

More Flexible Carbon Offsets Needed for Heavy Emitters to Meet Net Zero Goals

- Net zero targets are in danger of being missed as companies struggle to decarbonize
- The Science Based Targets initiative may allow companies to use carbon credits for Scope 3 emissions
- McKinsey report shows that only 22% of low carbon products are profitable without a green premium

Heavy emitting companies are in danger of missing their net zero commitments unless they are allowed to use carbon offsets more flexibly as part of their emissions reductions plans, according to a leading carbon consultant speaking at Nomura Greentech's Sustainable Leaders summit.

"We're going to see that a lot of companies aren't decarbonizing fast enough," said the consultant at the event which took place under the Chatham House Rule "There's a lot of challenge right now and it's like letting perfection get in the way of the good."

He referred to the recent announcement by the board of the UN-backed Science Based Targets initiative (SBTi) - which certifies whether a company is on track to help limit global warming to under 1.5°C – about potentially permitting companies to use carbon credits to offset emissions from their supply chains, known as scope 3. Currently, companies are only allowed to use them for their residual emissions. Industrials, aviation and energy are some of the sectors with big scope 3 emissions.

"When SBTi came out and said we're going to allow offsets to be used for Scope 3 mitigation, that was an important signal for the market because without demand there's never going to be supply."

The consultant said that if the plans did go ahead, it would be significant as heavy emitters are finding it challenging to decarbonize their businesses via the more direct route of making greener products as those technologies often carry a green premium, which makes them more costly. The ability to use carbon offsets in the meantime could plug the gap.

He referred to a McKinsey report that shows only 22% of low carbon products are profitable without a green premium.

He gave the example of demand for Nylon 66 carbon credits in the auto industry, which use the high performance plastic in car airbags and across electric vehicles. Automotive clients are not willing to pay a green premium for a low carbon nylon 66, so his company creates an offset and sells it separately.

Bringing the third party technology and systems together has led to the abatement of 50 million tons of Nylon 66 a year in China with a single project producing 6 million tons of carbon credits annually.

The consultant explained that there's a big price difference between avoidance credits generated by measures such as planting trees that prevent CO₂ molecules from entering the atmosphere and removal credits, generated from technology like Direct Air Capture (DAC) that suck CO₂ from the atmosphere. As DAC is novel, it can command \$150 to \$200 a ton compared to \$3-35 a ton for forests and mangroves, he said.

There's also an anomaly in the system as a cement facility that captures its own carbon would be considered 'avoidance' while DAC is classified as 'removal', according to the consultant.

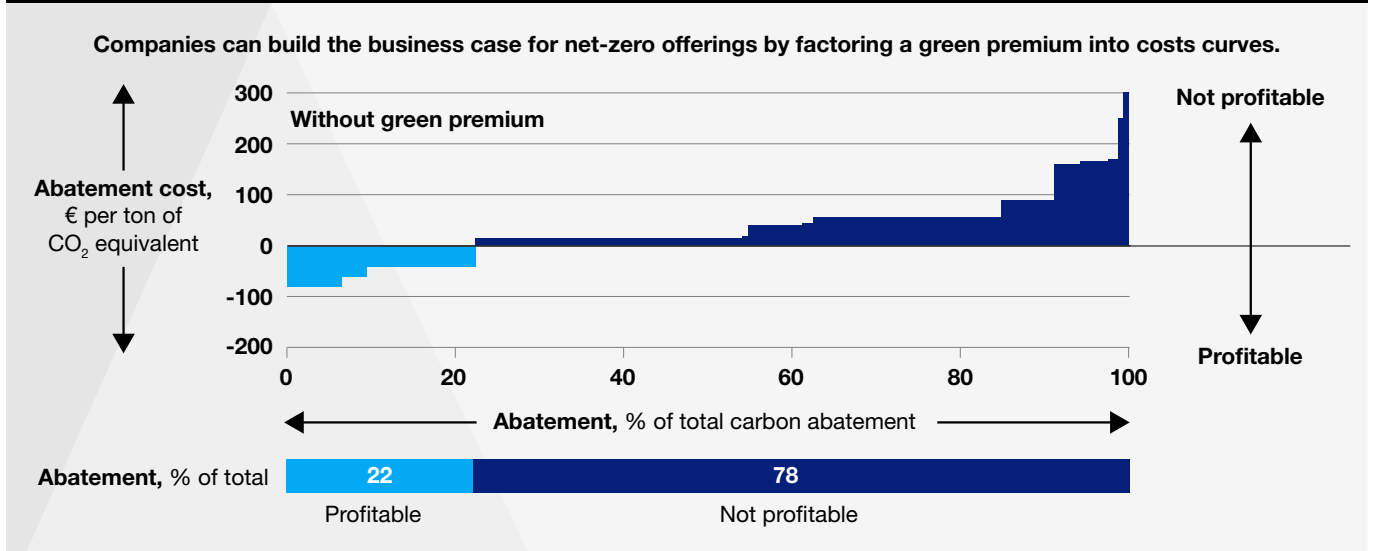
“Science based targets put a premium on removal. If this changes and we have better incentives for carbon capture and storage on cement facilities and there’s no distinction between removals and avoidance, then all of a sudden, the markets wouldn’t pay a premium.”

The high price of removal credits can also be attributed to controversy surrounding the legitimacy of some of the nature-based avoided emissions projects in recent years, whereas carbon removal technology is more transparent around its impact. A report last year asserted that rainforest offset credits in parts of Africa were largely worthless as the rainforest was no longer under threat.

The consultant said the biggest risk to the voluntary carbon markets lies in its voluntary nature which means that when the economy enters a more challenging period like over the last couple of years, companies worry more about their profit and loss statement, so it’s the first thing to be jettisoned.

“I hope that the use of carbon offsets goes down over time,” he said. “I really believe that it’s a transitional product over the next 15 years because as companies start to mitigate their own emissions their reliance on offsets or investments in external projects will start to reduce.”

Figure 1: Illustrative marginal abatement revenue and cost curve for net-zero offerings



Source: McKinsey & Company.

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