the obligation will be for upstream participants, and that will sit alongside the existing EU ETS. There's a possibility in the future that the two could merge, the proposal now is to have an entirely separate ETS covering those things, with a cap applying from 2026. This brings me to the carbon border adjustment mechanism. Obviously this is something that has got quite a lot of publicity in Australia. I'd like to take a step back for a moment and talk about the EU ETS. The ETS for the phase that we've been in, phase three, which has run from 2013 to 2020, 57% of the emissions allocations have been auctioned (subject to auctioning), and the rest have been provided/freely allocated.

How do we deal with the issue of carbon leakage? I won't bother to explain what it is, because I'm sure the audience is well across it. At the moment, the EU ETS addresses the issue of carbon leakage by providing free allocation based on a benchmark of the most efficient installations - the 10% top most efficient installations. We provide free allocations to prevent carbon leakage. If you think about that, we're in a situation where the price signal to address the externality of climate change is muted, it's weak, or in some cases even absent. We want to address that. What this proposal puts forward is to phase out free allocation for certain sectors within the EU ETS.

We're talking about cement, iron and steel, aluminum, electricity and fertiliser. The way CBAM will work is, there'll be a transitional phase from 2023 to 2025, there will be a reporting obligation for those sectors for direct and indirect emissions. And from 2026, importers of those substances will be required to submit CBAM certificates in direct proportion to the embedded emissions of those products, less any carbon price which has been applied in the third country. That's a very important point. So we're talking about a WTO compatible scheme here. If there is a carbon price in that third country, this could be in the form of a carbon tax or an ETS, then that price is deducted directly in proportion. The CBAM proposal is to apply the CBAM to direct emissions only. Those for which the installation has direct control. However during the transitional phase, the European commission will undertake a review with a view to potentially expanding the scope of CBAM to other sectors, and potentially to incorporate indirect emissions.

In summary, on the CBAM, it's a WTO compatible scheme that's designed to preserve the environmental integrity of the EU's emissions reduction policies, particularly the EU ETS and the carbon price, and in effect to make sure that there is a level playing field for EU companies, so that they don't face a disproportionate burden as free allocation comes to an end. One more thing. I'll leave it there for CBAM, but I understand there's interest in the land sector, so to touch on that very quickly, amongst their proposals, there's one pertaining to agriculture and LULUCF, and the commission has put forward the idea of reaching a new target of attaining 310 million tons in the form of emissions sinks from the LULUCF sector by 2030, and also applying targets to individual member states, which as I understand is a new thing.

By 2035, the idea is to incorporate climate neutrality in the land sector in totality. So to have LULUCF sinks in effect, offset agricultural emissions, including non CO2 emissions. So we're looking for climate neutrality by 2035 in a combined agriculture LULUCF sector.

John Connor:

Thank you very much, Scott. Over now to Rebecca, from the investor perspective on these and other moves recently, and any highlights in the investment circle.

Rebecca Mikula-Wright:

Thanks very much, John. I'd like to pay my respects to the Gadigal people, where I'm based today. Investors are looking at that market and how the ETS is starting to work, obviously starting from the utilities sector, and then moving into other carbon-intensive industries. We're book-ended by these pretty large ETS systems (EU and China) and that's putting additional pressure on our trade exposed industries as it might relate to those two markets.

To dive into a little bit of detail regarding trends we're seeing with investors. We released a new survey this week, a net zero investment survey, we've been taking this survey with members for five years now, we had over 50 participants representing over 3 trillion in assets under management who took this survey. Some of the headline insights from this survey are that policy remains a key barrier to investment, up quite significantly, it's the number one barrier over the last five years, but there has been a significant jump. Investors are embracing international climate frameworks, and initiatives, and there's been quite a proliferation of those recently.

The interim targets, that are emerging, are becoming a key component of an investor's Paris aligned portfolio, and really this net zero expectation has become the norm among investors globally, but it's also the expectation now in Australia, in New Zealand as well. Then also on climate disclosures, they're up, but they do continue to lag expectations.

I'll dive into detail on some of those high-level insights, please go to the website for the full report. On the climate aligned investment and the methodologies investors are using, we've seen a big spike in the use of specific Paris aligned investment frameworks for implementation. Over 45% of investors now use this rather new framework, which goes to show the benefit of these frameworks, that take investors to a quite granular level, and helps them set out the components for an effective net zero strategy. This provides the range for asset owners or managers and considers the different mandates and starting points that they might need to consider, depending on where they're up to. There's a range of methodologies that we go through and obviously investors use different ones for example, property, where the [inaudible] framework has obviously been used for many years now.

And the Sustainable Development Goals is something that's been consistent over time, but the specifics of these net zero investment frameworks are really coming out as the number one being used by investors now because of their application through the portfolios at a more granular level. Looking at the different asset classes, where investors have undertaken climate aligned transition analysis. We're seeing enlisted equity, as having 70% of investors undertaken this analysis already, given the greater availability of data. This is followed by the infrastructure sector at just under 50%, and then real estate and fixed income.

The whole of portfolio level, this is the trend we've seen over the last five years, is heading to the 40% of investors who are really looking at this, as opposed to those individual asset classes. And that's a very welcome sign, and again underpinned by these new frameworks that are taking a very holistic approach, that's an evolution we're seeing with investors in the market.

In physical risk and resilience, obviously in the listed equity space, and at that whole portfolio level, this is something that investors have been very aware of and the exposures they might face in their portfolios. But there is a lot of work to do in getting the data, especially in the Australian context. Really costing in the costs of physical risk, and how that impacts their assets. There's been some good work by the government in the national adaptation strategy, and an ongoing assessment that will help investors collate this data and make that more usable.

There's a lot of development underway through the Coalition for Climate Resilient Investment trying to look at how to price in this risk, and then develop the appropriate investment vehicles off the back of that, but quite a bit more work to be done to assist investors on that front. And the net zero investment and net zero investment targets, again, looking more broadly and getting more specific net zero targets across their portfolios. Often what investors do, is take the listed equities as a starting point, and they might take a proportion of their assets to start with and look at how they can align a proportion of assets to net zero and work that through, and then gradually increase that proportion and move that along to different asset classes as they get more confident and understand how this works through their portfolios.

The consideration of social issues by investors, and this is referring to the mechanisms of the just transition and the implications of this transition to net zero, is very high on the agenda. About 75% of investors are considering this, that's up about 20% over the last year, and we expect that to grow. You may have seen we released a report on the just transition, and what investors are doing and can do, and how they're looking to work with a variety of federal and state governments, as well as other stakeholders and the communities in which their assets are based to help address these issues throughout this transition.

We're seeing an increase in the proportion of investors setting net zero emissions by 2050 targets, and we have several international initiatives, the net zero asset manager initiative, as one example, that investors are signing up to. And again, that takes a proportion of their assets and increasing that proportion over time until it ultimately gets us to that 100% that's covered by net zero emissions by 2050. Those 2050 targets must be underpinned by interim targets. Pleasingly, we're already starting to see about just under 40% of investors at a whole of portfolio level, and similar numbers across listed equity and fixed income, looking at those interim 2030 targets that they need to work towards, to ensure that those 2050 targets are indeed credible targets.

Rebecca Mikula-Wright:

We know that some of those interim 2030 targets are already set by some investors and real estate companies in Australia, for example. On the disclosure front, I mentioned, we have around 55% of investors now who participated, are recording the TCFD, which is pleasing, and this is obviously under the current voluntary settings, it's not as rapid of an uptake and use of this framework as we would like.

We've put out a report asking for mandatory disclosure of TCFD and outlined a roadmap that we think the regulators could take, the Council of Financial Regulators, to map out how that mandatory disclosure could come in over the next few years to really get that recording up to much higher levels.

The barriers to investment, that's constant in the last couple of years, the policy and regulatory uncertainty has jumped 30% in the last year, and arguably as the rest of the world has rapidly moved forward on climate policy, obviously the EU we've just heard about, in Asia, Japan, Korea, and China, and then it's net-zero targets and associated interim and 2030, NDCs that have been updated, and by us not moving forward in Australia, is increasingly leaving us further behind, arguably adding to the policy uncertainty. This is a barrier as investors see it, to putting more capital into the low carbon transition.

John Connor:

Thank you very much, Rebecca. Adrian, what are you seeing out there in the corporate world in responding to these various initiatives?

Adrian King:

Thank you for inviting me today. What is the corporate immediate response to the Fit For 55 and CBAM, which I think raised a few eyebrows across the corporate sector? In terms of the CBAM and Fit For 55, there's no doubt that it’s really sending another strong signal on the pace of decarbonization and carbon pricing. I do think it's taken a few by surprise, as we actually do generally see with some extra territorial type of regulations on many different topics. This is an example though, of one of the many cross border regulations we're going to start seeing as different countries take different approaches and move at different speeds. I do think this is just one of many to come. That is very complicated for corporates in particular, especially a multinationals, how do you manage those complexities.

Let me tell you three things I think corporates should be doing, and then I'll tell you what I think many are doing. The first one is the analysis of sales exposure, of these specifically applied products into the EU. We have percentage wise, dollar wise, generally they're often material, but not huge and not company destroying. But certainly that's the obvious thing to do. What's the exposure.

The second thing that they're then doing is starting to stress test their forecast, particularly around carbon pricing, because stress testing in the Australian context of $18 per ton, moving to 55 Euro per ton type environments is a significant change. People are looking to stress test to see, well, what does that really mean over different prices in different timeframes? The third one, which is probably the hardest, is really starting to consider the MRV, the measurement reporting verification aspects of what this type of policy could mean.

Many corporates are very comfortable now in Australia with corporate footprint and organisational footprint, but getting that down to the product level, which is where these go, and even into the consignment level, well that's quite a long way to go. A lot of organisations are trying to work out how would they get there? What is the allocation method, what is the veracity, and how would they prove the veracity needed to get those credits? So that's what many are doing, and should be doing, but there's no doubt not everybody is doing that. And actually not everybody is capable of doing that at the moment.

Again, partly I think, because this was not on many people's radars. Other approaches though, that are being taken, I'll describe them both as much higher-level approaches. The first one is looking at this as another geopolitical risk, trying to understand and assess from that context, and the same thing, looking at emerging regulatory risks. Trying to work out the possibilities of these risks coming through and potential impacts.

This second area where I'm seeing people respond to this is a market-based view. And if I was really to simplify that, it is assuming or taking the view of they can sell that product to someone else that doesn't have the same regulations. Of course, that may be a short-term solution, but again, one of the most, I guess interesting parts of this regulation and these proposals is not just that the EU could do this, but it could be setting a precedent for others to follow.

John Connor:

Great. I do want to shout out, and I'll pop in into the chat that the Australian Industry Group have been tracking this stuff for some time, they have just published a paper on the impacts.

John Connor:

Firstly, back to you Scott, for the comment you were making around the direct emissions and indirect emissions transition, to what degree will Europe be considering the offsets being done or undertaken, and how will they be measuring those or vetting those?

Scott Wyatt:

First of all, on verification, the Commission is looking into, or considering the processes that will be applied in terms of accrediting verifiers. And second point, and it's not speaking to your question, a quite important point on the CBAM. We're envisaging a phase in from 2026. How it will work is the free allocations that I spoke about for those particular product classes, will be phased out in 10% increments over 10 years. In addition to this transitional phase, there'll be a phase in period as well, over 10 years. That's something to bear in mind, I guess it's my words, not theirs, but a bit of a deliberate soft start.

In respect to offsets, to be honest, I don't think that the policy allows for that as it stands now. There are two main ways by which companies in third countries, producers can reduce their exposure to CBAM, and that is through third country governments adopting or having some form of carbon pricing. And for everyone's interest, I just checked the World Bank website, and they indicate that there're 45 national jurisdictions with carbon pricing and 35 sub-national jurisdictions. It's certainly gaining traction around the world. And then the second way through which of course companies can potentially reduce their exposure to CBAM is of course, through reducing their embedded emissions.

I realise that is easier in some industrial processes than others, but the world is changing, new technologies are emerging. Hydrogen, for example. Those are the two main ways through which companies and countries can reduce their exposure to CBAM, through adopting some form of carbon pricing or ultimately reducing the embedded emissions in those products.

John Connor:

Thank you. We want to see Australia's carbon pricing mechanism evolve. We do have one in Australia, and even a compliance mechanism. There's a capacity for that to evolve.

John Connor:

The transparency issue is important, and certainly also in the broader negotiations coming up for Glasgow. Adrian, we've got the government here looking at guarantee of origin schemes, I know some of the states are looking at this because they may want to be assisting their exporters. Will Europe be looking at the actual CBAM certificates that come from the company and their exports rather than necessarily a default for the broader national economy. To Scott, and then maybe Adrian.

Scott Wyatt:

On the broader question of transparency, there was a consultation process that took place with CBAM, and obviously the Commission has incorporated feedback it gleaned from that consultation process. The EU will be working with third countries in respect to the details, in terms of how CBAM will be implemented around the world, and certainly in terms of the potential impact, say for example, for least developed countries, this thing will be providing technical assistance in terms of helping them comply with the scheme. And more broadly, I'm sure you're aware that the EU is the world's largest provider of climate finance as well.

John Connor:

Adrian, how will you assist companies with CBAM certificates?

Adrian King:

It's still at proposal stage, so I think it's fair to say that there's a long way to go in terms of the detailed design of how the mechanics would work. I certainly do expect some arrangements to be considered for certain countries, there will be some simplification I'm sure, if anyone else does set up a CBAM equivalent, to make the trade components easier.

In terms of the other countries, I can speculate a guess, there was a number mentioned earlier on, again I think it's safe to say that anyone who is moving very fast in decarbonisation, or ahead of the pack, is going to be somebody who's got a vested interest at a national level to implement similar strategies. If you're moving fast in decarbonisation, then it's in your interest to keep your industries moving fast and protecting them to a certain extent. Not so much competitive advantage.

In terms of the mechanics though, we don't know the real detail yet, I do think there's some obvious places to look in terms of early stage mechanisms. There's quite a few carbon neutral products, of mainly voluntary or almost all entirely voluntary, or whether the industry association for low carbon product type methodologies and certifications, whether it's through aluminum, and of course there's the usual carbon neutral certification or carbon zero certification.

I think there's a fair amount of thinking already happening, on innovation. Which ones are picked up and how it is done in the EU is still, I think, quite a few years away. But in terms of companies thinking about how that could look and how you would start allocating some of those cost products or even consignments, I guess my point is, there are companies already trying to do it, industry trying to do it. Those are pretty good places to look for. Whichever are most relevant to your industries and products.

John Connor:

Thank you. Rebecca, several questions here around the range of the frameworks that are emerging. Are there common sets of criteria emerging? Are they settling on key areas, how are investors looking to simplify some of these frameworks?

Rebecca Mikula-Wright:

Very good question given how many initiatives and frameworks there have been out there. We've been working with our global peer networks through the investor agenda, which brings together the different climate networks and all the groups that work with investors around the world. We've just released, a couple of months ago, a framework that's the mother of all frameworks that sits across all of them, called the Investor Climate Action Plan Framework. This is an expectations ladder, so that we can create a common framework, that helps investors wherever their starting point may be, and working through the four or five pillars they need to consider across their portfolios.

It's in their policy advocacy, their investment, how they engage with companies, and the disclosure of all of that activity, as well as the governance that goes with all of that. Across those five pillars, this framework sets out, if you're at the beginning of integration into your portfolio, what does that look like across each of those five areas? And then how do you progress from an early stage to net zero? And what does net zero alignment look like?

We've now got this framework, and we've agreed that with these global investor networks to create some commonality and to get some clarity around these frameworks and how they fit in together. And when investors are ready, what are the net zero commitments and targets and the resources and the tools and the methodologies that they can look at to get them to net zero. That's a new framework that's been released in recent months that we hope becomes the new norm to help guide investors to the ultimate north star of aligning with net zero.

John Connor:

Thanks. I've got a question here about the fairly significant moves announced this week by two of our biggest companies here, the question is how do investors believe the sale of carbon intensive assets will meet portfolio requirements for a particular company against the universal investor perspective. How do you view those developments? Is there a trend line that stakeholders need to be tracking?

Rebecca Mikula-Wright:

There's been quite a bit of activity in Australian market recently, we're seeing this offshore as well. This is why initiatives like Climate Action 100+ were established. Investors have a mechanism to engage with these high bidding companies. It's very much about how do you transition these companies to align with net zero, selling off their assets isn't going to solve that problem. Those emissions don't go away.

In many cases, investors are opposed to those moves of selling off assets, because they're trying to get that company to reduce their exposure. That's why investors might choose to stay and engage with the company to do that, whereas others will obviously take a divestment approach, if engagement hasn't worked.

Different investors have different approaches, the idea is that they're trying to work with that company, and if they're getting results with that company to reduce the emissions. Then they want to stay with that company because ultimately the company will be successful and sustainable in the longer term. While the company might be more successful and sustainable by selling off those dirty assets, it just puts the problem somewhere else, and some investors are still exposed, they still have to engage with that company, that's with high carbon intensive assets.

Rebecca Mikula-Wright:

The problem doesn't go away. For some large superannuation funds, they're universal owners, they have exposure across the whole of the economy, they do need to take that systemic approach to their engagement. So this just transfers the problem, it doesn't make it go away at all.

John Connor:

Scott, back to you. How's the linkage happening with the UK scheme that's emerged? What are some of the hurdles that will need to be passed? You mentioned the legislative process, what reaction has been internally?

Scott Wyatt:

First, on the UK ETS, I'm not up to speed with the deliberations on linking with the EU ETS. Most colleagues in this video conference, I'm sure would be aware that there is now a link with the Swiss ETS, but I'm not sure what's going on in respect to the UK ETS. In terms of CBAM for example, with the UK applying its own carbon price, as I was saying before, any country that's applying a carbon price won't be liable for that proportion of any embedded emissions in terms of the CBAM obligations.

We've been monitoring the situation around the world, and reactions in Australia which have varied, obviously on CBAM. The processes is going forward in terms of next steps, all of the legislative developments to Fit For 55 need to be scrutinised by the EU co legislators. That's the European Parliament and the European Council. Most legislation in the EU, in terms of the Council I'm talking about, the European member states, must go through qualified majority. It 55% of the member states, in effect 14 now, and the member states making up 65% of the EU population.

That's the qualified majority rule in terms of how most of the legislation will pass, and simple majority in the Parliament as well. The whole package is a priority for the Parliament and the Council, but it's difficult to put an exact timeline on this, because like the Australian system, there'll be a lot of back and forth, inevitably, and some of the legislation will be amended.

John Connor:

Any chance before COP26?

Scott Wyatt:

That's a tight turnaround. I would be very surprised if any of it makes it over the line by then. It's not a short process, but having said that, there's a lot of support in the broad sense for these measures from the member states and from the European Parliament. The European Parliament in fact, was pushing for a 60% reduction in emissions.

John Connor:

On agriculture, you talked about the targets for LULUCF, and that being a new development, and an interesting one for Australia to consider if we have our LULUCF, and from broad broader emissions. Is there an intention to link some LULUCF to the trading scheme?

Scott Wyatt:

There's no intention to incorporate LULUCF into the EU ETS that I'm aware of. On the land sector, just as a bit of a segue for your members, this is not the end of the story, there're going to be more proposals coming forward in terms of EU climate ambition, and one of those for example, is in fact, a carbon farming initiative.

Scott Wyatt:

They'll be looking at incentivising, increasing soil carbon, this kind of thing. And as I understand it, using some of the funds potentially from the Common Agricultural Policy and Member State funds and assisting farmers through providing frameworks to credit them for their work, I know that this thing has a lot of traction in Australia. So there's some parallels there.

John Connor:

But not creating credits that can be offset against some of the targets or other covered sectors?

Scott Wyatt:

Yeah. I see what you're saying and no, I don't think so.

John Connor:

Okay. Then that goes to the impact of CBAM for Australian agricultural products. Now, of course you don't have a price covering the agricultural sector currently, so it wouldn't necessarily be an impost on Australian agriculture in that sense.

Scott Wyatt:

We realised there are some sensitivities in play there, the EU is Australia's third largest trading partner, I'm not a trade expert, but as I understand it, most Australian exports to the EU are mineral commodities and related things and agricultural products. As you mentioned, agriculture is not included in the EU ETS and similarly methane gas is also not included in the EU ETS.

Rebecca Mikula-Wright:

I'm conscious a question came in before, and it's a bit of a segue, but staying on agricultural. It took me back to the question about the physical impacts across the value chain that someone brought up earlier in the chat. This is quite interesting in the agricultural sector, because it does face a lot of these risks all at once. Upstream inputs, water and fertiliser, downstream inputs like transport, and then the physical impacts to crops and floods and that sort of thing. So yes, investors do need to consider right across the value chain regarding the physical risk side, and thus the complexity around trying to do that. Obviously in the local context for the agricultural market, but of course this does apply to offshore supply chains as well, and trying to mark those physical risks.

Scott Wyatt:

On the agriculture question, just for the information for those on the video conference, Austrade has put out a short publication addressing this issue and not surprisingly indicating that the impost is negligible, if anything at all. One thing I wanted to point out is that there're potential opportunities in terms of trade and investment for Australian companies in terms of addressing the broader question of agricultural emissions. I realise there are some companies that are progressing ventures in respect to developing feed supplements that reduce enteric emissions, this kind of thing. And this is very much on the radar in the EU as well.

And for example, we have a methane strategy that in particular talks about that as being an avenue for mitigation. There are trade and investment opportunities, this is not all about costs.

John Connor:

Adrian, what are some of the opportunities that companies can see and be positioning for. For Australian companies? And it's not just in relation to Europe, but elsewhere.

Adrian King:

Absolutely as always, every risk creates an opportunity. Every time we all use the word risk, we should be thinking about the other side of the coin. But there's a lot of questions, obviously on offsets and the option for Australia to participate or use offsets.

Most of the design hasn't been set, we do see different frameworks, some allowing offsets. So the general rule is certainly not allowing them, and even when they do allow them, they are very specific. I say this, they usually go through very significant equivalency type tests. I think one of the things to look out for, as we do go through this is, will be if they allow offsets, for example as a way of reducing the exposure to CBAM.

If they do allow offsets, what type of offsets? At the moment they've been quite specific on types. I don't expect them to take any shortcuts, they will generally be very high integrity units. A lot of businesses here in Australia have great opportunities to create offsets, given what we do. Whether we use them in the Australia market or whether we start using them internationally, I think is a massive opportunity for the whole ag sector.

John Connor:

And then opportunities also in technology and measurement, the point you were making about measurement reporting evaluation, this is a verification, that this is an area where Australia actually has got a head start and has significant opportunities both in the regulatory frameworks, but also in the technology that's emerging.

Adrian King:

I do think we've got one of the best understandings of our footprint, is the way to describe it. Across the country we've got a good understanding, it's monitored, it's regulated. We’ve got a good starting point. That's largely at the organisational level, how we draw that down to product type level is the next challenge. If you've got a good starting point, this is certainly an advantage.

John Connor:

Scott, back to LULUCF, it will be more taxes and grants and schemes that will drive some of that LULUCF, or other market mechanisms which may happen alongside for getting climate neutrality in the land sector by 2035?

Scott Wyatt:

To give one example alongside the many elements of the Fit For 55 package, there's a new forest strategy that's come out, trying to improve the quality and quantity of forest in the EU and protecting remaining old growth forest. Also setting a goal of planting 3 million trees, as I mentioned there's a methane strategy that looks at reducing methane in the land sector, this kind of thing. So, there are various tools in the toolbox.

John Connor:

You mentioned the biodiversity strategies, part of the deal. There's a question in here about biodiversity loss. I don't know if you can respond to that, one of the big questions is the co-benefits and how we might measure the additional attributes.

Scott Wyatt:

Biomass is used in the EU and the new renewable energy directive proposal, the proposed amendments look at tightening the sustainability criteria because, whilst biomass has a role to play, one has to be careful in terms of indirect land use change and potential perverse outcomes.

Rebecca Mikula-Wright:

Whether it's the CBAM mechanism or other mechanisms, when investors are looking at the companies they invest in, they're looking to get absolute emissions down, and how that company is planning to do that, the capital expenditure they're putting towards emissions reductions, the transition, their business strategy, aligning to 2050, near term, 2030 interim targets. That's ultimately what it's about, reductions. When it comes to the matter of offsets, you can't keep emitting and then just offset your way out of this, The clear focus needs to be the emissions reductions, and working towards 2030 goals to make sure that we can get to that 2050.

Adrian King:

This is an example of what is going to happen around the world with fast decarbonization. We’ve got to make sure, certainly from a corporate perspective, we're not looking at the Australian context as being the default, in fact, the opposite. Expect more of these overseas, different systems and approaches and speeds. And from a corporate perspective, it just makes the world a bit more complicated, but it isn't going to go away. And as corporates must deal with multiple other complexities, such as other taxing, regulations, or whether it's labor rights, this is just another area of international complexity.

Adrian King:

So, start understanding it, get ready and get your data ready for whatever the rules, because you can't set the rules, you have to comply with them.

Scott Wyatt:

We are drawing close to COP26. One thing we didn't talk about is the IPCC report, which is again another assessment as to where we're heading and a reminder of the urgency of what needs to be done, so the EU is calling on all countries to put forward ambitious targets, and policies to back these up, particularly G20 countries representing 80% of global emissions.

Scott Wyatt:

There's a leadership role there, including for advanced economy countries, such as Australia. From the EU point of view, we are backing up what we are saying, in terms of our targets, with concrete policies.

John Connor:

Thank you all for your participation today.