THE CLIMATE TRUST

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Ringing in the New Year with a Forecast of the Top 10 Carbon Market Trends

The Climate Trust's annual predictions on carbon market policies and ideas that will matter in 2018

PORTLAND, Ore. – The Climate Trust, a mission-driven nonprofit that specializes in mobilizing finance for conservation projects, announced its fifth annual prediction list of carbon market trends.

The trends, which range from the maritime industry following aviation's lead in carbon reduction commitments to increased dismantling of federal agencies addressing climate change, were identified by The Climate Trust based on interactions with their diverse group of working partners—government, investors, project developers, corporates, and the philanthropic community.

"In the face of federal inaction, the momentum around climate action in 2017 was extraordinary," said Sean Penrith, Executive Director for The Climate Trust. "When our team gathered together to discuss our predictions for the New Year, it quickly became apparent that despite the big lift ahead of the U.S. (and the world) related to climate change, the room was filled with an overwhelming sense of positivity and anticipation to see what we could collectively accomplish in another year's time. We hope that sentiment is reflected in our forecast."

1. **More links will be added to the cap and trade chain gang.** North America has had two regional cap and trade markets operating the last several years, the Western Climate Initiative (WCI), involving California, Ontario and Quebec, and the Regional Greenhouse Gas Initiative (RGGI), involving nine northeastern states. Mexico has just crashed the party announcing in mid-December plans to launch a national mandatory market in August 2018. The list of jurisdictions linking up with cap and trade markets will only grow in 2018. New Jersey and Virginia are on a clear pathway to join RGGI, and several states that are already part of RGGI are considering expanding cap and trade to the transportation sector. Oregon is also poised to join WCI in 2018, as passing cap and trade legislation is one of the Governor's top priorities. Ontario is facing political uncertainty around its future in WCI with the party leading the polls pledging to pull out of WCI and pass a revenue neutral carbon tax instead. Despite this pledge, the challenges of pulling out of the linked market and broad business support in Ontario belie that a change in government doesn't necessarily mean the end of cap and trade in Ontario. A dark horse jurisdiction may also emerge in 2018. Expect 2018 to be the year of continued momentum towards expanding cap and trade markets, and the emergence of new states examining whether such an approach makes sense for them.

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2. **States, U.S. cities will quicken the pace in developing climate change adaptation plans.** 2017 was a horrific year for natural disasters that wrought havoc throughout the United States. By October, natural disasters had already cost the United States over $25 billion according to the National Oceanic and Atmospheric Administration, and that was before wildfires broke out in southern California. PBS reports that 2017 is on track to break records for the number of major natural disasters in a year. With many of these events crippling major U.S. cities, officials and citizens will be thinking hard about how to prepare their cities for a future with more frequent and stronger disasters. Some cities have already taken the lead on developing and implementing climate adaptation strategies, such as Miami Beach's efforts to elevate streets and install pumps. In 2018, we predict that a record number of cities will begin the process of developing climate change adaptation plans.

3. **Institutional investors will increasingly count social and environmental impact as part of their fiduciary obligation.** Foundations will follow McKnight's early lead by committing to invest endowment dollars (not just grant money) into climate mitigation and social improvement projects. Likewise, university endowments will adopt policies that address climate change in their investment portfolios as an integral part of their fiduciary commitment.

4. **Shipping will follow aviation's lead and agree to a carbon reduction commitment that will rely on offsets at the onset.** A few years ago, the biggest future carbon market you've never heard of was created when the international aviation sector agreed to carbon reduction targets. Given the international nature of airline travel, aviation emissions have proven difficult to regulate. The establishment of a commitment, overseen by the United Nations International Civil Aviation Organization, and the creation of an offset market to allow the sector time to develop biofuels and fuel-efficient fleets, has provided a roadmap for other multi-national industries to follow. The clear candidate to follow this blueprint is the maritime industry. Although a growing number of shippers have called for some form of regulation, developing countries, which are dependent on ships to transport their manufactured goods to major markets in developed countries, have called for a go-slow approach. However, annual shipping emissions are already 30% greater than those from air travel and forecast to grow by another 17% if left unchecked. Meeting the Paris commitments will require progress on developing and agreeing to a framework for the shipping industry—just like in the aviation sector.

5. **The first year of the Trump administration has seen deregulation and dismantling at agencies working to combat climate change.** While President Trump has made broad and sweeping actions to reverse progress on addressing climate change, such as withdrawing the United States from the Paris Agreement, deliberate and quiet efforts are having a powerful effect at the agency level. Scott Pruitt, Director of the EPA, has taken a meticulous approach to deconstructing decades of regulation and basic environmental protections, including repeal of the Obama-era Clean Power Plan, which sought to curb greenhouse gas emissions. The Department of the Interior announced plans to hold the largest-ever auction of oil and gas leases in the Gulf of Mexico, and many scientific and administrative posts have been filled with people hostile to curbing greenhouse gas emissions. With at least three more years of the Trump presidency to go, we predict that the EPA and offices focused on climate change in other agencies will see further deconstruction in 2018.

6. **The Trump administration's intransigence on climate science will backfire in the 2018 midterms.** Republicans remain the only major party in a global democracy to deny basic climate science. With intensifying weather, scientific consensus that anthropogenic greenhouse gases are to blame, and cheap renewables and electrified transportation demonstrating that mitigation can be affordable and improve our lives, the position of the Trump administration and many Republican party members simply cannot be sustained. In 2018, we expect Democrats to increasingly fight for the economic and environmental benefits of carbon pricing and look to chastise climate-denying legislators for their ignorance and intransigence. This strategy (which David Roberts calls "agnoism") will pay dividends in the 2018-midterm elections, and Republicans will (slowly) reconsider the tenability of their outdated position on climate change.

7. **U.S. companies will voluntarily, and increasingly, report on financial policies and performance related to the environment and social responsibility.** The Sustainability Accounting Standards Board (SASB) recently published its Exposure Draft Standards for 79 industries, with the public comment period having closed on December 31, 2017. We predict there will be a continued increase in the number of U.S. companies that choose to include discussion of their policies and performance regarding the environment, social responsibility and similar matters in their required external reports or in what is often referred to as a sustainability report. Even though the standards are not legal requirements, we predict an upturn in voluntary acceptance that will inspire other companies to feel obligated to provide similar disclosure to their stakeholders. Due to the prominence and credibility of the SASB Board members, the SASB has generated considerable momentum in a short period. The end result is a win-win for the companies and capital markets because the disclosures are not onerous and focus on financially material sustainability factors that result in providing extremely useful information for investors.

8. **Public support of dairy digester development will shift to credit enhancements to mitigate risks for private investors.** Explosive growth in the development of California digesters will continue in 2018. In 2017, California awarded grants to build 18 new digesters over the next two years (which will almost double the number of digesters in the state). With double the funding available in 2018, we expect more than 35 new projects to be supported. As projects become more cost-effective, their technology becomes increasingly understood and their impacts are proven, private capital can, and should, play a greater role in building new digesters to meet the state's goals—significantly reducing methane emissions. To encourage this transition, expect climate-policy advocates, project developers, and the dairy industry to increasingly advocate for shifting public support from grant making to credit enhancements that mitigate risks for private investors in dairy digesters. In 2018 we expect to see a final design for California's pilot financial mechanism to be proposed. We also expect a large number of advocates will line up to fund this mechanism, with at least $25 million to backstop price guarantees for the environmental markets that drive project economics but face real regulatory risk.

9. **Climate smart agriculture and soil health will gain prominence in 2018.** Collective activities in agriculture, forestry, and land use change are responsible for 21% of our global emissions, second only to the energy sector. The international 2017 climate talks in Bonn released the blockade restraining the agricultural sector from playing an active role in solutions for climate change. At the 23rd Conference of Parties (COP), the Subsidiary Body for Implementation (SBI) and the Subsidiary Body for Scientific and Technological Advice (SBSTA) took up the charge to "address issues related to agriculture." The path set by the SBI and the SBSTA now engages agriculture as a strategic priority to

develop on-the-ground practices that help curb greenhouse gas emissions. The Nature Conservancy found that natural climate solutions offers over one-third of the cost-effective climate mitigation we need by 2030 to achieve our Paris target of a less than 2 °C world. We will witness agriculture step up and adapt to climate friendly practices in the face of global population growth and the impacts of rising temperatures on smallholder farmers. The Sustainable Development Goal of achieving a hunger-free world by 2030 is being challenged by these mounting influences. The outcome of COP23 means that the theory, research, and discussions on agriculture will finally turn into tangible action on the ground.

10. **Global health implications of climate change will sound an alarm for insurance markets.** Climate change is on track to deliver "the biggest global health threat of the 21st century," according to the British medical publication, *The Lancet*. Increasing global temperatures will aid the spread of vector-borne diseases like Malaria, Lyme disease, Zika virus, and water born illnesses such as Cholera and Toxoplasmosis. We have already begun experiencing the increased mortality risks from flooding, intense precipitation, and high summer temperatures and fires. Sadly, we will witness even more pronounced health impacts this year. While the property and casualty insurance market has become aware of the effects of a changing climate, the healthcare sector is just starting to understand the import that this will have on health care costs, services, and delivery. Ceres conducted research that ranked 148 of the largest insurance companies in the country. While Blue Cross Blue Shield of MA recognizes climate change as a significant threat to public health, a few companies surveyed by Ceres stated that they do not believe climate change is a material business risk. We will see an awakening in the health insurance sector in 2018 and an effort to follow European insurers who are active in combatting and adapting to climate change. The former CEO for AXA SA, Henri de Castries, said in his 2016 speech, "We have no choice, a 2°C world might be insurable, a 4°C world certainly would not be." The alarm clock for the health insurance industry will sound off loud and clear in 2018.

"The Trust's two decades of expertise in this space has laid the foundation for our team to make sound carbon market predictions year after year," said Sheldon Zakreski, Director of Asset Management for The Climate Trust. "In fact, a record number of our 2017 predictions hit the mark, including environmental justice groups taking an active role in climate policy decisions, private industry picking up U.S. government slack, the California Air Resources Board prevailing in a high-profile lawsuit, China taking the lead in carbon markets, as well as an alarming number of U.S. citizens becoming climate refugees, with a related surge in momentum for global climate litigation."

Director of Investments, Kristen Kleiman, added, "In particular, California's move to recommit to their cap and trade system provided a valuable market signal to support linkages and increase jurisdictional participation in offset markets. Riding this wave of market interest, The Trust is now poised to fully commit our $5.5M pilot carbon investment fund, and launch our $100M 10-year private equity Fund II in 2018."

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