

## Analysts expect few surprises from 2007 data

Verified emissions data for 2007 are unlikely to reveal big changes compared to how much carbon dioxide EU companies emitted in 2006 and 2005, according to carbon market analysts.

The European commission this week announced it will release last year's verified emissions data as soon as 80 per cent of them have been reported to Brussels, which could be as early as 1 April.

The data release will be closely watched by carbon traders, as this is the only firm data for carbon allowance demand released annually.

Although they say the data are unlikely to yield big surprises, analysts will study the data closely to uncover European emissions trends.

"It seems that industrial production in EU ETS sectors has not really increased, and has even decreased in some cases. Electricity production has grown overall but impact on CO2 emissions of the sector is unclear," said Alexandre Marty, managing consultant with ICF International, a consultancy.

Overall, Marty expected the emissions data would show companies emitted close to the same amount of CO2 as they did in the first two years of phase one.

"It is hard to anticipate how EU ETS operators will have reacted to the quasi disappearance of the carbon constraint, given the very low EUA price," Marty said.

Deutsche Bank's Mark Lewis agreed it would be

difficult to accurately predict the 2007 emissions ahead of the official data release, but believed the risk was to the downside. Emissions could be lower than in 2006 as warmer weather in 2007 curbed heating demand, while renewable energy generation continued to increase, Lewis said.

"I would expect emissions to be flat at best and in fact they could well register a decline," he said.

"Over time, however, because the phase two cap is some 9 per cent lower than the phase one cap, and because the cap will fall even more drastically from 2013 onwards, there will be a big demand for carbon credits over both phase two and phase three."

As a result, traders should look at the longer-term EU abatement costs to comply with the cap over 2008-20, rather than solely on annual figures, Lewis argued.

"Too much emphasis is put on this number because we only get one data point per year," Lewis said, urging the European commission to release verified emissions data quarterly.

Meanwhile, Point Carbon estimates the emissions in 2007 were 19 million tonnes higher in 2007 than in 2006, at 2,047 million tonnes, excluding Malta, Cyprus, Bulgaria and Romania.

The un-coordinated release of 2005 data in April 2006 showed the system was over-allocated for the first phase, prompting a price fall, with phase one allowances now virtually worthless.

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### EUA closing prices - historical

EUA prices for December 2008 delivery, as assessed by Point Carbon. Prices are published daily at [www.pointcarbon.com](http://www.pointcarbon.com)



**EUA closing prices, OTC**

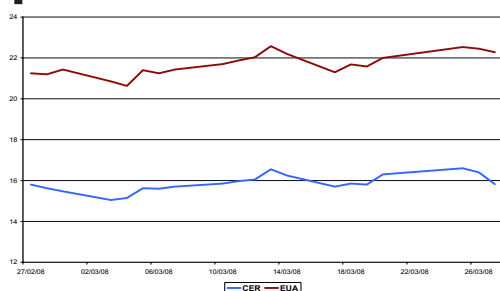
Contract	Bid	Offer	Close	Change
EUA spot	0.01	0.01	0.01	-
EUA 2008	22.28	22.29	22.28	-0.30
EUA 2009	22.85	22.90	22.88	-0.25
EUA 2010	23.45	23.55	23.50	-0.34
EUA 2011	24.20	24.30	24.25	-0.42
EUA 2012	25.25	25.35	25.30	-0.32

**Secondary CER assessment**

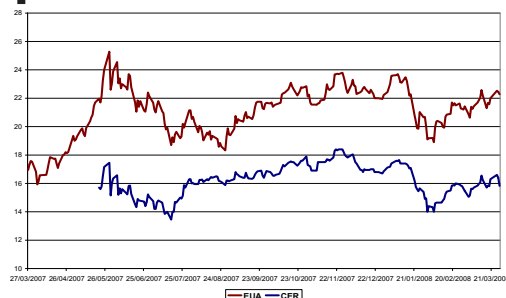
Contract	Low	High
Dec-08	15.80	15.85
Dec-08-12	15.30	15.40

Quoted prices are euros per EUA/CER, at close of market 27 March, as assessed through Point Carbon's bid-offer-close methodology for the over-the-counter (OTC) market. Changes refer to the last issue of CME.

For methodology, see [www.pointcarbon.com](http://www.pointcarbon.com).

**EUA and secondary CER prices (£/t)****Last month****Last 12 months**

For methodology, see [www.pointcarbon.com](http://www.pointcarbon.com)

**Market comment**

The price of European carbon allowances fell over the last two weeks, depressed largely by flagging prices in other energy products such as oil and German power.

The benchmark EUA December 2008 contract finished Thursday's session at €22.28 in the brokered OTC market, down €0.30 from the closing level on 13 March, after having traded in a €1.69 range.

Crude oil futures, which lately have provided direction for carbon allowances, declined over the period. The Brent front month contract closed at \$105/bbl on Thursday, down \$2.54 since 13 March.

German power, another energy product watched closely by carbon traders, also dropped. The 2009 baseload power contract closed at €63.55/MWh, down €0.75 from its closing level on 13 March.

Traders also attributed some of the weakness in carbon to continued strength in coal, although coal prices fell slightly over the two-week period.

"Carbon was always going to struggle because coal was stronger. I saw a bit of fuel-switching today as some utilities bought gas so that dampened demand for EUAs," one trader said earlier this week.

API 2 coal for 2009 delivery closed at \$127.25/tonne on Thursday, down \$3.75. However, the contract is \$23.00 higher than in January.

In the secondary market for certified emission reductions (CERs), prices fell more than EU allowances. The credits for December 2008 delivery were valued at €15.83 on 27 March, down €0.72 from two weeks ago, following the launch of futures contracts for the credits by three exchanges.

"Someone had a lot of selling to do, maybe because they have got issued a lot of credits, and they hid themselves doing it by trading on the exchange," one trader commented.

However, the price of secondary CER credits for delivery this December could still rise due to limited supply in the market, one trader said. "There isn't a huge amount of natural supply," he said.

Around 79 million EU allowances traded across all platforms.

## Three exchanges launch CER contracts

The European Climate Exchange (ECX), the European Energy Exchange (EEX) and Nymex-backed The Green Exchange all launched CER contracts over the last two weeks, with liquidity quick to build up at ECX.

The newest contract on the market is EEX's, which was launched on 25 March. The Green Exchange's became available as that exchange went live on 17 March, while ECX opened for CER trading on 14 March.

Oslo-based Nord Pool has allowed trading in the UN-endorsed offset credits since June last year, but despite Nord Pool's early launch, ECX seems to have attracted most liquidity of the two.

And the early dominance of ECX was not unexpected, according to Louis Redshaw, an emissions trader with Barclays Capital.

"ECX was always going to get the liquidity, because so many companies are signed up to trade and are likely to want to keep their collateral in one place," he said.

The emergence of exchange-traded CER contracts is a boost to the CER market, as they in addition to providing standardisation of contracts allows for transparent price discovery, according to Redshaw.

"It really, really helps. That's one of the benefits of the exchange," he said.

However, the majority of trades are still done in the brokered market, said Imtiaz Ahmad, executive director with investment bank Morgan Stanley, because some exchange contracts specify credit deliveries in specific national registries.

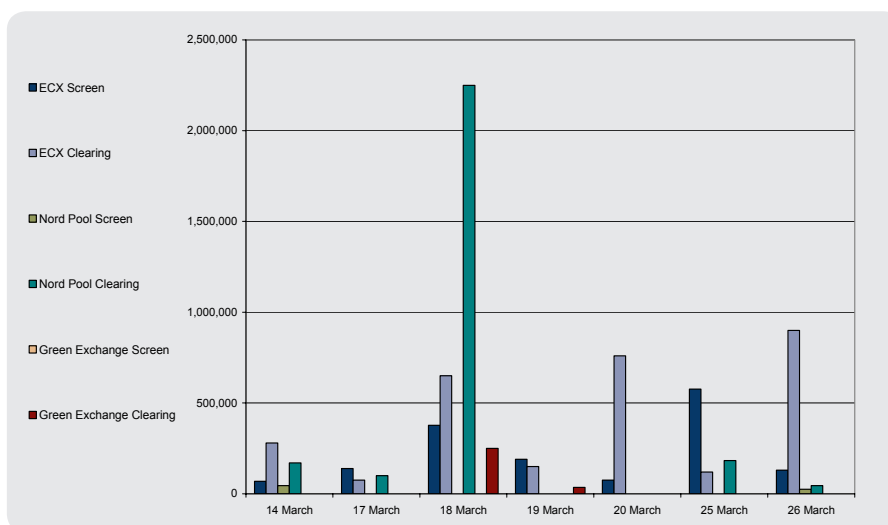
For this reason, he said many continental companies preferred buying CERs for compliance purposes via an OTC contract rather than trading on the ECX, which requires the credits to be delivered into an account in the UK registry.

But this is one of the contract's benefits, Redshaw said, as the majority of CERs will be delivered from the UN into UK accounts.

While few trades have been reported in CERs on The Green Exchange, no credits traded on the first days of CER trading at EEX. The reason was technical problems at two of the market-makers, said Maik Neubauer, chief operating officer at the Leipzig-based exchange.

We are quite convinced that we will see the first trades during the next days," he said.

**CERs on exchanges** The figure below shows daily volumes traded on exchanges and OTC deals cleared on exchanges, from 14 March. Green Exchange had its first trading day on 17 March, and Nord Pool was closed 20 and 25 March. EEX has not handled any trades yet. *Sources: Exchanges.*



## Finland issues phase-two allowances

Finland issued EU allowances for 2008 on Thursday, becoming the third country to do so, according to Finland's energy market authority.

The country followed Denmark and Austria, which issued their allowances in late February, according to a deadline in EU emissions trading legislation.

Finland will issue a total of around 36 million allowances for 2008, taking the total number of allowances available for spot trading to around 90 million.

That is well below the more than 2 billion allowances that should have been issued, with 24 member states still left to put their allowances on the market.

The reason for the delay is partly that some member states are late in meeting formal requirements. Some member states also disagree with a commission plan for issuing allowances before the EU market has been linked to the UN market.

According to an update on a European commission website, the UK, the Czech Republic and Ireland are cleared for issuance, but have not done so yet.

## UK greenhouse gas emissions fall 2% in 2007

UK emissions of six greenhouse gases amounted to an estimated 639.4 million tonnes of carbon dioxide equivalent in 2007, down 2 per cent from the previous year, according to provisional data released by the government.

Net CO<sub>2</sub> emissions also fell by 2 per cent during the same period, to 543.7 million tonnes from 554.5 million tonnes, thanks to fuel switching from coal to natural gas for electricity generation, coupled with lower fossil fuel consumption by households and industry, the Department of Food, Environment and Rural Affairs, said in a statement.

Carbon dioxide, which was reported as total emissions minus total removals of CO<sub>2</sub> from the atmosphere by carbon sinks, accounts for some 85 per cent of UK's greenhouse gas emissions.

The Kyoto protocol calls on the UK to reduce greenhouse gas emissions 12.5 per cent below the 1990 level by the period 2008-12. In 1990, the UK's emissions stood at 776 million tonnes of CO<sub>2</sub> equivalent.

## Sweden to lower CO<sub>2</sub> tax for ETS installations

The Swedish government has proposed to lower a tax on carbon dioxide emitted from installations covered by the EU emissions trading scheme.

Swedish ETS companies could see CO<sub>2</sub> costs cut by SEK230 million (€24 million) if Sweden's parliament and EU bureaucrats approves the tax adjustment.

Swedish industry currently has to pay a SEK605 (€64) CO<sub>2</sub> tax per 1,000 litres of oil consumption, which the government proposes to lower to SEK432 for installations that are covered by the EU's cap-and-trade scheme for carbon dioxide emissions.

The country has previously sought to remove carbon taxes for companies covered by the scheme, but cancelled its plans after meeting resistance from the European commission.

However, as this is just a reduction of the tax, Sweden is confident it will be accepted by Brussels, said Lars Lundholm of the Swedish finance ministry.

The country has asked for the European commission's approval, and hopes to apply the tax adjustment on 1 July this year.

The proposal was sent to parliament last week

## Hungary sees rush of AAU buyers

A number of buyers are queuing up to buy governmental Kyoto carbon credits, known as assigned amount units (AAUs), from Hungary, an environment ministry official told Point Carbon.

"More than a dozen potential buyers have contacted us," the official said. The AAUs can be used by other governments to comply with their targets under the Kyoto protocol, or by private companies in some countries to meet voluntary or mandatory targets on a national level.

The European Bank for Reconstruction and Development (EBRD) told a conference in Budapest Wednesday it has offered the Hungarian government to purchase AAUs for some €5-10 million (\$7.9-15.8 million), according to reports in Hungarian media.

The EBRD and the European Investment Bank administer the Multilateral Carbon Credit Fund (MCCF), a fund purchasing Kyoto credits on behalf of six governments and six private companies. The AAUs from Hungary would be used towards Kyoto

compliance by Ireland and Spain, two of the fund's investors.

The EBRD has offered to buy a number of AAUs from Hungary as a stand-alone deal under Hungary's green investment scheme, but has also offered to tie it to its loans to the country, by softening the terms, according to the official.

"Our decision is still pending, the amount the EBRD has mentioned is not really a large sum," he said. Other potential buyers are prepared to purchase significantly larger amounts of credits. It became known in December that Japan is negotiating a potential 10-million AAU deal with Hungary. The official declined to name the other interested parties.

"We are in an advanced stage of negotiations with Japan and hope to conclude a deal by the end of April," the official said.

Most countries in the central and eastern European region are in a position to sell AAUs during the Kyoto period, as the economic restructuring of the 1990s led to greenhouse gas emission reductions far beyond what is required by them in the Kyoto protocol.

Countries are setting up green investment schemes, which will earmark AAU sale revenue for use in environmentally sound projects. Several countries are about to finalise AAU sales, for example, the Netherlands and Latvia expect to announce such a deal in the coming weeks.

However, pricing remains a key issue in the AAU market as buyers and sellers alike lack a historical reference point. So far, only one AAU transaction has ever taken place – when Slovakia sold 200,000 AAUs to a Japanese trading house in 2002, at an undisclosed price.

Meanwhile, Japan will buy an undisclosed number of carbon credits from Poland in an attempt to help the country meet its target under the Kyoto protocol, a Polish environment ministry official confirmed to Point Carbon on 18 March.

### **Irish power generator to spend €11 billion on renewables and energy efficiency**

Ireland's main electricity generator, Electricity Supply Board, said on Thursday that it would spend €22 billion (\$34.8 billion) on new infrastructure over the next 12 years, with half that figure to be spent on renewables and energy efficiency.

ESB said in a statement that its 'strategic framework to 2020' would aim at halving its carbon dioxide emissions over the 12 years, including a goal to be "carbon net zero" by 2035.

"Fifty per cent of the overall investment package is geared towards investments in our renewable future. €4 billion of this will be directly invested in renewable energy projects and €6.5 billion will be spent facilitating renewables including smart metering and smart networks," the company added.

The Irish generator, which also buys in power from the UK, said it aimed at delivering one-third of its electricity from renewable generation.

"This will include over 1,400 megawatts of wind generation, in addition to wave, tidal and biomass," the state-owned utility said.

Under legislation proposed by the European commission in January, which is subject to approval by the European parliament and council of ministers, Ireland will have to cut greenhouse gas emissions by up to 20 per cent by 2020, compared with 2005.

Ireland will also have to generate 16 per cent of its energy needs from renewable energy, compared with a current level of 2 per cent. The company said that some of the investment would be in facilities outside Ireland.

"With the development of a single British-Irish electricity market by 2020, ESB's international profile will continue to expand. The company will invest in more generation plants and renewables in Britain and further plants in Europe," it said.

### **European auto industry calls for harmonisation of car CO2 taxes**

European CO2-related taxation for cars should be harmonised in order to prevent distorted environmental results influenced by "widely varying schemes" in each country, the European Automobile Manufacturers' Association (ACEA) said on Thursday.

A new survey from the group shows that over the past 15 months, France, Spain, Finland and Ireland introduced some form of CO2 taxation for cars, bringing the total number of EU member states with such a system to 14. And other countries, such as the Netherlands, Denmark and Portugal have made significant changes to their existing schemes, ACEA said.

"CO2 related taxation of cars and of alternative fuels are an important tool in shaping consumer demand towards fuel-efficient cars. Only a harmonised tax scheme, however, will give the necessary clear market signal which will be decisive in achieving the desired cuts in CO2 emissions," Ivan Hodac, head of the ACEA, said in the statement.

"The fragmentation of systems, furthermore, has a distorting effect on the internal market," Hodac said, pointing out that EU finance ministers recently rejected a European commission proposal for a directive on car taxation. "This is a missed opportunity on an essential issue and that, at a time when expectations about massively reducing CO2 emissions are high at the national level."

For instance, ACEA in the statement pointed out that Italy offers a one-off incentive for consumers purchasing a new car. Meanwhile, France and the UK use CO2 emissions systematically for taxing privately owned and company cars.

And while the UK, France and Luxembourg use CO2 emissions as the main factor for car taxation, other countries apply a combination of criteria including car price, engine capacity and CO2 emissions.

"The car industry advocates a linear system, in which tax levels are directly proportionate to the car's CO2 emissions and every gramme of CO2 is taxed the same. Car tax schemes should neither include nor exclude specific technologies and be budget neutral in end-effect," the ACEA statement said.

EU regulators are currently pushing through legislation for improvements in motor technology that would reduce emissions from new cars sold to 130 grammes of CO2 per kilometre (gCO2/km), while other complementary measures would contribute to a further cut in emissions of up to 10 gCO2/km.

The proposed legislation is meant to help the EU meet its overall goal in reducing greenhouse gas emissions by at least 20 per cent below the 1990 level by 2020.

### **Italian industry sets up private carbon fund to buy UN credits**

Four Italian industry groups have set up a €60-million (\$93.4 million) carbon fund to purchase UN offset credits to help them meet targets under the second phase of the EU emissions trading scheme.

Green Initiative Carbon Assets, established in Lugano, Switzerland, comprises power generators Sorgenia

Spa and Iride Group, Italian iron and steel producer Lucchini Group and investment group Equiter, which invests in public infrastructures such as motorways and coal utilities.

The new fund was established in mid-January 2008 and is seeking carbon reduction projects that have "received approval for construction and implementation by the local authorities," Guglielmo Cioni, general manager of the fund told Point Carbon.

The minimum contract size for the fund is 200,000 credits and all projects will be considered, bar forestry projects, which are not allowed to comply with EU targets under the scheme.

"We will also try to avoid projects which may be seen as risky such as large hydro plans," Cioni said.

"We are looking at Brazil, China and India, but we would also like projects in other areas such as Africa and there will be some in joint implementation countries," Cioni told Point Carbon.

So far, the fund has not contracted any emission reduction credits and Cioni did not mention how many credits the fund wanted to buy.

### **Trading Emissions turns in £74 million profit in last six months of 2007**

UK-listed fund Trading Emissions plc on Thursday posted £74 million (\$94 million) post-tax profit in the last six months of 2007 and said it is on target to deliver a portfolio of 66 million tonnes of emission reductions between now and the end of 2012.

In interim results, the company, which pools carbon credits from emission reduction projects in developing countries, said profits were up sharply from £2.94 million in the corresponding period in 2006, as the company delivered a higher volume of carbon credits.

Trading Emissions said its portfolio adjusted for delivery risk now contained 57 million credits, known as certified emissions reductions (CERs) of which 1.9 million had been issued by the UN body that administers the Kyoto protocol's clean development mechanism (CDM) by 26 March.

Of the company's portfolio of 57 million credits, projects registered by the executive board of the CDM are expected to deliver 14.4 million credits, while projects 'validated' or audited by third parties stand at 14.25 million, Trading Emissions said.

**Editorial enquiries**

Håvard Hamnaberg  
hh@pointcarbon.com  
Tel: +47 977 67 143

**Sales enquiries**

Lee Tumelty  
lt@pointcarbon.com  
Tel +47 22 40 53 64  
Fax +47 22 40 53 41

**Other enquiries**

Point Carbon, Norway  
(Head Office)  
P.O. Box 7120 St.Olav, Akersgata 55  
N-0130 Oslo  
Norway  
Tel +47 22 40 53 40  
Fax +47 22 40 53 41  
contact@pointcarbon.com

**Website**

www.pointcarbon.com

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**Offices/Representatives****UK**

Point Carbon, UK  
Second Floor  
102-108 Clerkenwell Road  
London, EC1M 5SA, UK  
Tel +44 (0) 20 7253 7878  
Fax +44 (0) 20 7253 7856  
london@pointcarbon.com

**Ukraine**

Point Carbon, Ukraine  
3 Sportyvna Ploscha  
Entrance IV, 4th floor  
Olymp Business Center  
Kiev, Ukraine 01601  
Phone + 380 44 499 0308  
Fax +380 44 499 0309  
kyiv@pointcarbon.com

**Belgium**

Point Carbon, Brussels  
Avenue Louise 125  
1050 Brussels, Belgium  
Tel +32 2 533 3412  
brussels@pointcarbon.com

**United States**

Point Carbon North America  
900 Second St, NE  
Suite 309  
Washington, DC 20002  
Phone: +1 202 289 3930  
Fax: +1 202 289 3967  
washington@pointcarbon.com

**Japan**

JPower  
Ms. Sumie Nakayama  
Tel +81 3 3546 9375  
Sumie\_Nakayama@jpower.co.jp

Mizuho Information and Research  
Institute, Inc.  
2-3 Kandanshiki-cho  
Chiyoda-ku Tokyo  
101-8443 Japan  
Tel +81 3 5281 5410  
Fax +81 3 5281 5466  
yasushi.setoguchi@  
gene.mizuho-ir.co.jp (Office)  
setoro@attglobal.net (Res.)

**Germany**

Perspectives GmbH  
Sonnenredder 55  
22045 Hamburg, Germany  
Phone: +41 433550073  
Fax: +49 89 14 88 28 08 22  
info@perspectives.cc

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