Many governments believe that carbon trading will provide substantial funding to protect or sustainably manage forests in their countries via proposed schemes to Reduce Emissions from Deforestation and Degradation (REDD). This briefing explains why...

CARBON MARKETS WILL NOT DELIVER FOR SOUTHERN GOVERNMENTS, FORESTS AND PEOPLE

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WHY CARBON MARKET

HOW MUCH MONEY IS NEEDED?

In the current REDD debate the amount of money required has been the primary focus, often without a clear indication of what the money should be used for. Previous attempts to halt deforestation and forest degradation have however shown that the key requirement is not money, but a clear action plan to address the underlying drivers of forest loss coupled with sufficient political will to implement the plan.[1] Developing a realistic estimate of how much money is actually needed would involve national level discussions to achieve agreement on the causes of deforestation and how much it would cost to develop and implement a concrete action plan to address them. The process should be consultative and inclusive of all stakeholders, similar to the Forest Law Enforcement Governance and Trade Voluntary Partnership Agreement (FLEGT VPA) process that has taken place in Cameroon, Central African Republic, Ghana, Indonesia, Liberia and the Republic of Congo.[2]

Chart 1: Existing and expected finance for REDD 2010-2012

Government funds: 8.38 billion[3]	Compliance carbon market: 0.0 billion	Voluntary carbon market: 0.6 billion[4]

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Government funds currently committed to REDD schemes are large (see chart 1), but many Southern governments have had bad experiences with broken promises and the strings that came attached to development aid. They therefore do not have much hope for public funds to support anti-deforestation measures. Indeed, considering the financial crises in industrialised countries, it is unlikely that the current large aid flow to REDD will continue.
Many Southern governments have therefore put their hopes in a global carbon market that includes forest carbon or 'REDD' credits. We believe these hopes are misplaced, for the following reasons:

The largest carbon market will not include forests until at least 2020

Ninety-seven per cent of the existing carbon market is linked to the European Union's Emissions Trading Scheme (EU ETS).[5] The EU ETS currently does not accept forest offset credits and this will not change until at least 2020. After this time, it is unclear whether there will even be a European carbon market. There are other regional trading schemes but whether or not they will include forest credits remains to be seen.[6]

The likelihood of a global carbon market is diminishing

Until 2010, much growth in carbon trading volume occurred in the secondary carbon market. This is important to note because while at least some of the money raised in the *primary* market is invested in climate projects, in the *secondary* market, the same permits and credits are traded multiple times with no additional climate benefit, before they are eventually sold to a buyer who will use them to cover emissions. Even this growth in secondary trading is now stagnating.[7] Since 2008, many banks have closed or downsized their carbon trading desks (e.g. Bank of America, ABN Amro, UBS Warburg and Credit Suisse).[8] Carbon credits were recently declared the world's 'worst performing commodity'[9] and there is nothing on the horizon to suggest that carbon markets will come back from the brink.

Forest offsets in the voluntary carbon market have been fraught with difficulties

Although there is no imminent prospect of a global carbon market, let alone one which accepts forest credits, 'REDD' credits are being bought and sold on the voluntary carbon market. This is a market highly dominated by North American entities generating, selling and buying credits based on land in the Americas, in particular South America.[10] More importantly perhaps, whilst a number of controver-

TS WILL NOT FINANCE FOREST PROTECTION

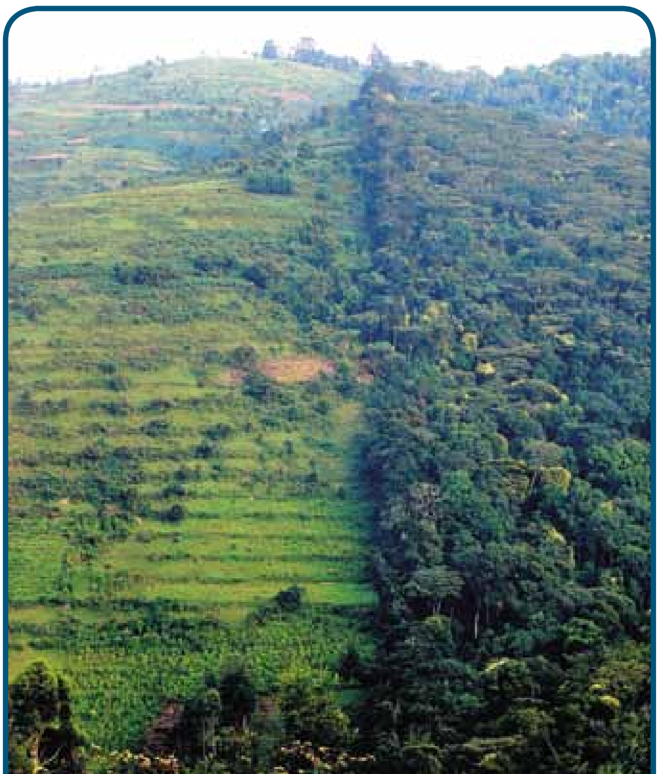
sies have surrounded the compliance market, many of the worst examples of dubious and damaging offset credits come from the (largely unregulated) voluntary market.

Even if there was a forest carbon market, little money would go to forests

A global carbon market would work the same as any other commodity market – most of the money would enrich those who trade or speculate in the commodity whilst producers would receive a limited percentage of the final cost, in many key commodity markets as low as 3 per cent.[11] A study looking at a possible future trade in forest carbon credits concluded that if such a market materialised it would require US$20 billion worth of trading to deliver US$0.6 billion for forest projects.[12]

Even if funds would go to forests they would not go to “high-risk” countries

Investors put their money where risk is lowest and return is highest. This is why more than 75 per cent of carbon offset projects approved in the Clean Development Mechanism (CDM) can be found in only three countries.[13] Only 6 million of the 424 million CDM credits issued by August 2010 had gone to projects located in African countries, and 80 per cent of these have gone to a single industrial gas plant in Egypt.[14] This would be no different in a forest carbon market (as has already been shown in the voluntary market),[15] and so countries perceived as a high risk for investment (including many African countries), would be unlikely to attract substantial volumes of funding.



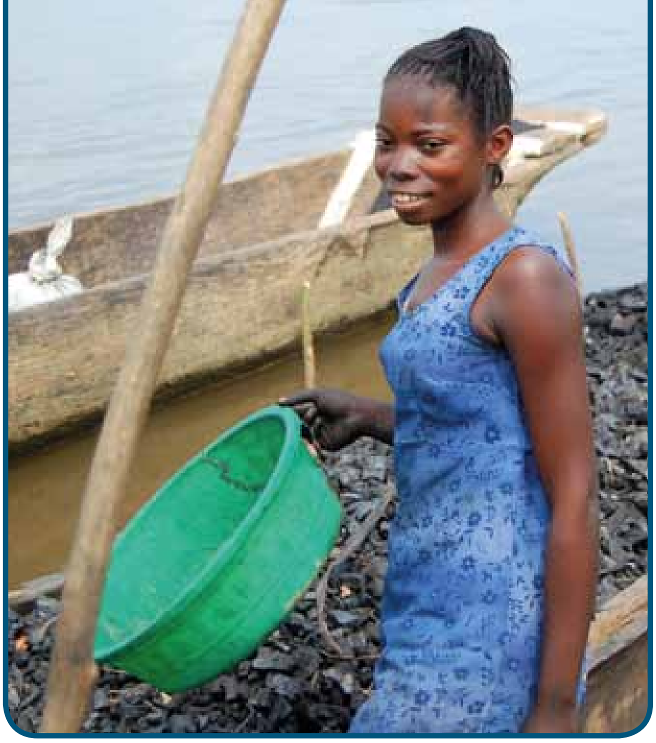
SOME ALTERNATIVES

Market based or market linked alternatives[16]

Financial Transaction Tax (FTT)
A tiny tax on financial transactions – as little as one hundredth of a percent – could raise US$650 billion per year.[17] Although many adaptation and mitigation measures would need to be financed through such a fund if it ever materialised, a small proportion would provide enough to help reduce deforestation. The European Commission and many European governments, including Germany and France, already support the FTT, and research from economic institutions including the International Monetary Fund (IMF) has shown it to be technically feasible.[18]

Tax on international shipping and aviation
There are many different proposals on the table to tax international aviation and ‘bunker’ (shipping) fuel. The emissions from these industries are significant, and they are currently not only under-taxed, but also benefit from fossil fuel subsidies.[19] Redirecting these subsidies to climate mitigation and adaptation is another potential large source of finance.[20]

Public funds
Even in times of austerity measures, if government spending priorities were brought in line with their climate change policies, money would also become available for



forest projects and for activities to deal with the drivers of deforestation. Government funding is still the major funding source for REDD as chart 1 shows.

Public funds could also be used to address illegal logging. The World Bank (WB) estimates that illegal timber may comprise over a tenth of a total global timber trade worth more than US$150 billion a year.[21] More funding and political support to address illegal logging would therefore go a long way to keep forests standing and provide funds to Southern governments.

Private investments

Projects where companies buy forests to speculate on financial markets (as is the case with trading in forest carbon credits) have led to many problems. However the Forest Trust's Climate Tree project is an example of an initiative which channels private investment into improving forest use without letting Northern companies off the hook with regards to reducing their own emissions as carbon offset projects do.[22]

CONCLUSION

In conclusion, it is highly unlikely Southern countries will receive substantial funding from forest carbon markets because:

- **It is unlikely that a global carbon market will appear in the time relevant for the REDD debate, but if one did...**
- **it is doubtful that forest carbon credits would be widely included and tradable across different carbon trading schemes, but if they were...**
- **only a small percentage of these funds would reach forest offset projects, and of that small percentage...**
- **an even lesser percentage would reach forest projects in the poorest countries, and of this already much reduced percentage...**
- **only a fraction would go to forest communities.**

Therefore, it would be wise to expect that money to halt deforestation would not come from a forest carbon market. Currently almost all funding for REDD comes from governments, and in the future it is more likely to come from initiatives such as taxes, levies, financial transfer payments from North to South, development aid and private investments.

Southern governments need to be realistic about where money for forest protection will come from. Spending time setting up expensive systems to monitor carbon fluxes in forests, whilst waiting for forest carbon markets to appear will not help halt tropical deforestation, especially in African countries where the barriers to investing in carbon trading remain acute.[23] Governments – North and South – need to focus on direct investment to make the structural changes necessary to deal with the real causes of deforestation and keep forests standing. As this briefing shows, there are plenty alternatives more likely to provide the funding required to do this than trading forest carbon credits.

Footnotes

1 Recognition of indigenous peoples' and local communities' tenure rights and improving forest governance is seen as key to address deforestation and forest degradation. The Rights and Resources Initiative found that "the cost range of recognising community tenure rights ($0.05/ha to $9.96/ha) is several times lower than the yearly costs estimates for administering, implementing and financing an international REDD scheme ($400/ha/year to $20,000/ha/year)." http://www.rightsandresources.org/documents/files/doc_1474.pdf

2 The EU FLEGT Action Plan is the European Union's response to the global problem of illegal logging and the trade in timber products. It sets out a range of measures to combat illegal logging, including Government Procurement Policies; Financial due diligence; Voluntary Partnership Agreements between the EU and timber producing countries and has led to the adoption of an EU wide illegal timber regulation to control imports of illegally sourced timber.

3 Figures taken from http://reddplusdatabase.org/

4 www.forest-trends.org/documents/files/doc_2828.pdf Pages iv and v. REDD accounts for 33 per cent of the US$414 million over the counter voluntary market in 2010. Figures multiplied by three to give estimated figures for 2010-2012.

5 State and Trends of the Carbon Market 2011. See page 9 "the share of the carbon market primarily driven by the EU Emissions Trading Scheme (EU ETS) rose to 97 percent, dwarfing the remaining segments of the market". http://siteresources.worldbank.org/INTCARBONFINANCE/Resources/StateAndTrend_LowRes.pdf

6 California will begin its carbon trading program in 2013, but the likelihood of the state accepting 'REDD credits' is far from certain. The enabling regulation currently allows only for domestic offsets, and concerns remain around the ability to regulate and ensure offset quality outside its borders. In California, the concept of international offsets remains very unpopular at the political level. Australia is also set to start a cap and trade scheme in 2015, but the regulations detailing the limitations on credits allowed under the scheme have not yet been released. So far there are no methodologies allowing for avoided deforestation, although there will be an allowance for credits from plantations, following Kyoto-compliant methodology. There are also trading schemes planned or ongoing in New Zealand and Japan.

7 State and Trends of the Carbon Market 2011. See Page 9 Table 1. http://siteresources.worldbank.org/INTCARBONFINANCE/Resources/StateAndTrend_LowRes.pdf

8 http://www.endseurope.com/21308/corporate-environmental-news-roundup-54

9 Wynn, Gerard. "Carbon Offsets Near Record Low, Worst Performing Commodity" Reuters, August 8 2011.

10 North America was the top region for sourcing carbon credits in 2008, generating 42 per cent of the volume http://www.ecosystemmarketplace.com/pages/dynamic/article.page.php?page_id=7415&section=home

11 http://www.mundenproject.com/forestcarbonreport2.pdf

12 Ibid.

13 Chart 5 page 67. http://www.fern.org/sites/fern.org/files/tradingcarbon_internet_FINAL.pdf

14 http://www.africanbiodiversity.org/system/files/PDFs/CDM%20Report_Feb2011_lowres.pdf

15 State of the Forest Carbon Markets 2011. See page 39. http://www.forest-trends.org/documents/files/doc_2963.pdf

16 Market based includes carbon trading but also taxation measures, although some prefer to call these market-linked mechanisms.

17 Bonn Brief no. 8, Innovative sources of climate finance, June 2011. http://www.foe.co.uk/resource/briefings/Bonn_2011_08InnovativeSources.pdf

18 See: World Bank Group, IMF, OECD. Mobilizing Climate Finance: A Paper prepared at the request of G20 Finance Ministers, September 19, 2011; and: IMF (2010). A Fair and Substantial Contribution by the Financial Sector, Final Report for the G-20: www.imf.org/external/np/g20/pdf/062710b.pdf.

19 http://www.guardian.co.uk/environment/2010/aug/03/fossil-fuel-subsidies-renewables

20 For more information about these alternatives and others see, Assessing the Alternatives - Financing Climate Change Mitigation and Adaptation in Developing Countries http://www.stampoutpoverty.org/?lid=10939

21 OECD, OECD Environmental Outlook (Organisation for Economic Co-operation and Development, 2001), p122.

22 http://www.tft-forests.org/climate-tree/

23 Why Congo Basin countries stand to lose out from a market based REDD. http://www.fern.org/congobasinloseout