SM190 | 8.17.2024
Summer Playlist 2024 | Episode 6
Hannah Hauman, Global Head of Carbon Trading, Trafigura

Our Summer Playlist continues this week with Hannah Hauman, Global Head of Carbon Trading at Trafigura. David Greely sits down with Hannah to discuss how seemingly separate EU regulations on corporate green claims and reporting are coming together to create a new definition of net zero and a new approach to driving corporate climate action.

Hannah Hauman (00s):
So when we are thinking about how markets solve, a critical piece of this is what is that problem exactly? How do we define that quantity or that exposure that we are now needing to mitigate, to manage? If you can measure it, you can manage it. That's exactly what's taking place here in really creating that bedrock or fundamentals of what that net zero picture looks like.

Announcer (23s):
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David Greely (01m 06s):
Welcome back to our Summer Playlist 2024 on SmarterMarkets. I'm Dave Greely, Chief Economist at Abaxx Technologies. Our guest today is Hannah Hauman, Global Head of Carbon Trading at Trafigura. We will be discussing how seemingly separate EU regulations on corporate green claims and reporting are coming together to create a new definition of net zero and a new approach to driving corporate climate action. Hello, Hannah. Welcome back to SmarterMarkets.

Hannah Hauman (01m 34s):
Hi, Dave, great to be back.

David Greely (01m 36s):
Well, I have been looking forward to having you back on the podcast. Thanks for being here. I think we have all become accustomed to thinking about carbon markets in terms of voluntary and compliance markets with corporate action driven by climate commitments in the voluntary markets and by government regulation in the compliance markets and I have been looking forward to talking with you because you see a third approach now taking shape, particularly in the European Union and you see this approach taking shape through the combined effect of seemingly separate climate regulations, addressing issues like corporate sustainability reporting, the certification of carbon removals reductions and corporate green claims. More specifically, these include the EU Corporate Sustainability Reporting Directive, the CSRD and the EU Carbon Removals and Carbon Farming Certification, CRCF Regulation and the Green Claims Directive and I want to dive into each of these with you, but first, could you start us off by giving us a roadmap so that we can understand how these types of regulation could come together to create, in your view the first regulatory defining of net zero?

Hannah Hauman (02m 45s):
So as you said, we will talk a lot about Europe today, but in reality this is a trend that we are seeing playing out globally, specifically that governments are increasing their pace on legislation, quite ironically, as corporates are starting to slow the pace on their side. So what we are now seeing is really the inflection point as that government policy is now actually conforming into policy legislation and ultimately law and these really take different kind of forms and shapes and you mentioned a few of those, but the way to think about the overarching framework and how they work together is we have elements like CSRD, which is really talking about carbon accounting. We have the CRCF, which is talking about carbon removals or the quality of what a net and net zero looks like and then finally the EU green claims, which is exactly what it sounds like, talking about how companies actually account for their missions reporting, how they communicate this to investors and consumers alike.

David Greely (03m 46s):
And so let's dive into those details. Let's start with the CSRD. What does that require and why is it important?

Hannah Hauman (03m 54s):
So the CSRD is a very large piece of disclosure legislation that my technical colleagues could go on and on about in terms of the intricacies. But in short, what it is a mandatory reporting requirement for corporate emissions accounting for scopes one, two, and three. This also requires reporting on how companies are set up to meet their targets, where are the risks to achieving those targets, and then what does that look like as they progress into 2030 and net zero. So in short, what this is really looking at is this is now regulating corporate emissions accounting akin to financial reporting for much greater transparency and visibility and importantly standardization of these processes across industry.

David Greely (04m 38s):
Yeah, and from a US perspective, I think it automatically in my mind, recalls the memories of Dodd-Frank and when you start to put the weight of financial reporting onto sustainability reporting, which started off a number of years ago, people often viewed it skeptically as kind of a marketing effort as opposed to a real disclosure. So what does it mean for a corporation to have its emissions reporting, accounting and claims being written into that financial reporting, and how do you see it affecting corporate climate behavior?

Hannah Hauman (05m 10s):
So I love the Dodd-Frank analogy and think it's exactly on point and in with regards to sustainability, what we have typically seen is that target setting corporate sustainability reports has really kind of begun and ended in the ESG ivory tower and what this is now changing is this is now bringing it into investor claims, financial claims. This is now actually putting it at the heart of business, which now really allows companies to make a much greater cultural change towards competing on these metrics. So now we're involving the CFO's office, the treasury's office, now the commercial business lines, which changes this from, I would say a, an overall high level target to now a core aspect of how companies do business and how companies compete, be that for investment dollars for financing for customers in the future. So really changes the specter on what business as usual looks like.

David Greely (06m 02s):
It's interesting you say it, it changes how companies compete. Could you give an example of that?

Hannah Hauman (06m 08s):
Absolutely. So we see, I would say a lot in the media about things like sustainability, linked financing, lower carbon kind of product alternatives. But the reality is that very few of these are standardized approaches today, and I would say are more experimental by producers or by banks to really be able to begin to reward decarbonization efforts. What this now changes is we are no longer calling things quote unquote low carbon or generally sustainable. We are now increasingly standardizing the metrics on how companies can compete for those extra five basis points from their finance banks. For example, when we are looking at it from an investor perspective, again, we're now increasingly objectifying those metrics and really allowing companies to again, use this as a mode of offense and not necessarily just defense.

David Greely (06m 55s):
So is the EU alone in putting sustainability reporting into financial behavior or other countries following suit?

Hannah Hauman (07m 03s):
So the EU is definitely first, but absolutely not alone. We are seeing other countries ratifying their own version of CSRD, so places like the UK, Singapore, Australia, even China, that are all really kind of putting their own spin on these requirements, but at their core are requiring regulated reporting of emissions accounting for corporates and in with increasing inclusion of scope three emissions as well related to company supply chains.

David Greely (07m 3s0):
And I wanted to turn to, as you said, putting the net zero, you know, the second piece of regulation, you mentioned the EU carbon removals and farming certification, the CRCF regulation. How does that put the net, net zero,

Hannah Hauman (07m 44s):
The CRCF? And again, if we kind of bring it back to the frame of if CSRD is the accounting, we are now defining the quality of what that net in net zero means. So the CRCF is an EU mandated and administered program, which is now the first ever EU wide metric on how to define certify, monitor, and issue carbon removals in Europe and why that's important is again, you now have an EU registered body that is administering the scheme, defining its protocols and defining what materially is a net or removal within the scheme.

David Greely (08m 23s):
This is a getting down into when is a ton, a ton, how does it get into that question of when a ton reduced or removed counts as a ton emitted?

Hannah Hauman (08m 33s):
So this is not surprisingly a key point of the debate at the moment. They are currently in the task forces in really working to define exactly how rules should translate across different methodologies. What we do know now is that we will have engineered removals, so things like direct air capture, and we will also have nature-based removals. So things like forestry or soil carbon or carbon farming will also be a part of this. What's not clear yet is how the different rules will apply to these different forms of carbon removal. So very similar to let's say even fossil emissions, we account for methane emissions differently than how we account for carbon dioxide emissions. They have different durations, they have different materiality on its environmental impacts and removals are no different. So we need those amendments and adjustments for those protocols that ensure that we have that. Like for like even beyond that, we are also now talking about how do we account for fossil based emission versus a biogenic emission and how does that impact the equivalent removal that is required to ensure that kind of like for like accounting. So again, there's a lot of working groups and a lot of scientific bodies tackling this problem right now, but their current approach is meant to be publishing in the next 12 to 18 months on what that definitive protocol is for those different types of activities.

David Greely (09m 52s):
And I wanted to ask you, how does that work that these groups are doing build upon or align with a lot of the work that's happened in the voluntary carbon markets? So for example, do you see certain methodologies that have been developed in the voluntary carbon market side, many of which, you know, went back to the CDM days and of olive? Do you see those being like picked out as appropriate or are they kind of starting more blank sheet of paper

Hannah Hauman (10m 19s):
Without trying to read too many minds and project onto the regulators I would guess it's gonna be a mix of both. So some of these technologies or in effect brand new. So direct air capture is very nascent today, but will be a large source of removals in the future and that requires its own scientific studies and protocols that have never existed in any form. In other instances, we might be able to borrow infrastructure from the previous versions of the CDM and the voluntary market around what is kind of the best versions of a forestry methodology and how do we best adapt that to regulation. So I think if you look at the working group, it's no surprise that you will have a lot of leading industry experts from both regulatory crediting as well as bond tree crediting schemes that are really working to approach exactly that. What is the right blend? How do you take the best of what's available and improve upon it further with the best technology we have now.

David Greely (11m 13s):
And we have had, you know, groups on the voluntary side like the ICVCM, the VCMI, you know, doing similar work in what a high integrity credit is, what is a quality claim. It seems like the EU is kind of getting its foot in the door here in a way by offering a carrot that corporations will be able to count the benefits of their removals on the European continent after 2030 toward their EU ETS obligations and of course, you know, following the bad experience Europe had with the clean development mechanism under the Kyoto protocol, Europe's generally been, you know, in my view, low to allow outside credits into its trading scheme. Why do you think the EU is offering this carrot now because it seems like a pretty big deal that they will be offering these potential outside emissions credits to be used.

Hannah Hauman (12m 04s):
So first I would think about it in a slightly different way. It's maybe not necessarily a carrot for corporations to avoid paying EU VTS, for example and it's much more of a price signal to signify investment in carbon removals on the continent. So this goes far beyond a corporate really looking to mitigate cost. This is really about how does Europe meet its net zero goals on the continent and drive capital investment to those places that's required. So we are now creating a secondary supply source potentially alongside the government auctions if they are to allow this to be included in the EUETS. The second piece of this is why is this different from the CDM days and I

think it's really important to look at what is the design and what is the intent. So if you look at previously in Europe, there was a period where you could import credits from international sources.

Hannah Hauman (12m 59s):
These were often renewable energy projects and what happened was the design and intent of that program was really to drive climate finance internationally, but not necessarily to need to export on the other side. So no surprise, it was extremely effective. In fact, probably too effective at driving that international climate finance where you had a limited demand within Europe under the regulation and effectively unlimited supply globally, but it delivered against that goal and aim of how do you drive international climate finance. The new EU CRCF is vastly different in both that design and intent. Firstly, it is primarily focused on European borders, so how do they drive investment within the continent. It's very particular on the qualities that it will allow which is what we discussed previously on those removals. How do we assess like for like how do we assess duration, things like permanence and equally its core objective. Yes, there is a climate finance element, but the core objective is really around the carbon accounting. And I think you'll see the protocols and methodologies really, really reflect that.

David Greely (14m 07s):
Why do you think accounting is so important as an economist by background? I have had to learn over the years that, you know, while economics is important, accounting seems to drive behavior. How important is that there? Setting the accounting for net zero?

Hannah Hauman (14m 20s):
I'm not an economist by background, but I have always been a trader and specifically a trader within physical markets. So when we are thinking about how markets solve a critical piece of this is what is that problem exactly, how do we define that quantity or that exposure that we are now needing to mitigate, to manage? If you can measure it, you can manage it. That's exactly what's taking place here in really creating that bedrock or fundamentals of what that net zero picture looks like.

David Greely (14m 48s):
One of the interesting things is, you know, we started the conversation with, we're talking a lot about the EU, but of course this is more global movement in general and one thing we've seen broadly is the EU trying to extend its regulatory reach and I am curious in this case, how does this allow the EU to extend its regulatory scheme, the ETS, into the voluntary carbon markets?

Hannah Hauman (15m 12s):
So I think I would probably flip that the other way around, in fact. So what we often see is that whenever there are increased regulatory measures on defining what eligible credits look like, that the voluntary market actually borrows from the regulator as much as the other way around. So for example, we have markets like Australia, which is a regulatory scheme. You have credits that are really certified by the government and managed in terms of protocols and issuance and in fact you actually see a lot of corporates purchasing those regulatory units for voluntary claims. And the government has a system whereby corporates understand how they can account for it, how they can communicate it, so on and so forth. We recently have had a new scheme in Singapore, which is also based on credits, but this time internationally sourced credits and very similar effect there. We are now seeing corporates wanting to also look at the Singapore regulatory credit as a means for its own voluntary action. So I don't necessarily think it's a, let's say one-way system, and it's very much that corporates will be informed by the regulation, and regulation will be informed by what's happening in the voluntary space.

David Greely (16m 23s):
They want to take it now to the last piece of regulation, the EU green claims directive, which regulates how companies may talk about what they are doing on the climate side and when you look at that, how does that regulation of the claims that can be made, what is that requiring and why is that important to putting together these three legs of the stool I guess.

Hannah Hauman (16m 46s):
I am going to use some words that you may have heard previously. Words like standardization, objectivity, robustness, no different to let's say that demand side of the equation, which is that emissions accounting, we need to define the quality, but then we also need to define how that is actually being used in the market and on what basis. So today we see a lot of descriptions in retail goods in corporate advertising, whether that be carbon neutral or low carbon. There is not really clarity on what that means as we look product to product and firm to firm. So what's really interesting about the EU green claims directive is we are now getting in effect a gap accounting version of what is the appropriate way to claim offsets, talk about decarbonization process and really actually define what

makes a product carbon neutral or low carbon, and what were the scientific objective measures that companies used to get there. So what we are really looking at going forward is kind of this concept of calorific content that we think about when we think about food, but again, moving more towards what is that objectively low carbon number, not just descriptive, categorical.

David Greely (17m 58s):
And so now we, we put these three pieces together, we have a regulatory definition of what constitutes a ton of a carbon emissions reduced or removed rules on how a green claim, including a net zero claim may be made and those claims now carrying the legal weight of financial reporting. So how do you see this regulatory approach reshaping the way we need to be thinking about the potential path forward in the carbon markets?

Hannah Hauman (18m 24s):
What's interesting about this is, as you mentioned, this is the three-legged stool. They look from the surface as though they are three very independent regulatory tracks, but in reality they are all moving at the same pace and really seeking to deliver at the same time for good reason and that's really because we're moving out of what I would say is a pure voluntary kind of guise of what corporate action looks like as we are now not only regulating the claims, but we are also regulating the underlying accounting and progression of those targets. So as we move forward, I think we are thinking less about these as completely two separate types of markets in terms of voluntary and regulatory, and we are really thinking about regulated markets, which in their own right are already increasing in terms of sectors, geographies, products that they extend to, but now also a regulated corporate commitments market, which is now really again, moving away from that sustainability report as primarily focused on graphics and much more focused on what are the objective measures that companies are taking towards climate action and again, how do they compete on the basis of decarbonization and progression towards targets.

David Greely (19m 34s):
It's interesting because I think for a long time many of us have been looking for a way of, you know, do the voluntary markets and the compliance markets become one market at some point, and how's that going to happen. Is it full scale compliance markets developing as Paris agreement gets more and more operationalized and the VCM withering away, is it that they come together somehow through the Article 6? When you look at it now, do you see this more regulatory approach where we kind of have these patchwork of across geographies across countries? Do you see that as maybe the more interesting route right now? How do you think we get there Or do we.

Hannah Hauman (20m 13s):
I think it's the necessary route, I think to, to quote the Paris agreement common but differentiated approaches. Because the reality is that different countries, but even different sectors are on very different trajectories to meeting those net zero paths. So when we think about, let's say convergence of voluntary into regulatory, I always think that's a bit of a misnomer because the reality is that regulatory markets aren't even homogenous and they reflect their own set of circumstances and their own levers that they're trying to pull when it comes to how you price carbon and how you direct private sector investment into carbon reductions and carbon removals. So I think the more likely approach is that we will continue to see, let's say overlapping, but slightly divergent policies around the globe that are really moving towards, I would say the same singular goal, which is out there on the horizon at 2050. But in reality we'll look very different on different timescales. So 2025 we'll see a lot more divergence than we will in 2045, for example. As we have a lot of different players on different starting points with different technology available and equally different abilities to pay.

David Greely (21m 24s):
As you said, you are a trader. How do you think about it with these different regulations coming in on different timescales you know, when you look at the markets, how do you look at it in terms of opportunities and risks that are out there now?

Hannah Hauman (21m 37s):
So there's certainly a lot of both, especially in markets where we are policy driven. So this is a great thing because that means that we are generally moving at the speed of what the latest technology allows, but it also means that long-term investments can be challenging are subject to what we call pen stroke fundamentals. So if a legislator changes tomorrow, that might now change the paradigm in how you are operating, but that's the reality of these markets and they're meant to kind of continuously evolve. What we do see from our customers is that this also just presents a lot of inherent risk, a lot of unknowns, especially when we are trying to make plans for 2030, for 2050. So we really work with a lot of clients across a lot of geographies that have these overlapping exposures that

have, let's say, very different exposures depending on which asset or which region we are looking at and are really looking for how can they reduce that risk, how can they increase that surety and ultimately get along with moving down kind of their target

David Greely (22m 40s):
And thinking across different areas with different pen stroke risks. One thing that's been interesting to me is we've been discussing EU regulations and directives, but then what does it mean for the rest of the world and I mentioned a number of countries are adopting similar regulations and sometimes similar approaches, but I was wondering also, are there lessons from the EU's carbon border adjustment mechanism, CBAM about the ability of Europe to in effect export its carbon price and regulatory reach to the rest of the world. How do you see that the ability of EU to kind of get others beyond its borders to be exposed to this carbon price in a way through these regulatory mechanisms?

Hannah Hauman (23m 20s):
So I think this has been probably the largest catalyst in global regulation certainly this year, and I am sure will extend over the next few Europe's, CBAM or its carbon border tax is effectively pricing on imports the same price on carbon as what it is holding its domestic installations to and that in effect is exporting its price unless the country of origin is also pricing carbon at an equivalent level. So what this now means is Europe's obviously protecting its long-term ambitions and protecting its domestic manufacturing, but equally what we are now seeing is countries elsewhere now preparing for their own domestic regulatory schemes as they would much rather have those carbon revenues domestically versus surrendering to the EU. So this looks like expansions of existing schemes, places like China, for example, overhauls in Australia, new schemes in Japan and Korea, and also brand new domestic schemes altogether.

Hannah Hauman (24m 22s):
So places like India, South Africa, Brazil, that really are exposed to this carbon border tax and would much rather be collecting those carbon price revenues at origin. So that is extremely catalytic and we are seeing a lot of legislative advancement on the back of that. And really for that kind of 2026 timing when the EU CBAM comes into play. The analogy here with CSRD is actually very similar. So first, CSRD requires not only scope one and two reporting, but also scope three or supply chain emissions. So this now effectively entraps global operations that are related to those supply chains in terms of this disclosure and reporting requirement. Further, in terms of the companies that are actually obligated under CSRD, it is not just EU listed companies, it's not even just EU incorporated entities, it is anyone who sells products in the EU in terms of its final reporting requirements. So this is now again, just exporting this obligation and this disclosure requirement globally and generally what we see is that Europe is first, but others are not so far behind. So while this is a very large piece of European legislation, in reality we see this as a new global regulatory framework.

David Greely (25m 39s):
Yeah, and you mentioned earlier that you know, you manage what you measure and it seems like the path is we are gonna force you to measure it. Once you're measuring it and reporting it, then you are going to manage it and I guess maybe to finish off, one thing I was curious about is these are very detailed, specific pieces of legislation and I am curious for people who are trying to stay on top of how carbon markets are developing, how do you approach it? How do you look through the lists of acronyms that are coming out, the policies, the directives, and kind of see through those individual dots to kind of get the pointless picture, you know, like an impressionist painting. How do you step back and start to get a sense of how the big picture is developing?

Hannah Hauman (26m 22s):
That's a great question. I like the impressionist analogies. I think that's very accurate. So I think the simple answer is if you are reading about this in your spare time, it, it can be extremely difficult. I think in these markets and in regulatory advancements generally, there's a lot, a lot more noise in there, a signal, but equally you kind of have to take it all in to be able to distinguish one from the other. I think one of the benefits that we have is we're steeped in context whether we like it or not, you are constantly swirling with what regulators are saying in different parts of the world, how policy is impacting your customers, your own operations, how you're preparing for your own business. So it's a lot to keep track of, but I think maybe to use your earlier analogy of Dodd-Frank, at the time it seemed terribly complex and impossible. And I remember, you know, the technicalities and the working groups that that we went through at the time to be able to prepare and now it's every day and it's commonplace and it's just a part of how we do business and I think that's the reality of what's coming when it comes to this enhanced level of climate disclosure and regulation. For now, it's a lot of noise, not a lot of signal, but going forward I really think it's gonna be redefining what that business as usual looks like.

David Greely (27m 35s):
So it's going to be hard for some of us to keep up just by reading a couple books on our summer beach reading list. You are steeped in it all the time. I imagine your reading list might be something other than carbon markets, but I don't know. So I will ask you because for our summer playlist series, it's become a tradition to ask each of our guests what's on their personal beach reading list this summer. So before I let you go, I wanted to ask you, what are you reading this summer, Hannah?

Hannah Hauman (27m 59s):
So not planned at all, but very much aligned with that previous question, how to focus on the signal over the noise. Actually rereading two books at the moment, Atomic Habits and Essentialism, all about how to focus on less but better.

David Greely (28m 15s):
Thanks again to Hannah Hauman, Global Head of Carbon Trading at Trafigura. We hope you enjoyed the episode. We will be back next week with another episode of our Summer Playlist 2024. We hope you will join us.

Announcer (28m 29s):
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