



The Challenge of Financing High Quality Natural Climate Solutions:

MSU Webinar 11.28.2023



Agenda

1. Disclaimer
2. Introduction to AFF and FFCP
3. What is project finance?
4. The scale of the challenge
5. Overview of revenues and expenses in a NCS project
6. The traditional view
7. Challenges to the traditional view
 1. Smallholders and “carbon only” projects
 2. The problem with high quality
8. Potential Solutions

Disclaimers

- 1) Finance is neither my educational nor my professional background. (I am an English major, a Peace Corps volunteer, a program designer, and a fundraiser)
- 2) The FFCP is a very particular kind of carbon project which we believe represents the needed future of NCS projects. Therefore, my view is definitely not neutral (BUT, I have tried to represent alternative ideas and points of view as well).

Twin Goals of FFCP's work:

1. Demonstrate the **financial viability** of creating high quality carbon credits through the engagement of family landowners across the U.S.
2. Through so doing, catalyze the growth of companies and programs to accelerate deployment of high quality NCS on family lands in the U.S. (including but not limited to FFCP)

What is finance? (my words)

Finance is the mechanism by which we balance expenses and revenues over time.

- We do this by paying a capital provider to give us money to cover expenses when we have no revenue, in exchange for a share of the revenue we will generate.
- The higher the chance that we won't be able to deliver on that revenue, the more that capital provider will charge to compensate them for taking a risk.
- For finance to succeed, we must have **enough revenues** so that we can afford to share some of them with a capital provider; our expenses must be **small enough** that we can afford to cover them with money we borrow; and the risk must be **low enough** that the capital provider will not require more revenue than we can provide.

Why is it needed?

- To reach just family lands in the U.S. at the scale needed to create a globally relevant source of mitigation requires ~\$50 billion. Most of that expense will occur long before carbon credits are generated and can be sold.

Why do we need it?

To reach only family lands in the U.S. at the scale needed to create a globally relevant source of mitigation requires ~\$50 billion. Most of that expense will occur long before carbon credits are generated and can be sold.

That is far beyond the capacity and willingness of the federal government or private philanthropy to support.

Revenues and costs in an NCS project

Expenses

- Landowner engagement
- MRV
- Deductions required by standards
- Program administration
- Landowner payments
- Cost of practice implementation
- “Insurance”
- Sales and marketing of credits
- Cost of capital

Revenues

- Credit sales
- Other sales (timber, easements, etc.)
- Philanthropy or grants
- Land sales

Traditional Financing

Expenses

- Find projects where the expenses are relatively low
- Stack several sources of revenue
- De-risk the investment by finding buyers ahead of time to commit to buying a specified volume of credits at a specified price
- Secure the project with the land as collateral

Challenges

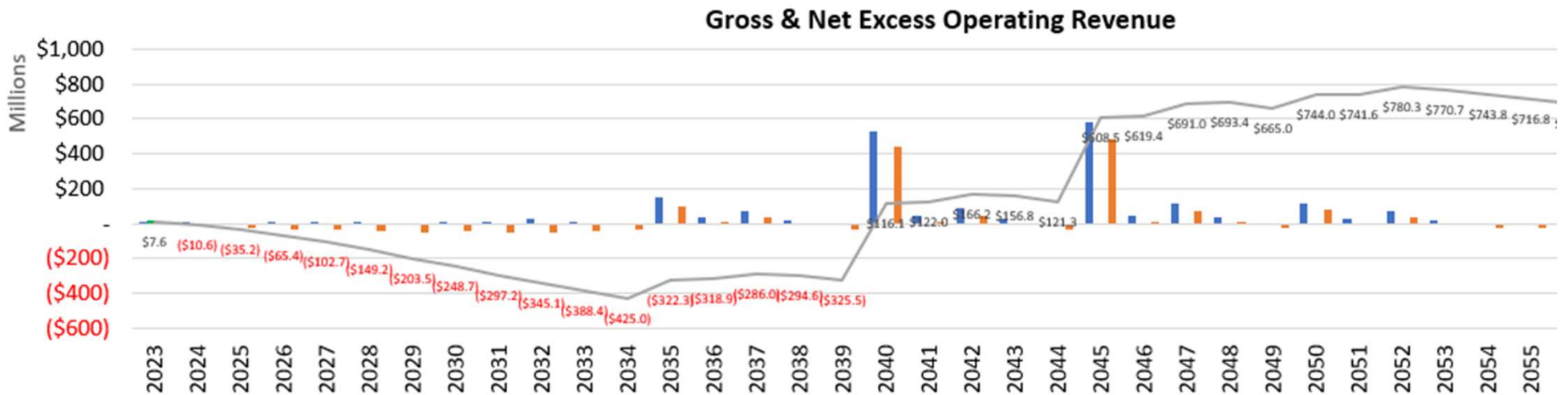
Expenses

- Find projects where the expenses are relatively low – **additionality concerns? Does this get us to scale?**
- Stack several sources of revenue – **majority of land in production globally is owned or managed by smallholders, limiting this strategy**
- De-risk the investment by finding buyers ahead of time to commit to buying a specified volume of credits at a specified price – **how do we square this with true ex post verification?**
- Secure the project with the land as collateral – **again, smallholder issue; equity issues generally**

— The Challenge Before Us

NCS Projects Historically	What NCS Projects must become if they are to matter
Focused on large landowners and industrial operations	Engage all landowners regardless of size
In order to reduce costs, found the lowest barriers to implementation, the “low hanging fruit”	Must adjust mainstream landowner behavior at scale
Utilized questionable baselines to inflate credit yields and / or make them predictable, and / or utilized methodologies that produced credits immediately	Dynamic baselines or more stringent regulations on modeled baselines will mean <i>true</i> ex post verification, and the generation of credits over time. This introduces uncertainty and delays revenue.
Because working with large landowners, had recourse to other revenue streams or the land itself to secure the transaction	Must likely succeed or fail on the carbon values alone
	Must reduce cost of capital to equitably distribute revenue with landowners

FFCP Example



- High upfront costs for landowner recruitment and initial implementation through 2034
- Positive cash flows from that point on, although “breakeven” point takes until 2040 to achieve

Some good news

- Increased demand, increased prices
- Broad agreement among stakeholders on the necessity of the market

Some bad news

- Market uncertainty
- Enhanced rules and regulations (a good thing – but not for this topic)
- Not every credit or project is equal, but they produce the same thing (a credit)
- Negative media environment

Potential Solutions

1. Debt issuances with 3rd party credit enhancement
2. Buyer finance

Key (Controversial) Takeaways

1. We must find someone to own the risk that is inherent in high quality nature based projects.
2. We cannot rely on traditional finance or conservation finance approaches. Every actor in this market is going to need to move beyond their comfort zone.
3. At the heart of issues over quality and equity is this question of finance. We cannot solve those issues without solving this one.