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Financing the Energy Transition | Episode 6
Leah Wieczorek, Vice President, Global Carbon, Macquarie Group

We continue our Financing the Energy Transition series this week by welcoming Leah Wieczorek into the SmarterMarkets™ studio. Leah is Vice President of Global Carbon at the Macquarie Group. SmarterMarkets™ host David Greely sits down with Leah to discuss the role that banks like Macquarie play in scaling the carbon markets and in financing the energy transition.

Leah Wieczorek (01s):
Whenever there is a problem, there is a room to provide a solution and deliver value. I think generally speaking, there's a lot of financing out there for carbon projects and the three major challenges that I see are: one, some investors that are too focused on specific project types. Two, early stage projects that might have issues to access financing for feasibility studies. And three, bullish investors that don't necessarily understand the underlying risks for certain projects, which can include corresponding adjustments, other political risks, and also the actual price that you can sell offsets for as well as the drivers for the voluntary carbon market.

Announcer (41s):
Welcome to SmarterMarkets, a weekly podcast featuring the icons and entrepreneurs of technology, commodities and finance ranting on the inadequacies of our systems and riffing on ideas for how to solve them. Together we examine the questions. Are we facing a crisis of information or a crisis of trust and will building smarter markets be the antidote?

David Greely (01m 06s):
Welcome back to financing the Energy Transition on SmarterMarkets. I'm Dave Greely, Chief Economist at Abaxx Technologies. Our guest today is Leah Wieczorek, Vice President Global Carbon at Macquarie. We'll be discussing what role banks like Macquarie play in scaling the carbon markets and in financing the energy transition. Hello, Leah, welcome to SmarterMarkets. It's good to get to talk with you again. For our listeners we met through the WIMAR SG event that's the Women in Mining and Resources in Singapore held an event in September on Carbon Markets in the Net Zero future where I was a moderator and you were a panelist. Really great discussion, and we have it on our website for anyone who wants to go back and watch the event. But it left me wishing that I had more time to talk with you and one of the things I've wanted to talk with you about more is the role that banks like Macquarie are playing in financing the energy transition in carbon reduction projects. In particular how banks are or, you know, are not acting as financial intermediaries between the carbon reduction project originators and the companies wanting to use carbon credits to offset some of their carbon emissions. Before we dive into that though, I know that before you joined Macquarie, you worked for South Pole and led their business development team for Asia, and I'm curious about that perspective, you know, what kind of carbon projects are corporates looking to off take carbon credits from?

Leah Wieczorek (02m 32s):
Yeah, thanks David and very nice to chat with you again today. I think it's not a secret that most corporates with net zero commitments prefer carbon credits from removal projects over avoidance or reduction projects and while corporates should focus on removal projects at the net zero stage, most organizations are still far away from reaching net zero and hence reaction projects will remain an important part of the decarbonization strategy for years. Also, I think when, when looking into the overall supply of offsets, the reality is that most carbon credits out there are still from avoidance projects and while we see many market participants trying to increase the share of removal projects, it is important to note that those projects can come with significant risks, especially we're talking about nature-based solution removal projects that have a project lifespan of, you know, 20, 30 years and we also should not forget that different project types can be relevant for different locations. When a new forest is established, for example, it takes much longer time to get a rich biodiversity, but hundred years of an old forest are very important because they are so rich in in biodiversity.

David Greely (03m 56s):
Can you talk a little more about that preference for carbon removal projects over carbon avoidance reduction projects? Are those carbon removal projects seen as higher quality credits?

Leah Wieczorek (04m 09s):
Yeah, that's a very good question and I think at the moment we see so many discussions going on around the topic on what kind of carbon credits are actually considered high quality. I believe we should not determine what, you know, what project is actually high quality purely based on the type of the project, but rather really look into how's the project design and how is it implemented in regards to additionality baseline assessment, permanence assurance, community engagement, and a general, you know, core benefits and when doing your own due diligence, you'll likely find that the same project type can be designed and implemented very differently with regards to those attributes. So generally speaking, we recommend to our clients to do their own DD either to do it in-house or to hire an independent party to support them with it and obviously needless to say that organizations should align themselves with best practices and stay abreast of the latest developments to really make sure that their strategy constantly involves as the market matures.

David Greely (05m 19s):
And when we were speaking before at the WIMAR event, you've told me that Macquarie's approach of providing equity directly into carbon reduction or removal projects is different from many others and I wanted to follow up with like, why is that important and how would you describe Macquarie's overall approach to financing carbon reduction projects?

Leah Wieczorek (05m 42s):
Yeah, well, climate change is high up on Macquarie's agenda and we want to support the energy transition in the long term, hence we're investing long-term capital into the wider ecosystem, but also investing directly into individual projects. Now, to give you some concrete example when, when talking about the wider ecosystem, we've recently announced an investment into EP Carbon, which you might have heard of before. They are leading offset project consultancy based in the US Now when talking on, on a project level, Macquarie has been working with C-Quest Capital and partners to develop a sub-Saharan Africa cook stove program that is expected to result in abatement of approximately 220 million tons of carbon over the next 10 years, which are then jointly marketed by Macquarie and C-Quest Capital and the broker will distribute cook stoves to around 3.7 million households and is providing meaningful social and health improvements in these communities.

David Greely (06m 48s):
That sounds like a really interesting project. But going back to the point of the wider ecosystem, how important do you see is building out the wider ecosystem and its basic market infrastructure and in particular, what do you see as the most critical areas where that infrastructure is currently lacking?

Leah Wieczorek (07m 07s):
Yeah, well, as we all know, a solid infrastructure is crucial for our market to function. One of the main challenges that the voluntary carbon market faces in regards to developing into a more mature market is the lack of standardization and regulation. I think we've made some great progress over the past couple of months with launching carbon exchanges and rating agencies and, and both can play a very crucial role. So carbon exchanges can play major role in promoting price transparency and also reducing transaction costs for helping buyers and sellers to find each other in a much more efficient way than we have today and meanwhile, rating agencies for carbon projects can also help buyers to make informed assessment on which carbon credit projects have been well assigned and implemented and can be considered high quality offsets. However, due to the lack of standardization, we see many rating agencies coming up with very different kind of ratings for the same projects. Often this is also because they evaluate different parts of the project. However, this can be extremely confusing, for less sophisticated buyer who might not have the sufficient in-house expertise to actually do a technical assessment. So we really see this as holding these two things around standardization and regulation holding back the market.

David Greely (08m 33s):
Yeah, I could see where it'd be very frustrating where people get different ratings for the same project from different rating agencies

Leah Wieczorek (08m 39s):
Exactly.

David Greely (08m 41s):
And, and I'm curious, you know, when thinking about the types of projects that you know, you're financing at Macquarie, is there a certain size or development stage of project that's more dependent on bank financing than others?

Leah Wieczorek (08m 56s):
Whenever there's a problem, there's a room to provide a solution and deliver value? I think generally speaking, there's a lot of financing out there for carbon projects and the three major challenges that I see are one, some investors that are too focused on specific project types, two early stage projects that might have issues to access financing for feasibility studies, entry bull investors that don't necessarily understand the underlying risks for certain projects, which can include corresponding adjustments, other political risks, and also the actual price that you can sell offsets for as well as the drivers for the voluntary carbon market and as mentioned earlier, Macquarie is investing long-term capital into the wider ecosystem and into carbon project directly. We structure all our investments individually and based on what the partner of project means besides that we also provide technical support for projects via our partners like EP, carbon or also in-house.

Leah Wieczorek (09m 59s):
Now when making investment decisions, we typically take a top-down approach into portfolio management. We first assess projects on a portfolio basis and then assess capital allocation that suits our book across the capital structure. In terms of project level decisions, I think we typically are project type agnostic and you know, rather focus on the quality and integrity of the underlying projects. As mentioned earlier, different kind of project types can be impactful for the kind of jurisdictions. We also provide early stage financing for feasibility studies if the project idea passes our initial due diligence process and we also do an extensive amount of due diligence in-house to really make sure that we understand the underlying project and really the associated risks with it and that we also feel comfortable in managing those risks.

David Greely (10m 52s):
I'm curious like if we, if we take it from a carbon project developer's perspective, why does a, why do you think a project originator comes to a bank like Macquarie to finance their project as opposed to trying to find a corporate partner or an investor?

Leah Wieczorek (11m 09s):
I think this really depends on, on what the developer is looking for. A corporate kind of investor, which is also off taker might be only interested in a very specific project because they want to match the project type of their overall communication strategy or they want to have the project as close as possible to their location. Whereas we can be a bit more flexible in general, we build long-term relationships with developers and can then also help the same developer to finance multiple project across, you know, different jurisdictions including different kind of project types and I think also one of the key things why, why developers come to us is because we're quite flexible when it comes to the financing structures. We typically really offer tailored solution based on their needs.

David Greely (12m 00s):
And what do you look for in a project when evaluating it?

Leah Wieczorek (12m 04s):
Well, every project comes with risks and as I mentioned earlier, for us it's really important that we feel comfortable with those risks and that we really feel like we, we understood the risks properly. In general, we look out for the following four criteria if I was to narrow it down, I think number one would really be where's the project based you know, what are the jurisdictional risk, is land ownership clearly defined, which is obviously specifically important for nature-based solution projects where you would potentially acquire concession. Then we would also look into who's developing the project and who's implementing the project on the ground, what is actually their track record, have they done that before. Other things we take into consideration like project duration, how long is the back period and then another very important topic is also about what are the interactions with the local communities on the ground where they consulted prior to project development and what is the actual value add for them. That's obviously not just a snapshot of few of the kind of factors, but these are really some of the first things that we would look at when making a decision whether we would want to proceed or not with the project.

David Greely (13m 19s):
So you have a good idea of the type of project you would like to find. Then I guess there's always also the question of, you know, what types of projects may actually be available. So I'm curious, you know, what challenges do you face in financing carbon projects?

Leah Wieczorek (13m 33s):
Yeah, I think for us finding investable projects is really one of the key challenges. We screen multiple projects on a weekly basis, but unfortunately only a very small amount of those projects actually passes our initial due diligence process and one of the key things that

we struggle with is really the limited commercial sophistication and understanding of risk, which is particularly noticeable in the explosion of new developers without track record and also amongst some of them coming back from CDM days and I think it's important also to highlight here that we need new market participants and we need the market to definitely grow. However, we really need to ensure that it grows with integrity and that the quality of projects is only improving. So project developers that are too enthusiastic about what they can actually deliver can cause reputation or consequences for the industry.

Leah Wieczorek (14m 29s):
So we really need to be careful about the selection with whom we actually want to partner. Yeah, and I mean other, other challenges that that we face is obviously long project duration can increase the overall risks and can come with a very long payment period. Again, I think specifically in regards to nature-based solution projects, that's a big topic and then also it's also about, you know, getting comfortable with all the uncertainties in regards to article six. When you are thinking into investing into a project, one of the key questions that you'll find yourself asking is, will you actually be allowed to expert to come credits of this project and if not, that can significantly change the value of the, of the underlying asset and then I guess like for every large organization, it's also developing institutional learning in an emerging asset class.

David Greely (15m 23s):
And, and when you described earlier your process for evaluating projects and she said, you know, screening new potential projects on a sound like a weekly basis. Now that level of evaluation sounds like a very people and time intensive process, and I'm curious how challenging is it to find people with the expertise in searching for and evaluating these opportunities?

Leah Wieczorek (15m 48s):
Yeah, it's quite challenging. As we all know, the market grow a lot over the past 12 to 24 months and there's only a very limited pool of people with carbon expertise out there. I think we've been quite fortunate to have established a strong team that has expertise across the value chain of offsets, and we have really a mixed skill set in-house. You know, we have posters that have I think developed projects over the past 10 years. We have environmental engineers, structured finance expert commodity traders, et cetera, et cetera. So it's a very broad skill set that we're very fortunate to have in-house.

David Greely (16m 30s):
And when you look at your team and all the people working on it, I'm curious, what are some of the success stories in financing carbon reduction projects that you've had?

Leah Wieczorek (16:39):
I think really what has been one of the biggest success is not actually one, one specific project, I think for us as a team which might also come back to the fact that we have such a mixed skillset in-house, is that we've been really able to finance very different kind of projects over the past two years and when I say different kind of projects I'm talking about, you know, household projects, in least developed countries up to nature-based solution projects into developed countries and I think this was really a big step for us to prove that we as an organization can get comfortable with different kind of project types in very different jurisdictions.

David Greely (17m 20s):
And you know, you, you've talked a lot about how Macquarie is active throughout the, the whole carbon offset value chain and I wanted to move downstream on that a little bit. What types of investors and buyers of carbon credits do you work with. I guess more specifically, what type of organizations come to a bank like Macquarie for carbon credits as opposed to investing directly or buying them on the secondary market?

Leah Wieczorek (17m 46s):
Yeah, we mostly work with me size to large companies that either have obligations in some of the compliance car markets and or that want access to the voluntary car market and in fact, we offer multiple procurement structures to those kind of corporates ranging from spot forward options to direct project investment opportunities. We do see a lot of interest from organizations to get directly involved into projects, but to be honest, only a very small amount of those corporations actually have the in-house expertise to do so and are really willing to take on the early stage development risks. So often this is something where they also come to us and ask us how, how can you help us to provide us with direct access. How do we get comfortable with the risks and so on.

David Greely (18m 37s):
Yeah, and I would imagine, you know, you're, you're balancing a lot of different projects against a lot of different investor needs, and so you're gonna have some inventory to manage on that side. How important is being able to resell credits in a secondary market to your business?

Leah Wieczorek (18m 52s):
The secondary market plays an important role to promote price transparency and to provide organizations with access to car offsets from various project types and locations. Besides that, the secondary market offers a variety of different procurement strategies that can help corporate corporates to secure long-term supply and hedge carbon prices and as we all know, the voluntary carbon market is constantly evolving, new methodologies are being developed and others are becoming less relevant or even faced out. So this also influences buyer's decision on what offsets the volume. So for us it's really important to constantly monitor the market and really ensure that we can act as simply as possible, which also means that we need to have a very balanced portfolio that meets the involvement client requirements, and hence we actively manage and optimize our inventory on, on a daily basis and, and really have a couple of people that are purely dealing with start.

David Greely (19m 50s):
And now maybe stepping back from the, the day-to-day practicalities, I'm curious, like when you look out over, say the next five, 10 years, how do you see carbon finance developing and what do you see as the big unanswered questions that are really gonna influence how carbon finance develops?

Leah Wieczorek (20m 08s):
I think in general we will see more and more participants coming into the market and, and many that will want to provide finance. However, the challenge that we see is to match projects and investors as often the requirements of fall off and I think also specifically, you know, in regards to the whole risk discussion, and I believe how many investors will come into the market and how easy it will be for voluntary carbon projects to access finance will depend on number of developments including how much process will we make in regards to standardization and regulation, how will domestic compliance markets develop. Will they cover X percentage of, of the voluntary market in the near future and if yes, then how will they interact and also how will the whole discussion around Article 6 and corresponding adjustments involve and also influence the voluntary carbon market, which is obviously a point that we were all hoping, I think, to get more clarity out of COP 27, but I guess we'll need to wait for COP 28 in, in in UAE next year to hopefully get a bit more clarity on that.

David Greely (21m 20s):
Yeah, there's a bit of a waiting for Goudeau aspect to some of these things. And where do you see some of the biggest opportunities in carbon finance, in the carbon markets and coming years?

Leah Wieczorek (21m 31s):
As we all know, I think there's not only one solution to solve climate change, and we all need as many solutions as possible that can lower emissions, which also means that we need a vast variety of different project types. So I could not just go ahead and name a single type of opportunity as I think it will really be a mix as it should be in general. I think for us, we want to stay as nimble as possible and we're constantly looking into new upstream and downstream opportunities and really we see where, where we can value at and I think for us, whenever we are entering a new market, we do, we do an extensive study on the jurisdiction and the environmental and social challenges on the ground, which typically helps us to identify what project type could be beneficial and based on the result, we will then really narrow down the, the potential opportunities.

Leah Wieczorek (22m 24s):
But I think, you know, more broadly speaking, it's really exciting to see that at the moment this space is attracting so much interest and attention and I think obviously in 2021, the, the market has boomed quite a bit this year the market has been much slower and I think we've been facing many more, you know, challenging questions around different kind of pain points and weaknesses of the market and obviously there are also many different voices out there with many new people entering the market. But I think ultimately that's really what we need and I think that's what's helped or what will help us in, in the long term to move the market to a more mature market and I think ultimately that's what will bring a lot of new opportunities and also allows new investors to actually access that space.

David Greely (23m 21s):
Thanks again to Leah Wieczorek, Vice President Global Carbon at Macquarie. We hope you enjoyed the episode. Join us next week with our guest, Mark Frayman, Partner at Orion Industrial Ventures. We hope you'll join us.

Announcer (23m 35s):
This episode has been brought to you in parts by Base Carbon. The trading of carbon credits can help companies and the world meet ambitious goals for reducing greenhouse gas emissions, but how do we judge the quality of these projects and how can we ensure that our investments are creating real value. At Base Carbon, we are focused on financing and facilitating the transition to net zero through trusted and transparent partners. It's time to focus on what's important. It's time to get serious on carbon. Learn more at Basecarbon.com. That concludes this week's episode of SmarterMarkets by Abaxx. For episode transcripts and additional episode information, including research, editorial and video content, please visit smartermarkets.media. Please help more people discover the podcast by leaving a review on Apple Podcast, Spotify, YouTube, or your favorite podcast platform. SmarterMarkets is presented for informational and entertainment purposes only. The information presented on SmarterMarkets should not be construed as investment advice, always consult a licensed investment professional before making investment decisions. The views and opinions expressed on SmarterMarkets are those of the participants and do not necessarily reflect those of the show's hosts or producer. SmarterMarkets, its hosts, guests, employees, and producer Abaxx Technologies shall not be held liable for losses resulting from investment decisions based on informational viewpoints presented on SmarterMarkets. Thank you for listening and please join us again next week.